

### 3 COMMON TRANSMISSION AND DISTRIBUTION ISSUES

#### 3.1 2009 Plant and Other Assets Opening Balances

25. During the course of the oral hearing, AE indicated its intention to update the opening balances for plant and other assets for 2009 to reflect the 2008 actual closing balances:

Q. During the break, there was -- just to point out one further question in relation to the capital, and now that you have the actual opening and closing balances for 2008, is it ATCO's intention to reflect the closing balances for 2008 in the opening balances for 2009 at the time of the refiling?

A. That's correct.<sup>15</sup>

#### Commission Findings

26. Both the Consumer Group (CG) and the UCA recommended that AE's 2008 actuals be adopted as the starting point for AE's 2009 test year. There appears to be agreement among parties that the 2008 actual closing balances should be reflected in the 2009 opening balances. The Commission considers this to be a prudent course of action and directs AE in its compliance filing to update its 2009 opening balances to reflect the 2008 actual closing balances for plant and other assets, except for the amounts related to the Additional Deductions.<sup>16</sup> AE is directed to identify the Additional Deductions separately and to treat these amounts as placeholders for the compliance filing.

#### 3.2 Management Fee

27. In its Application, AE noted that the current regulatory treatment of existing and forecast levels of contributions in aid of construction (CIAC) prevents AE from earning a fair and reasonable return on assets that are used and useful in the provision of service to customers. Specifically, AE submitted that it retains the full responsibility to own, operate and maintain assets financed by CIAC but does not receive any compensation for the performance of these functions.<sup>17</sup> AE engaged an expert witness, Dr. Charles Cicchetti of Pacific Economics Group, to assist in developing its position on these matters. AE proposed the following management fees and corresponding "notional equity percentages" for 2009 and 2010:<sup>18</sup>

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<sup>15</sup> Transcript Volume 4, page 493, starting at line 22

<sup>16</sup> Additional Deductions refers to income tax deductions for easements costs, stock handling costs, and removal and abandonment costs. For further information refer to Section 6.2 of this Decision

<sup>17</sup> AE Application, Section 31, Attachment 1, page 3

<sup>18</sup> AE Updates Rebuttal, Schedule 1, page 1 and 2, and AE Rebuttal Evidence, page 248

Table 4. Summary of AE Management Fee Amounts and Notional Equity Percentage

	Test Year (\$ Million)	
	2009	2010
Transmission Management Fee		
Percent for Amortized Payment	6.83%	6.83%
Amortized Payment Amount	2.3	3.1
Distribution Management Fee		
Percent for Amortized Payment	6.46%	6.46%
Amortized Payment Amount	8.5	10.0
Total Transmission and Distribution Management Fee	10.8	13.1

28. CG engaged an expert witness, Mr. William Marcus of JBS Energy, to evaluate AE's proposal to collect management fees. The UCA, CG, Industrial Power Consumers Association of Alberta (IPCAA), TransCanada Keystone Pipeline GP Ltd. (Keystone) and First Nations did not support AE's proposal to collect the management fee and argued that the management fee:

- was contrary to the EUA;
- should be dealt with in the next AESO GTA;
- contributed to rate shock and added unnecessary costs to customers;
- was excessive;
- would compensate for risks twice;
- defeated the purpose of CIAC;
- violated the concept of prospective regulation; and
- should be replaced with Keystone's AESO Rider I proposal.

29. AE maintained that a management fee was necessary because:

- AE does not receive any compensation for the ownership, operation and maintenance of the assets financed by CIAC and the assumption of risks associated with these assets;
- section 122(1)(h) of the EUA clearly provides the Commission the authority to grant the requested relief; and
- the level of CIAC diminishes its approved level of return (currently 8.75 percent) by some 57 basis points to an effective return of 8.18 percent.

30. AE submitted that it should be treated as having separate Transmission and Distribution entities and argued that its management fee proposal with respect to CIAC had been fully justified and that it should be approved for inclusion in revenue requirement for the test years.

### Commission Findings

31. The Commission notes that the Chair in this proceeding questioned Dr. Cicchetti with respect to the services that would be provided in return for the management fee.<sup>19</sup> In reviewing the response of Dr. Cicchetti, the Commission considers that it is unclear what services were to be provided. In addition, AE submitted that its request for a management fee was grounded in the fact that it retains the full responsibility to own, operate and maintain assets financed by

<sup>19</sup> Transcript Volume 5, page 679, line 12 to page 680, line 5

CIAC but does not receive any compensation for the performance of these functions. However, the Commission notes the evidence of Mr. Marcus:

What is actually being “managed” for contributed property is O&M expense. These expenses and the cost of managing these expenses are included in rates, and the increase in contributions has not resulted in a significant increase in ATCO’s business risk.<sup>20</sup>

32. As noted by Mr. Marcus the costs of managing the contributions are included in rates today.<sup>21</sup> Dr. Cicchetti also acknowledged that there was no cost basis for the management fee.<sup>22</sup>

33. Prior to approving any new fees, charges, or costs such as a management fee, the Commission must be satisfied that the charge is just and reasonable. AE has not convinced the Commission that the management fee is just and reasonable. The evidence is not clear or compelling as to what specific services are being rendered in return for the management fee, for which compensation is not presently provided.

