



Alberta Electric System Operator

2009 Deferral Account Reconciliation

February 10, 2011



The Alberta Utilities Commission
Decision 2011-049: Alberta Electric System Operator
2009 Deferral Account Reconciliation
Application No. 1606095
Proceeding ID No. 589

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1 Background

1. The Alberta Electric System Operator (AESO) filed an application (application) with the Alberta Utilities Commission (the AUC or the Commission) on April 15, 2010, to reconcile its deferral accounts for the period ending December 31, 2009.
2. In the application, the AESO requested that the Commission:
 - (a) approve deferral account balance reconciliation calculations for the period January 1 to December 31, 2009 as described in Section 3 of the application
 - (b) approve deferral account balance reconciliation calculations for the period January 1 to December 31, 2008 as described in Section 4 of the application
 - (c) approve deferral account balance reconciliation calculations for the period January 1 to December 31, 2007 as described in Section 5 of the application
 - (d) approve deferral account balance reconciliation calculations for the period January 1 to December 31, 2006 as described in Section 6 of the application
 - (e) approve deferral account balance reconciliation calculations for the period January 1 to December 31, 2005 as described in Section 7 of the application
 - (f) approve deferral account balance reconciliation calculations for the period January 1 to December 31, 2004 as described in Section 8 of the application
 - (g) approve the customer allocation methodology as presented in Section 9 and Appendices G through K of the application, for purposes of recovering and refunding outstanding variance amounts from and to the AESO's DTS, FTS, and STS rate classes
 - (h) approve the collection and refund of customer amounts through the use of a one-time payment/collection option described in Section 10 of the application
 - (i) approve the collection and refund of customer amounts included in the application on an interim refundable basis, with such amounts subject to adjustment in final approvals as described in Section 11 of the application
 - (j) approve an AESO proposal to provide compliance reviews of second and later deferral accounts to be included in the AESO's 2010, deferral account reconciliation application, and to financially settle with customers as soon as practical after the compliance review is filed

- (k) confirm its acceptance of the AESO's responses to outstanding directions provided in Section 11 of the application
- (l) provide such further and other relief as the Commission may prescribe

3. The AESO stated that the application incorporated all costs paid and revenues collected by the AESO that:

- have not been settled in prior deferral account reconciliation filings
- relate to 2009 or prior years for all costs except those related to losses
- were accounted for up to December 31, 2009

4. The application included a request for approval of the immediate interim settlement of deferral account amounts included in the application. The AESO noted that its proposed settlement with customers would be interim and refundable, and subject to adjustment in the Commission's final decision in respect of the application.

5. Notice of the application (notice) was issued by the Commission on April 15, 2010. In the notice, the Commission took note of the AESO's request for approval of an immediate interim settlement with customers, and requested that they include comments in their statements of intent to participate (SIPs) either supporting or opposing the AESO's request for immediate interim settlement. SIPs were filed in response to the notice by FortisAlberta Inc., the Industrial Power Consumers Association of Alberta, the Office of the Utilities Consumer Advocate (UCA), TransAlta Corporation and TransCanada Energy Ltd.

6. In accordance with Commission correspondence dated May 4, 2010, a technical meeting in respect of the application was held at the offices of the AESO on May 12, 2010.

7. On May 13, 2010, the Commission issued Decision 2010-209.¹ In that decision, the Commission approved the AESO's request for an interim settlement of deferral account balances set out in the application. Decision 2010-209 also directed the AESO to notify the Commission when the interim settlement was completed.

8. On May 14, 2010, following the release of Decision 2010-209, the Commission set out an initial process and schedule for considering the application as follows:

Process schedule	Deadline
Information requests to the AESO	June 1, 2010
Information responses from the AESO	June 15, 2010
Submissions on need for intervener evidence	June 18, 2010

9. The Commission received correspondence from the AESO dated June 10, 2010, in which the AESO requested that certain information (hereinafter "the Confidential Information") requested by IPCAA in an information request be kept confidential when filed, pursuant to

¹ Decision 2010-209: Alberta Electric System Operator 2009 Deferral Account Reconciliation – Interim Settlement, Application No. 1606095, Proceeding ID. 589, May 13, 2010.

Section 13 of AUC Rule 001 . The information requests pertained to AESO expenditures on the conversion of four unit transformers at the Genesee generating station (the KEG project), which was previously approved in Decision 2008-101.²

10. The Commission responded to the AESO's confidentiality motion in correspondence dated June 14, 2010. As the information for which the AESO sought confidential treatment pertained to a report prepared by Revay and Associates Limited (Revay Report, Cost Review Report, or CRR) about facilities built on behalf of Capital Power Corporation (CPC or EPCOR),³ the Commission's June 14, 2010, correspondence sought, as an initial matter, to confirm that CPC was aware of IPCAA's request for access to the information for which the AESO was seeking confidential treatment. To this end, the Commission directed the AESO to forward the Commission's June 14, 2010, correspondence to CPC so the company could comment on the AESO's motion for confidential treatment of the confidential information. A schedule for the consideration for the AESO's confidentiality motion described in the Commission's June 14, 2010, correspondence was set out as follows:

Process schedule	Deadline
Additional information from the AESO	June 18, 2010
Comments on motion from interested parties	June 25, 2010
Reply comments, if any, from the AESO and Capital Power Corporation	July 5, 2010

11. On June 18, 2010, the AESO filed correspondence which indicated that:

- CPC was aware of the information request of IPCAA
- CPC supported the request for confidentiality set out in the AESO's June 10, 2010, letter
- the AESO had forwarded a copy of the Commission's June 14, 2010, letter to CPC

12. A SIP for proceeding 589 was received from CPC on June 18, 2010. On the same date, CPC filed a submission on the AESO's confidentiality motion.

13. On June 25, 2010, TransAlta filed a letter in support of the AESO's June 10, 2010, confidentiality motion. A late filed submission on the AESO confidentiality motion was received from IPCAA on June 28, 2010, in which IPCAA expressed conditional support for a proposal by CPC to release a redacted version of the CRR containing the confidential information.

