



April 8, 2008

Distributed via e-mail

To Registered Participants and Interested Parties
AESO 2004-2005 Deferral Account Reconciliation Application

Dear Participant:

**Re: Request for Stakeholder Input on Recognition of Interest
in AESO 2004-2007 Deferral Account Reconciliation Application**

At the February 8 technical meeting and in information requests on the AESO's 2004-2005 deferral account reconciliation application, participants raised the topic of recognition of interest relating to amounts in the AESO's deferral accounts. In preparation for filing the extended 2004-2007 application (as proposed in the March 14 cover letter to the AESO's information responses and subject to approval by the Alberta Utilities Commission (AUC)), the AESO has further considered the matter of interest in light of the unusual circumstances of this application.

This letter describes the manner in which the AESO contemplates treating interest in the deferral account reconciliation in the 2004-2007 application, provides the rationale for that treatment, and seeks input from stakeholders. Stakeholders are invited to discuss the matter at a consultation meeting on Wednesday morning, April 16, in Calgary (as detailed at the end of this letter), and to provide written comments using the attached comment form by Friday, April 18.

The AESO considers it appropriate to account for interest in the extended 2004-2007 deferral account reconciliation application because of the following unusual aspects of the application.

- The application will cover an extended period which includes first reconciliations for 2007, 2006, 2005, and 2004, as well as re-reconciliations or reconciliations of adjustments for years from 1999 to 2003.
- The application has been delayed for the reasons discussed in Appendix A-2 of the original 2004-2005 application.
- The application includes a number of large one-time adjustments, some of which are laid out in Schedule TCE.AESO-002 (b-c) in the AESO's information responses filed on March 18, 2008.

The AESO intends to file future deferral account reconciliation applications on an annual basis, with Rider C managing variances during a year and reconciliation occurring within six months of year end. The AESO does not consider that interest would ordinarily be included in such annual filings. Recognition of interest in the extended 2004-2007 application is therefore considered a one-time, extraordinary approach.

Recognition of interest in the AESO's 2004-2007 deferral account reconciliation will not affect the net deferral account balance being reconciled, since section 14 of the EUA requires that "on an annual basis, no profit or loss results from its [the AESO's] operation." The AESO must therefore be left with a zero balance after deferral account reconciliation, whether or not interest is accounted for. For clarity, the AESO does not earn or incur interest directly on its deferral account balances, but rather deferral account surpluses and shortfalls are managed in conjunction with other financial obligations of the AESO. The AESO carries a certain amount of debt to provide working capital and fund capital purchases, and deferral account balances affect the amount of debt carried. The cost of interest incurred on debt accrues to the AESO's "own costs" which is allocated to AESO customers in accordance with the AESO's approved tariffs.

Recognition of interest will therefore result in amounts being moved between production years and months, between rates and rate components, and between customers. As discussed in Information Responses TCE.AESO-002 (e), -003 (d), and -009 (c), deferral account surpluses reduce debt balances that the AESO would otherwise have been required to carry, and therefore avoid interest expense. Similarly, deferral account shortfalls increase debt balances that the AESO would otherwise have been required to carry, and therefore incur additional interest expense. Recognition of interest in the deferral account reconciliation would involve the following steps:

1. calculate the monthly interest expense or revenue that would have been incurred based solely on the outstanding deferral account balance,
2. adjust interest expense that was actually incurred on a monthly basis to reflect the calculated increase or decrease in interest as calculated in step 1, and
3. credit or charge an equivalent amount to the production periods, rates, and rate components relevant to the deferral account balance which gave rise to the interest expense adjustment..

The increase or decrease in interest expense would be allocated as incurred in a period in the same manner as interconnection charges in the AESO's deferral accounts. The equivalent credit or charge would be allocated in the same manner as the deferral account balance which gave rise to the interest expense adjustment. Amounts will therefore move between production periods, rates and rate components, and customers, although no change in net deferral account balance will occur.

In considering interest in the extended 2004-2007 application, the AESO proposes the following principles to recognize interest.

- (a) **"Normal" deferral account treatment would not attract interest.** The AESO suggests that, if the AESO had utilized Rider C to consistently maintain its forecast deferral account balances at or near zero continuously throughout the deferral account period, no interest should accrue. Maintaining forecast deferral account balances near zero through Rider C would have allocated deferral account balances to customers in accordance with the basis upon which Rider C was developed, and no interest adjustment would be required.