34. The Commission has also considered the arguments in relation to what percentage level of CIAC causes a problem for a utility. The Commission notes that while Mr. Marcus contended that CIAC was not a problem, he acknowledged during the hearing that:

If 100 percent of a utility's assets were financed by contributions, you would probably need to look at some other mechanism for providing a fair return, such as, for example, a return margin.<sup>23</sup>

and

I think my answer is pretty much the same as 75. You'd have to look at it, but when you start getting numbers closer to 50 percent, you start getting returns that are a viable business, and you may start thinking about some other issues to make sure that you've got a viable business there....

But as the number comes down, you can start looking at the business as a whole. You know, whereas if the number is 100 percent or 75, you've probably got to make sure that you provide a viable business.<sup>24</sup>

35. Thus to Mr. Marcus, it appears that CIAC could become a problem if it reaches a level somewhere between 50 percent and 100 percent of the total investment in utility property. In contrast, Dr. Cicchetti considered that at the 10 percent level, CIAC was a problem,<sup>25</sup> and at this level, return on equity is probably off by somewhere between 50 and 75 basis points.<sup>26</sup> The Commission notes that there is a wide variance between the percentage levels and no definitive point at which the experts concluded that CIAC needs to be addressed. In view of the variance in the experts’ opinions it is not clear to the Commission that the current level of CIAC justifies the implementation of a management fee.

<sup>20</sup> CG Evidence of Mr. Wm. Marcus, page 3

<sup>21</sup> CG Evidence of Mr. Wm. Marcus, page 10

<sup>22</sup> Transcript Volume 5, page 681, lines 3-4

<sup>23</sup> Transcript Volume 6, page 871, lines 21-24

<sup>24</sup> Transcript Volume 6, page 873, lines 3-12

<sup>25</sup> UCA-AE-81(a)

<sup>26</sup> Transcript Volume 5, page 626, lines 8-15

36. For the above reasons, the Commission considers that it should not approve the management fee. Accordingly, the Commission denies AE's requested management fee for the current test years.

37. Following the close of the evidentiary portion of this proceeding, a panel of the Commission heard AltaLink Management Ltd.'s (AltaLink) 2009-2010 General Tariff Application (Proceeding 102). In Proceeding 102 the concept of a management fee was raised and discussed as was Keystone's Rider I proposal addressing this concept.. Following the close of evidence in Proceeding 102, the impact of Rider I on the business risk of a utility was also examined in the 2009 Generic Cost of Capital proceeding.<sup>27</sup> Given that the management fee concept has been raised in both this proceeding and Proceeding 102, and the Rider I proposal has been raised in all three proceedings, the Commission is concerned that an approach for dealing with this concept on a global basis has not been available. The Commission considers that compensation for the ownership, operation and maintenance of assets financed by CIAC should be addressed comprehensively, rather than in individual utilities' tariff applications, or in the Generic Cost of Capital proceeding.

38. The Commission finds that consideration and evaluation of CIAC and related compensation to the utility could be more efficiently and effectively addressed going forward at a generic proceeding, which would allow for a more detailed review of all relevant issues at one time and by all potentially affected parties. The Commission will advise all parties in the near future as to the process that will be established.

### 3.3 Inflation

39. In the Application, AE proposed different inflation rates for the following categories: Labour, Other and Contractors. The inflation rates for each of these categories are summarized below. For ease of reference, the corresponding recommendations made by each of CG and the UCA are also shown.

Table 5. Summary of Inflation Recommendations

	AE				CG		UCA <sup>28</sup>	
	Original		Revised		2009	2010	2009	2010
	2009	2010	2009	2010				
Labour	6.0	6.9	6.0	6.9	3.5% non CEWA, 5.75% CEWA <sup>29</sup>	3	3.5	3
Other	5	5	3	3	0.7		3	2.5
Contractor and Capital	10	10	5	5	4.7	≤3	5	4.5

40. The following table sets out the Commission's findings for each of the inflation categories. The positions of the parties and the Commission's findings for each of these inflation categories are in the subsections that follow.

<sup>27</sup> 2009 Generic Cost of Capital proceeding EPS ID 85 – Transcript Volume 11, starting at page 1858

<sup>28</sup> UCA Argument, page 11

<sup>29</sup> The Commission's summary of CG's recommendation is based on the following "...the wage increases for 2009 and 2010 should be established at 3.5% for 2009 ...with one exception. Since the agreement with CEWA is already in place for 2009, the wage increases (5.25% plus 0.5% step increases) resulting from that agreement should be allowed for 2009."