14. The AESO filed reply comments in respect of its confidentiality motion on July 5, 2010. On July 6, 2010, the AESO completed its filing of responses to information requests, including the filing of a redacted version of the CRR.

15. By correspondence dated July 7, 2010, the AESO advised the Commission that it had reflected customer deferral account amounts in an interim financial settlement process that occurred in June 2010, as follows:

² AESO Recovery of Costs for Keephills-Ellerslie-Genesee Conversion of Unit Transformers, Application No. 1568182, Proceeding ID. 28, October 21, 2008.

³ The original agreement with the AESO dated February 28, 2008, was with EPCOR Power Development Limited Partnership, later known as Capital Power Corporation.

- deferral account amounts were included with preliminary billing information distributed to customers on June 8, 2010
- deferral account amounts were also included on final statements issued to customers on June 21, 2010
- amounts were financially settled with customers on June 28, 2010

16. The AESO also noted that some accounts, representing less than \$10,000 of the \$1.8 million settled with market participants, were not yet complete, but would be settled through manual processes in accordance with AESO practices for such cases.

17. Also on July 7, 2010, the Commission issued correspondence requesting that IPCAA advise by July 13, 2010, as to whether it continued to require an unredacted version of the CRR. In late filed correspondence dated July 15, 2010, IPCAA indicated that following its review of the CRR, it had determined that the redacted version did not contain sufficient information to allay its concerns.

18. The Commission issued a ruling on the AESO June 14, 2010, confidentiality motion on July 26, 2010. In the same correspondence, the Commission requested that parties signify by July 30, 2010, as to whether they intended to file intervener evidence.

19. The Commission received correspondence from IPCAA on July 30, 2010, in which IPCAA requested, among other things, that the Commission:

- receive and review an unredacted version of the CRR
- assess whether any redacted portions of the CRR should not be treated as confidential, and thus be provided to interveners for further review

20. On August 3, 2010, the UCA filed correspondence indicating that the UCA did not intend to file intervener evidence. No other parties made submissions on this question.

21. On August 5, 2010, the Commission issued correspondence in response to the July 30, 2010, correspondence of IPCAA. The Commission's correspondence indicated that, in consideration of the relief requested by IPCAA, the Commission was treating IPCAA's July 30, 2010, submission as a motion filed under Section 9 of the Commission's Rule 001: *Rules of Practice*. The Commission sought comments from interested parties as to whether all or some of the grounds for relief requested by IPCAA should be granted. Interested parties were also asked to identify potential impacts, if any, on the remaining process for Proceeding ID 589 in the event that the Commission decided to grant all or part of IPCAA's requests. The Commission set out the following schedule for submissions:

Process schedule	Deadline
Comments on IPCAA submission from AESO and interested parties	August 16, 2010
Reply comments, if any, from IPCAA	August 23, 2010

22. The AESO filed its submission pursuant to the above on August 16, 2010. IPCAA filed a response to the AESO's submission on August 27, 2010.

23. On September 9, 2010, the Commission issued its ruling in respect of the relief requested by IPCAA in its July 30, 2010 correspondence. In that ruling, the Commission directed the AESO and CPC to file one paper copy of the unredacted version of the CRR on a confidential basis, by September 15, 2010, so that the Commission could assess whether the redacted portions of the CRR should continue to receive confidential treatment. The Commission also indicated that, if it determined that the redacted portions of the CRR should remain confidential, the Commission would consider initiating a process whereby IPCAA would be permitted access to the unredacted CRR upon execution and delivery of a confidentiality undertaking.

24. In addition to ruling on the confidential treatment of the CRR, the Commission's September 9, 2010 ruling also ruled on other matters for which IPCAA sought relief in its July 30, 2010 letter. The Commission denied IPCAA's requested relief for most of these matters, but ruled in respect of certain of these items that IPCAA's concerns could be pursued by way of supplemental information requests to the AESO in accordance with the following schedule:

Process schedule	Deadline
Second round of IRs	September 15, 2010
Second round of IR responses	September 29, 2010

25. IPCAA filed a second round of information requests on September 15, 2010, and the AESO filed responses to these information requests on September 29, 2010.

26. Following its review of a confidential and unredacted version of the CRR filed with the Commission on September 15, 2010, the Commission found in a ruling dated September 24, 2010, that an unredacted version of the CRR should be made available to certain named representatives of IPCAA on a strictly confidential basis subject to IPCAA's compliance with procedures for the confidential handling the unredacted CRR report set out in the ruling.

27. Upon the Commission's receipt of confidentiality undertakings signed by IPCAA's counsel and one other IPCAA representative, a paper copy of the unredacted CRR was provided to IPCAA on October 8, 2010.

28. The Commission set out a final schedule for argument and reply argument in correspondence dated October 19, 2010. In that correspondence, the Commission set out specific procedures to apply in the event that argument and/or reply argument filed by the AESO or IPCAA referred to confidential information from the CRR.

29. Written argument was filed by the AESO, the UCA, TCE, and IPCAA on November 5, 2010. Reply argument was filed by the AESO, the UCA, and IPCAA on November 12, 2010. As the argument submission of IPCAA referred to both publicly available unredacted information and confidential redacted information from the CRR report, a complete version of IPCAA's November 5, 2010, argument which referenced confidential information was made available only to the Commission and the AESO.

30. The Commission considers the close of record for the application to be November 12, 2010.

2 Methodology and cost/revenue data included in the application

31. In Section 2 of the application, the AESO noted that the reconciliation processes used for the preparation of the application reflected prior Commission decisions, and conclusions arising from extensive stakeholder consultations related to the AESO's prior deferral account reconciliation application. The AESO also noted that it continued to use a software program to automate deferral account reconciliation calculations and that the reconciliation processes used for the application were the same as used for the AESO's 2008 deferral account reconciliation application.