- (b) **Interest will be calculated based on monthly deferral account balances.** If deferral account balances near zero would not attract interest as proposed in point (a), then it follows that interest would be calculated based on those balances which are not maintained near zero. Interest charges would accrue on deferral account shortfalls, and interest credits would accrue on deferral account surpluses, consistent with the deferral account balances by rate and rate component as reported monthly on the AESO's web site.
- (c) **Interest will accrue only after a transaction has been recorded by the AESO.** No interest will accrue on refunds or charges to the AESO prior to those transactions being recorded by the AESO. The AESO considers that interest on amounts before they are charged or refunded to the AESO should be addressed at the time the charge or refund is determined, in accordance with normal practice for assessing interest on such amounts based on the nature of the transaction. For example, if a transaction results from a decision of the Alberta Utilities Commission (AUC), the AESO expect that interest on the transaction prior to it being charged or refunded to the AESO would be determined as part of the AUC decision.
- (d) **Interest will be calculated using the Bank of Canada's Bank Rate plus 1½%.** Interest will be calculated on a monthly basis using a rate equal to the Bank of Canada's Bank Rate plus 1½%, in accordance with section 3(2)(e) of AUC Rule 023 respecting payment of interest.
- (e) **No interest will accrue in respect of transactions recorded in 2007 or 2008.** The AESO considers that filing a reconciliation of 2007 deferral accounts in May of 2008 represents normal timing for an annual deferral account reconciliation. Therefore, no interest would accrue with respect to transactions which would appear for the first time in a 2007 deferral account reconciliation. This is consistent with section 3(2)(b) of AUC Rule 023 which suggests no interest would accrue unless regulatory lag occurs, and a normal application process does not constitute regulatory lag. However, any deferral account balance which existed at the end of December 2006 would continue to accrue interest, in as much as that balance continued to exist after 2006.
- (f) **Interest will be calculated to the expected date of settlement with customers in June 2008.** In the March 14 cover letter to its information responses, the AESO indicated it would apply to settle amounts with customers immediately upon filing the extended 2004-2007 application. That application will be filed in May, and, pending AUC approval of the AESO's proposal, financial settlement of the deferral account balances with customers will occur at the end of June 2008. The AESO therefore proposes to calculate interest on deferral account balances arising from transactions that occurred prior to 2007, up to the end of June 2008.
- (g) **Interest will be allocated in the same manner as the deferral account balances on which the interest is calculated.** Interest amounts will therefore be charged or refunded to customers by production month and by rate and rate component, consistent with the manner in which the deferral account balances were charged or refunded to customers.

In accordance with the above principles, the AESO has calculated the following preliminary estimate of interest amounts to be included in the extended 2004-2007 deferral account reconciliation application:

| Production Year | Refund (Charge) (\$ 000 000) | | |
|--------------------|------------------------------|----------------|--------------|
| | STS | DTS | Net |
| 2002 | \$2.3 | \$0.0 | \$2.3 |
| 2003 | 2.6 | (1.0) | 1.7 |
| 2004 | (1.4) | 1.3 | (0.1) |
| 2005 | (0.7) | (0.6) | (1.3) |
| 2006 | 0.0 | (1.9) | (1.9) |
| 2007 | 0.0 | (0.5) | (0.5) |
| 2008 | 0.0 | (0.2) | (0.2) |
| Total | \$2.9 | (\$2.9) | \$0.0 |

As stated in the opening to this letter, the AESO would like to receive input from participants and stakeholders on the matter of recognition of interest in the extended 2004-2007 deferral account reconciliation application. Interest treatment must be finalized relatively quickly to allow the AESO to prepare the extended application for filing in May. The AESO therefore invites stakeholders to a consultation meeting as follows:

Time: 9:30 to 11:30 AM
 Date: Wednesday, April 16, 2008
 Location: 25th Floor, AESO Office, 330 – 5th Avenue SW, Calgary
 Refreshments: Coffee, juice, fruit, and pastries will be provided
 Registration: **Please register your attendance at this meeting with April Walters by e-mail to april.walters@aeso.ca or by phone to (403) 539-2463, by 5:00 PM on Friday, April 11, 2008, to ensure space is available**

Information for presentation and discussion at the consultation meeting is currently being prepared and will be provided on the AESO web site as soon as possible. The information, this request for stakeholder input, and other related material will be posted on the AESO's web site at www.aeso.ca, and may be found after posting by following the path Tariff ► Current Applications ► 2004-2007 Deferral Account Reconciliation.

The AESO also invites stakeholder to provide written comments after the consultation meeting using the attached comment form. Please provide comments by returning the attached comment form to john.martin@aeso.ca by **Friday, April 18, 2008**. The AESO will post all comments received on its web site, and will consider the comments when finalizing the extended 2004-2007 deferral account reconciliation application.

The AESO's original 2004-2005 Deferral Account Reconciliation Application and related information is posted on the AESO's web site at www.aeso.ca, and may be found by following the path Tariff ► Current Applications ► 2004-2005 Deferral Account Reconciliation.

If you have any questions on the AESO's deferral account reconciliation application, please contact me at (403) 539-2465 or by e-mail to john.martin@aesoc.ca.

Yours truly,

[original signed by]

John Martin
Director, Tariff Applications

Attachment

cc: Jamie Cameron, Alberta Utilities Commission
Heidi Kirrmaier, Vice-President, Regulatory, AESO
Carol Moline, Director, Accounting & Treasury, AESO