32. In Section 2.1 of the application, the AESO noted that, in addition to amounts settled in prior deferral account reconciliations for 2004 through 2008, the application incorporated all costs paid and revenues collected by the AESO that:

- have not been settled in prior AESO deferral account reconciliations
- relate to 2009 or prior years for all costs except costs related to losses
- were accounted for up to December 31, 2009

33. More specifically, the AESO provided details on the inclusion of cost and revenue data and data start and cutoff dates for:

- the first reconciliation of deferral accounts for 2009
- a second reconciliation of deferral accounts for 2008
- third reconciliations of deferral accounts for 2007, 2006, 2005, and 2004

34. The AESO highlighted significant prior period adjustments in Section 2.1.1 of the application and provided additional detail on the treatment of transmission system losses in Section 2.1.2. In Section 2.1.3, the AESO noted that any adjustments to 2009 or prior years which occurred after December 31, 2009, were not included in the application and would instead be included in a future deferral account reconciliation application.

35. The AESO discussed its general use and presentation of data on a "production month" rather than an "accounting month" basis in Section 2.2 of the application. For the years 2004 to 2009, the AESO noted that all costs were presented on a production month basis, with the exception of AESO "own cost" and Rider C amounts, which were presented on an accounting month basis. The AESO summarized its use of production or accounting based presentations of data for each year from 2004 to 2009 in Table 2-1 of the application.

Commission findings

36. The Commission notes that the AESO has generally used methodology and data assumptions consistent with the methodology and assumptions used for the 2008 reconciliation as approved in Decision 2009-191.⁴ The Commission approves the methodology and data assumptions described in Section 2 of the application as filed.

⁴ Decision 2009-191: Alberta Electric System Operator 2008 Deferral Account Reconciliation, Application No. 1604964, Proceeding ID. 186, October 29, 2009.

3 Cost and revenue variances and deferral account balances

37. The AESO identified a net surplus of approximately \$1.8 million (net of Rider C charges and refunds and any prior deferral account reconciliation settlements) to be allocated to customers, comprised of the following annual amounts:

- a surplus of \$2.0 million for 2009
- a shortfall of \$4.8 million for 2008
- a surplus of \$3.4 million for 2007
- a surplus of \$1.5 million for 2006
- a shortfall of \$0.1 million for 2005
- a shortfall of \$0.3 million for 2004

38. The AESO set out its 2009 financial results in Section 3 of the application, and cost variances from the AESO's approved revenue requirement for 2009 in Section 3.1. As presented in Table 3-1 of the application, the AESO noted that it recorded total costs for 2009 of \$133.4 million, or 56.7 per cent less than the total 2009 approved revenue requirement. The AESO provided explanations for specific line item variances shown in Table 3-1 unless the variances were either less than $\pm\$0.6$ million or less than ± 10 per cent (except where a variance was $\pm\$6.0$ million or greater).

39. The AESO described its processes for additional reconciliations of deferral account balances for 2008 (second reconciliation) 2007 (third reconciliation), 2006 (third reconciliation), 2005 (third reconciliation) and 2004 (third reconciliation) in Sections 4, 5, 6, 7 and 8 of the application respectively. The AESO provided additional explanations for line item variances exceeding specific thresholds set for each year.⁵

40. In argument, the AESO submitted that no information requests raised concerns with the accuracy of the revenue, cost, and adjustment amounts presented in the application, the periods for which data were included, or the attribution of costs, revenues and adjustments to production months and years.

41. The AESO noted that, as explained in Section 2.4 of the application, the application and related proceeding represented the proper venue for the consideration of the prudence of AESO costs incurred with respect to 2009. In addition, where significant adjustments to 2008 or prior year costs were included in the deferral account reconciliation, the application and related proceeding also represented the proper venue for consideration of the prudence of those adjustments.

42. The AESO submitted that, while additional information about forecast and actual costs and resulting variances for black start services contracted by the AESO was sought in a TCE information request, the AESO's response revealed no errors or imprudence with respect to black start costs.

⁵ For 2008, explanations were provided if a variance exceeded $\pm\$2.5$ million, or if smaller, if variances were at least $\pm\$0.25$ million and at least $\pm 5\%$ of the first reconciliation amount. For 2007, explanations were provided if the variance exceeded $\pm\$1.3$ million, or if smaller, if variances were at least $\pm\$0.13$ million and at least $\pm 3\%$ of the second reconciliation amount. For 2006, 2005, and 2004, explanations were provided if the variance exceeded $\pm\$1.0$ million, or if smaller, if variances were at least $\pm\$0.1$ million and at least $\pm 3\%$ of the second reconciliation amount.

43. The AESO noted that, while information requests from IPCAA had asked for additional information on the KEG project, the information provided by the AESO on this project had revealed no errors with respect to those costs. As such, the AESO submitted that no adjustments were required as a result of the additional information provided.

44. IPCAA provided extensive submissions in argument and reply in respect of the prudence of expenditures on the KEG project. In light of concerns described therein, IPCAA submitted that the Commission should apply a disallowance of at least 50 per cent of \$1 million in respect of that project. In addition to recommending a disallowance, IPCAA also argued that rather than recovering the entire amount of KEG project expenditures as a 2008 cost, this cost should be recovered over a much longer period reflecting the expected life of the assets. IPCAA's request was supported by TCE in reply.

45. The UCA expressed concern in argument that the AESO may not be accurately interpreting Commission decisions, with the result that certain cost adjustments arising from those decisions have not been applied to the correct year or years. Specifically, the UCA submitted that, while a refund of future income taxes ordered in Decision 2007-104⁶ related to ATCO Electric's 2007-2008 tariff application and not any prior year, the AESO determined that Decision 2007-104 resulted in adjustments to ATCO Electric's TFO tariff for the years 2003 through 2007.

46. In reply, the AESO provided extensive responses to IPCAA's concerns about the reasonableness of the KEG project expenditures, and also responded to the suggestions of IPCAA and TCE that the KEG project expenditures should be recovered over several years.

47. The AESO did not agree with the UCA's suggestion that its allocation of a \$16.1 million refund from ATCO Electric in compliance with a direction to transition to a flow through tax method was incorrect. The AESO noted that it had attempted to identify variances arising from Commission decisions in reasonable detail, including the attribution of amounts to specific years. The AESO further submitted that if it had misattributed amounts arising from Decision 2007-104, the AESO expected that the Commission or its predecessor would have issued directions to correct the AESO's misinterpretation. However, having received no such directions in recent deferral account reconciliation decisions, the AESO concluded that it had correctly interpreted and applied the relevant Commission decisions.

Commission findings

48. The Commission notes that IPCAA's request for a disallowance of KEG project costs in the amount of \$500,000 would impact 2008 production year balances. As set out in Section 4.10 below, the Commission has rejected IPCAA's recommendation.

49. As further discussed in Section 4.11 below, the Commission has also rejected the suggestion of IPCAA and TCE that the KEG project costs should be recovered over a long period reflective of the life of KEG project assets.

50. With respect to the debate between the AESO and the UCA as to whether an ATCO Electric refund addressed in Decision 2007-104 should have been applied to prior years or as an

⁶ Decision 2007-104: ATCO Electric Ltd. 2007-2008 General Tariff Application – Refiling, Application No. 1544572, December 21, 2007.

adjustment to ATCO Electric's 2007-2008 TFO tariff, the Commission notes the following comments from the AESO's reply:

The refund from ATCO Electric to the AESO included a year-by-year calculation of the future income taxes that had been collected by ATCO Electric as part of its transmission facility owner tariff in prior years. The AESO accordingly allocated those amounts to the relevant production years in its deferral account reconciliation. The AESO understands that ATCO Electric did not treat the amounts as part of its current year transmission revenue requirement, but rather as adjustments originating in prior years.⁷

51. From the above, the Commission understands that the AESO determined that the refund amounts should be attributed to specific years because the documentation provided by ATCO Electric to the AESO in support of the refund provided a breakdown which associated refund amounts to specific years.

52. The Commission finds that the AESO decision to make an attribution to specific prior years reflecting the breakdown provided by ATCO Electric was reasonable, and accordingly will not require the AESO to make any adjustments to deferral account balances for the years to which the refunds were applied. The Commission also finds that the decision to make the attribution was not specifically ordered by the Alberta Energy and Utilities Board (EUB) in the Decision 2007-071⁸ finding and associated direction which simply ordered that ATCO Electric submit for the EUB's approval a method whereby it would provide a timely refund but did not specifically require ATCO Electric to make an attribution of refund amounts to specific years. As such, the Commission considers that the decision to apply the refund on a go-forward basis or attribute the refund to specific years was discretionary to the AESO. Accordingly, the Commission considers that no adjustments need to be made to AESO deferral account balances in respect of the Decision 2007-104 refund.

53. However, the Commission considers that the issue of whether TFO tariff adjustments need be rigorously attributed to prior years or projected forward to future years is a component of the debate regarding potential simplifications of AESO deferral account reconciliation processes. This issue is discussed in greater detail in Section 6 below.

54. In light of the above-noted findings, the deferral account balances for each year set out in Table 2-2 of the application are approved as filed.

4 Keg project

55. Among the 2008 line items addressed in Decision 2009-191 was an expenditure of \$3.3 million on costs invoiced to the AESO from CPC in respect of expenditures on the KEG project prior to December 31, 2008. In view of the AESO's explanation that final costs arising from the KEG Project were not available by December 31, 2008, the Commission found in Decision 2009-191 that any cost balance in respect of the KEG project paid by the AESO after December 31, 2008, should be included in the AESO's 2009 deferral account reconciliation.⁹

⁷ AESO reply, paragraph 45.

⁸ Decision 2007-071: ATCO Electric Ltd. 2007-2008 General Tariff Application – Phase I, Application No. 1485740, September 22, 2007.

⁹ Decision 2009-191, page 8.

56. In Section 4.2 of the application, the AESO described proposed adjustments to its 2008 deferral account arising after the approval of the first reconciliation of 2008 deferral account balances in Decision 2009-191. The AESO indicated that the second reconciliation recorded cost for the KEG unit transformers conversion was \$5.5 million, \$2.2 million (or 66 per cent) more than the first reconciliation recorded costs of \$3.3 million.

57. The AESO noted that the \$5.5 million total cost of the KEG project fell within a ± 30 per cent accuracy range of the \$4.5 million cost estimate set out in the original project application approved in Decision 2008-101. The AESO further noted that it had engaged a consultant (Revay and Associates Limited) to review the KEG project costs and that the consultant's review had concluded that costs invoiced to the AESO in respect of the KEG project were the direct costs of carrying out the project and were prudent, accurate, and complete.

58. Argument and/or reply submissions in respect of the KEG project were provided by IPCAA, TCE, and the AESO. In consideration of the large volume and complexity of these submissions, the KEG project expenditures are discussed in detail in several subsections below.

4.1 Approach to KEG project prudence assessment

59. IPCAA submitted that because load customers are facing an unprecedented increase in transmission capital expenditures, it is important to develop quality cost reporting to confirm the prudence of expenditures.

60. Further, IPCAA submitted that while the Commission might question IPCAA's focus on a relatively small \$5.5 million expenditure, IPCAA proposed that, if the regulatory processes for the electric industry cannot manage costs prudently for a \$5 million project, the industry will not be able to manage the billion dollar projects now under development.

Commission findings

61. IPCAA's comments appear to suggest that it regards the assessment of the KEG project in this instance to be a test case for how prudence should be assessed for other types of capital expenditures, including in particular TFO direct assign projects. If so, the Commission disagrees.

62. In this regard, the Commission notes the express finding in Decision 2008-101 that the KEG project represented a unique project. Further, unlike a TFO direct assign project, the KEG project involved the AESO and an unregulated entity, over which the Commission does not have jurisdiction. It follows from these findings that Commission determinations with respect to the adequacy of the KEG project reporting, or with respect to the Commission's basis for assessing the prudence of the KEG project expenditures, should generally not impact information requirements or prudence assessment criteria applied to larger projects including TFO direct assign projects.

63. The Commission recognizes that the AESO was not bound by any specific criteria in providing support for the prudence of the KEG project. The AESO has provided the CRR in support of the actual costs of the KEG project and the Commission has assessed the prudence of the KEG project on that basis.

64. Because there is a cost to gather and assemble information, the Commission considers that the costs of collecting and providing more detailed support for a prudence assessment must be weighed against the materiality of the project variances.

65. The Commission has assessed IPCAA's submissions on the various faults that IPCAA alleged with respect to the CRR. These issues are discussed individually in the sections that follow. Despite the number of matters raised by IPCAA, the Commission has found that the CRR was sufficient to support the prudence of the KEG project expenditures for the reasons set out in this decision.

4.2 Process related concerns

66. In argument, IPCAA submitted that while the testing of the prudence of costs is inherently difficult in a written proceeding, this challenge was exacerbated by opposition from the AESO, CPC, and TransAlta to IPCAA's requests for the provision of detailed information.

67. IPCAA noted that it had required two rounds of information requests before IPCAA was able to get sufficient cost comparisons to develop questions that could test the prudence of the KEG project cost increases. However, IPCAA submitted that, because the Commission was unwilling¹⁰ to provide for another round of information requests, IPCAA considered the record to be incomplete. Because the applicant has all of the information and is incented to deny access to information that could challenge the legitimacy of costs, IPCAA submitted that interveners require the Commission to level the playing field with respect to information disclosure.

68. IPCAA submitted that its argument demonstrates that information on the record did not support a finding that a \$5,498,707 expenditure on the KEG project is prudent. Accordingly, IPCAA recommended that 50 per cent of the over-expenditure, or approximately \$500,000, be disallowed for cost recovery. Alternatively, should the Commission determine that further information is required before the Commission would consider a disallowance, IPCAA submitted that the Commission should direct the AESO to respond to additional information requests set out in Appendix A to IPCAA's argument and should set out appropriate further procedural steps after the AESO responses have been provided.

Commission findings

69. The Commission does not accept IPCAA's assertion that the record is not sufficient for the Commission to make a prudence determination at this time. The Commission finds that the record is sufficient for the Commission to test the prudence of the KEG project expenditures.

70. The Commission addresses the need for the AESO to provide answers to additional information requests set out in Appendix A to IPCAA's argument in Section 4.10 of the decision.

4.3 Confidentiality of KEG project information

71. IPCAA expressed concern that the AESO may be using regulatory processes to create an information deficiency environment for the purpose of avoiding their responsibility to defend the prudence of unreasonable costs. In the present instance, IPCAA submitted that the AESO and CPC had used confidentiality to prevent the disclosure of CPC's imprudence. After reviewing the confidential report, IPCAA submitted that there was no information in the report that would have harmed CPC's interests.

¹⁰ In reply, IPCAA clarified this comment as follows: "As a final matter, IPCAA would like to correct one word in its argument where it stated that the AUC "was unwilling to provide for another round of information requests" when IPCAA should have stated the AUC "was reluctant to provide for another round of information requests." IPCAA apologizes for this mischaracterization of events."

72. IPCAA submitted that, from its perspective, the assertions of CPC were motivated to hide behind the regulatory process, delay the provision of cost details and supporting explanations for the purpose of avoiding its obligation to demonstrate the prudence of its cost expenditures.

73. In reply, the AESO submitted that IPCAA had mischaracterized its request for confidentiality as attempts to create difficulty. Instead, the AESO submitted that it endeavored to be helpful while recognizing the commercial sensitivity of information in the un-redacted CRR.

Commission findings

74. In its September 24, 2010, ruling on the AESO's request for confidential treatment of the CRR, the Commission determined after review of an unredacted version of the CRR that, notwithstanding a strong presumption in favour of the open court principle in AUC proceedings, there could be a real and substantial risk to the commercial interests of CPC if certain information in the report were to be disclosed. The Commission finds no reason to vary this finding.

75. In light of the Commission's ruling that the CRR should be treated confidentially and the fact that IPCAA was ultimately able to review an unredacted version of the CRR, the Commission finds that there is no basis for IPCAA's allegation that confidentiality of the CRR had been invoked for the purpose of attempting to prevent the disclosure of imprudence.

4.4 Prudence testing principles for KEG project

76. IPCAA noted that Section 30(2) of the *Electric Utilities Act* (EUA) requires that rates charged to each class of customer must reflect the prudent costs attributable to each class of system access service provided by the AESO. IPCAA noted in addition that EUA S. 121(2)(a) requires the Commission to ensure that a tariff is just and reasonable and that S. 121(4) of the EUA places the burden of proof to demonstrate that a tariff is just and reasonable on the person seeking approval of the tariff. IPCAA submitted that the AESO and CPC thus fall under this burden of proof to demonstrate that the costs of the KEG project, which will become a part of the AESO tariff, are just and reasonable.

77. IPCAA submitted that findings made in decisions by the Commission and its predecessors have established longstanding definitions to be used for testing prudence. For example, IPCAA noted that in Decision 2000-01¹¹ the EUB observed the following:

...involves an evaluation of whether or not a decision reflects good judgement and discretion and is reasonable in the circumstances which were known, or reasonably should have been known, when the decision was made.

The concept of prudence is used to determine whether, at a particular time in question, an arrangement is or was appropriate and reasonable given the circumstances known or which ought to have been known.¹²

¹¹ Decision 2000-01: ESBI Alberta Ltd. 1999/2000 General Rate Application - Phase 1 and Phase 2, February 2, 2000.

¹² Decision 2000-01, page 46.

78. In addition, IPCAA noted the following test for prudence set out in Decision 2001-110:¹³

In summary, a utility will be found prudent if it exercises good judgment and makes decisions which are reasonable at the time they are made, based on information the owner of the utility knew or ought to have known at the time the decision was made. In making decisions, a utility must take into account the best interests of its customers, while still being entitled to a fair return.

79. IPCAA noted that, in Decision 2005-120,¹⁴ the EUB clarified that a presumption of prudence applied to utility expenditures can only be confirmed or overturned through an examination of the information and circumstances available to the utility or that it ought to have known at the time it executed decisions.

80. IPCAA took particular note of Decision 2005-120 findings discussing the requirement of a utility to fully explain and support both overall project costs and project cost components where project components exhibit large differences between forecast and actual costs, appear to be high relative to industry norms, or involve affiliate transactions. IPCAA also highlighted findings in Decision 2005-120 which expressed concern about the desirability of avoiding “information deficiency” situations where the prudence reviews may be hampered by the information needed to assess project costs at a more detailed level.

81. IPCAA submitted that it agreed with the EUB’s conclusions in Decision 2005-120 and had extracted the following six prudence test principles there from:

- (1) a utility must undertake actions with the best interests of customers in mind, while still being entitled to a fair return
- (2) a utility must fully explain and support overall project costs
- (3) the AUC must ensure that that onus under principle (2) is met particularly if project components have large differences between forecast and actual costs
- (4) the AUC must ensure that the onus under principle (2) is met if there are project component costs that appear to be high relative to industry norms
- (5) the prudence of direct assigned projects can best be conducted if project cost information at some meaningful level beyond the overall cost of the project is disclosed
- (6) that sometimes the appropriate type and level of information necessary to conduct a prudence review may not be available, and in that case, the full and proper application of the prudence review may be severely hampered, perhaps resulting in a situation where it is difficult to fully take into account the best interests of the utility’s customers and such an “information deficiency” situation should be avoided

82. Finally, IPCAA noted that in Decision 2001-110, the EUB discussed the obligation to consider “particular circumstances” of a transaction or expenditure in addition to considering the utility’s basic duties to exercise good judgment and act in a reasonable manner. Based on this precedent, IPCAA suggested that additional prudence principles should be developed to take into account particular circumstances of prudence assessments where information provided is deficient.

¹³ Decision-2001-110: Methodology for Managing Gas Supply Portfolios and Determining Gas Cost Recovery and Gas Rate Bundling Proceeding – Part B-1: Deferred Gas Account Reconciliation for ATCO Gas, Application No. 2001040, File No. 5680-1, December 13, 2001.

¹⁴ Decision 2005-120: AltaLink Management Ltd. Reconciliation of Direct Assigned Project Capital Deferral Accounts for the May 1, 2002 to April 30, 2004 Period, Application No. 1359518, November 22, 2005.

83. In reply, the AESO noted that, while IPCAA references findings in Decision 2000-01 regarding prudence assessments, IPCAA generally ignored that decision's finding that prudence assessments should "...determine whether, at a particular time in question, an arrangement is or was appropriate and reasonable given the circumstances known or which ought to have been known." The AESO submitted that an essential component of the Decision 2000-01 finding is that an assessment of the prudence of an arrangement should be considered in light of the time and in the circumstances the arrangement was made rather than at a later time with the benefit of hindsight and unhurried examination.

Commission findings

84. Although IPCAA extensively referenced Decision 2005-120, the Commission considers that IPCAA has both misinterpreted Decision 2005-120 findings and misapplied them to this proceeding. In particular, the Commission considers that IPCAA's proposition that Decision 2005-120 findings at pages 3-4 established six prudence test principles that apply not just to TFO direct assign projects, but also to the assessment of the prudence of any utility expenditure is incorrect. Decision 2005-120 expressed concern that an "information deficiency situation" might impair the ability of either the Commission or interested parties to test the prudence of AltaLink's expenditures on the direct assign projects under consideration in that proceeding. Nevertheless, the Commission's concerns with the availability of information in that case were insufficient to override the presumption of prudence extended to AltaLink.

85. Noting the above, the Commission considers that IPCAA's conversion of the concern stated by the EUB in the referenced section of Decision 2005-120 into principles is overreaching, as is IPCAA's further supposition that these principles must be met before the Commission can deem expenditures to be prudent in this proceeding.

86. The Commission considers three particular circumstances to be relevant in the present case.

87. First, it was clear in Decision 2008-101 that the AESO's (then) proposed expenditure on the KEG project constituted a unique situation that did not warrant the establishment of a general policy to guide potential future applications.¹⁵ In the unique circumstances of the KEG project, the Commission considers that there are no predefined criteria for establishing prudence and the AESO had broad discretion as to how it should demonstrate the prudence of the expenditure after project completion.

88. Second, the KEG project expenditures are relatively small in relation to some TFO expenditures on direct assign projects. Therefore, it was reasonable for the AESO to have weighed the value of making more detailed information available to facilitate interested party review of the expenditure against the cost of obtaining and assembling this information.

89. Third, unlike regulated investor owned utilities, the AESO is a not-for-profit corporation created under the *Electric Utilities Act* whose members must act in the public interest. This public interest obligation suggests a presumption of prudence may be applied to AESO expenditures. This is also borne out by S. 46(1) of the *Transmission Regulation*. Notwithstanding this however, the Commission considers that when the AESO contracts with a third party in

¹⁵ The Commission notes that at page 7, Decision 2008-101 expressly rejects a request made by the Office of the Utilities Consumer Advocate to establish a general policy regarding future payments to generators through the AESO's tariff.

circumstances such as the KEG project, where a third party's costs will not be subject to regulatory scrutiny (unlike a TFO's costs in a direct assign project), a greater duty of care is placed on the AESO in its oversight of that contract.

4.5 Prudence assessment criteria used in cost review report

90. In argument, IPCAA submitted that the authors of the CRR had failed to define prudence, and instead applied a narrow and incomplete criteria whereby costs were found to be prudent on the basis that (1) "all procurement packages follow procedures contained in EPCOR internal procedures manual;" and (2) EPCOR's internal accounting system assured that only direct costs attributable to the project were included in invoices to the AESO. IPCAA submitted that these review criteria should be considered to be woefully narrow and incomplete.

91. In addition, IPCAA submitted that the CRR authors erred by concluding that project expenditures were prudent on the basis that over-expenditures of 20 per cent were within the 30 per cent accuracy range designated in the estimate.

92. In reply, the AESO disagreed with IPCAA's suggestion that either it or the CRR authors had used the criterion of costs being within 30 per cent of the \$4.5 million original project cost estimate as the primary test for prudence. Instead, the AESO submitted that its primary test for prudence relied on a detailed examination of project costs carried out by an independent third party experienced in project audits.

93. The AESO submitted that IPCAA's suggestion that CRR authors had defined their own basis for review ignores the report's determination that procedures "were generally in accordance with General Accounting Standards for both financial and compliance audits."¹⁶

94. The AESO further submitted that IPCAA's suggestion that it had simply relied on EPCOR procurement procedures ignored the CRR authors' examination of these procedures before making a determination that they contained "normal and sufficient safeguards against abuse regarding solicitation of single source suppliers and other non-competitive arrangements for major purchases."¹⁷

Commission findings

95. IPCAA's argument that the CRR authors applied improper or inadequate criteria for their assessment of the prudence of the KEG project expenditures appears to be largely based on the following statement in the report:

The total value of invoices submitted by EPCOR to AESO (final invoice dated 30 November 2008) is \$5,449,520.92 (see Appendix E). This is \$915,452.92 greater than the estimate provided to AESO in March 2008, however, the percentage difference (20%) is within the 30% accuracy range designated in that estimate.¹⁸

96. The Commission recognizes IPCAA's concern that the report, particularly the above statement and the review criteria set out in the "Basis of Review" in the CRR, creates the appearance of a more limited review than was intended. However, the Commission notes the CRR authors' concluding opinion that its review procedures served to assure the AESO that

¹⁶ Exhibit 72.02, page 5.

¹⁷ Exhibit 72.02, page 7.

¹⁸ Exhibit 72.02, page 6.

“costs invoiced are not only “prudent” but also “accurate and complete”” with respect to the KEG project.

97. The Commission does not consider that the above statement implies that the CRR authors simply relied on the cost of the project falling within a 30 per cent accuracy range as the primary criterion for determining the KEG project expenditures to be prudent. Upon examination of the CRR, the Commission agrees with the AESO that the primary measure of prudence applied in this case is that independent individuals with experience in project assessment have reviewed project expenditures in considerable detail and determined that there were no improper transactions.

4.5.1 Effect of disclaimer

98. IPCAA submitted that its first concern with the CRR related to the following statement set out at page 10 of the report:

The Report is not to be relied on or used by third parties or outside agents to draw any inference or conclusions about this project and any interpretation given by them to the content of the Report is done so at their own risk.¹⁹

99. In consideration of the above noted disclaimer, IPCAA submitted that the only benefit of the AESO’s \$49,186 expenditure on the report was to provide a basis for interveners like IPCAA to ask information requests.

100. In reply, the AESO submitted that IPCAA overstated its concern with the disclaimer set out at page 10 of the CRR. The AESO submitted that such disclaimers are common for this kind of report and do not diminish the CRR’s conclusion that the costs invoiced to the AESO were prudent, accurate, and complete.

Commission findings

101. The Commission agrees with the AESO that the disclaimer represents boilerplate language in a report of this type. To the extent that the CRR was devised specifically for the purposes of a Commission review, the Commission considers that the disclaimer should recognize that purpose. Nonetheless, the Commission considers that the disclaimer does not hinder the Commission’s reliance on the CRR as evidence of the prudence of KEG project expenditures.

102. In addition, the Commission notes that no parties other than the AESO filed evidence in this proceeding. Accordingly, the Commission considers that, in this instance, no basis has been provided to suggest that any opinions or representations made by the authors of the CRR should be invalidated solely due to the existence of the disclaimer.

4.6 Issues related to KEG project cost estimate

4.6.1 Inclusion of contingency in estimate when costs already incurred

103. IPCAA submitted that the assessment of the prudence of the KEG project expenditures based on a comparison of actual costs with forecast costs could be flawed due to the inclusion of a contingency in the total project cost estimate when significant project expenditures have already been incurred.

¹⁹ Exhibit 72.02, page 10.

104. For example, IPCAA noted that a contingency was applied to a subtotal of \$1,088,850 for costs related to generating unit 3 conversion costs, even though \$391,323 of this amount had already been expended and invoiced for which a zero contingency would have been appropriate.²⁰ IPCAA submitted that if the \$391,323 amount (less a 9 per cent overhead of \$35,219, which may have already been applied to the \$391,323) is removed from the \$1,088,850, the balance is \$732,746. If the contingency of \$163,328 is divided by this estimate of future costs, the contingency level is now 22 per cent. A contingency of this level, combined with a 30 per cent accuracy range, results in an exceptionally wide range on this original estimate.²¹ IPCAA submitted that the addition of a contingency calculation on expenditures already incurred was inappropriate.

105. IPCAA submitted that, to the extent that the AESO and the CRR declared the costs to be prudent on the basis of being within the ± 30 per cent accuracy of the \$4.5 million cost estimate, such an assessment would not be valid due to the faulty basis for the 30 per cent accuracy range.

106. In reply, the AESO noted that IPCAA had raised several concerns that relate more properly to the basis for and accuracy of the project cost estimate originally reviewed in Decision 2008-101. While the AESO submitted that IPCAA's concerns were not warranted, the AESO submitted that the appropriate time to raise such concerns would have been in the proceeding that led to Decision 2008-101 when the estimate was first examined.

107. The AESO submitted that IPCAA's concern regarding the application of a contingency to project costs when significant expenditures have been incurred ignores the nature of a contingency. The AESO submitted that, while a contingency allowance is frequently estimated as a percentage of project costs, the likelihood of a contingency may be unaffected as costs are incurred during the course of a project. In the case of the KEG project, the failure of the spare generator transformer may be considered a contingent event. As such, the incurrence of costs in the initial planning and engineering of the project would not affect the likelihood of that event occurring nor the costs associated with responding to that event. The AESO submitted that it would therefore be inappropriate to reduce the contingency allowance due to the incurrence of costs in the initial stages of the project.

108. The AESO noted that IPCAA determined that the contingency amount was really 22 per cent after making adjustments to the base on which the 15 per cent contingency is applied, and that IPCAA had further extrapolated this logic to conclude that an accuracy range of approximately +45 per cent/-15 per cent rather than ± 30 per cent should be applied to the KEG project. However, whether expressed as ± 30 per cent of the original cost estimate or +45 per cent/-15 per cent of IPCAA's reinterpreted estimate, the AESO submitted the fact remained that the project was expected to cost between \$3,173,848 and \$5,894,288, the cost range described in Decision 2008-101 as \$4,534,068 with an accuracy of ± 30 per cent.

Commission findings

109. Considered in a general context, the Commission agrees with the AESO that it is reasonable to maintain a contingency allowance if the basis for the contingency allowance would not be impacted by expenditures that have already been incurred.

²⁰ Exhibit 72.02, Attachment A, page 3.

²¹ Exhibit 80.01, page 4, paragraph 3.

110. However, that does not appear to be the case in this circumstance. In considering the contingency allowance referenced by IPCAA, the Commission notes that the contingency allowance does not appear to be based on specific contingencies but rather upon a flat percentage allowance (15 per cent) to account for all potential contingencies. When the AESO filed its letter agreement on February 29, 2008, \$391,323 of this amount had already been invoiced in respect of costs for 2007.²² Accordingly, in this case, the Commission agrees with IPCAA that the AESO's inclusion of the contingency allowance on costs already incurred had the effect of overstating the potential for contingencies to create additional costs within the estimate considered for purposes of the initial KEG project approval granted in Decision 2008-101.

111. Nevertheless, the Commission does not consider that the overstatement of the estimate presented for Decision 2008-101 impacts the assessment of prudence in this case. If the prudence assessment had been based solely on the final cost of the project falling with 30 per cent of the estimate, as IPCAA argued, then this overstatement would have impacted the prudence assessment. However, as stated in Section 4.5, the Commission considers that the primary measure of prudence in this case is that an independent expert, with experience in project assessment, has reviewed the KEG project expenditures in considerable detail and determined that there were no improper transactions.

4.6.2 Application of total estimate accuracy range to project cost components

112. IPCAA submitted in argument that a utility has a duty to fully explain and support overall project costs and project cost components. Furthermore, IPCAA noted that its discussion of principles from prior decisions puts a particular onus on the Commission to ensure that both overall project costs and project component costs are fully explained and supported in situations where project components have large differences between forecast and actual costs.

113. In this regard, IPCAA noted that:

- the primary contract for the transformer conversion tap change for Genesee Unit 1 was 56.4 per cent over the original estimate
- the primary contract for the transformer conversion tap change for Genesee Unit 2 was 54.5 per cent over the original estimate and the engineering
- administration and overheads for Genesee Unit 2 were 42.0 per cent over the original estimate²³

114. IPCAA noted that each of these project component expenditures exceeded component forecasts by more than 30 per cent.

115. IPCAA submitted that, because the AESO and the CRR appear to base their respective prudence assessments on the total project cost being within a 30 per cent accuracy range rather than defending the prudence of individual project component expenditures, both the AESO's evidence and the CRR fail to support both overall and individual project component costs.

116. In reply, the AESO noted that, while IPCAA suggests that the accuracy range applied to the total project cost estimate should also apply by cost component, the AESO noted that no accuracy range was provided for individual cost components for the estimate examined in the proceeding that led to Decision 2008-101. The AESO submitted that the total cost estimate

²² Exhibit 72.02, Appendix A, page 14.

²³ Exhibit 88.02, page 1.

would reasonably have incorporated an expectation that variances could occur above and below the estimates for individual cost components, with offsetting impacts on the total cost estimate. The AESO noted that the notion that different project component variances offset one another has been discussed in the context of prior AESO deferral account reconciliations. In sum, the AESO submitted that the accuracy range of a total cost estimate should not simply be assumed to apply to each individual cost component of the estimate.

Commission findings

117. The Commission considers that IPCAA's concern about an alleged failure of the AESO and the CRR to demonstrate the prudence of individual components of the KEG project expenditures stems from IPCAA's over-riding view that the AESO and the CRR based their prudence pronouncement on the fact that total project costs fell within a ± 30 per cent accuracy range. However, as discussed in Section 4.5 the Commission has rejected this view, and found instead that the primary prudence criteria applied by the AESO was that an independent expert review had found no basis for imprudence after a detailed examination of project invoices.

118. The Commission is in agreement with the AESO that where an accuracy range is provided for the total cost of a project, it is reasonable to expect that the total cost estimate and accuracy range incorporate an expectation that variances both above and below individual component cost estimates could occur, with the component variances offsetting one another. As such, where an uncertain estimate subject to an accuracy range is established for a material expenditure such as the KEG project, it does not follow that, if the actual costs of individual project components fall outside of the total project accuracy range, the expenditures on individual components are imprudent unless proven otherwise.

4.6.3 Duty to seek approval for changes in project scope

119. IPCAA expressed concerns regarding an amount related to a contractual obligation identified in the unredacted CRR (disputed amount) which IPCAA submitted should have been disclosed by the AESO to the Commission during the proceeding leading to Decision 2008-101. Although the disputed amount relates to material that was subject to a confidentiality ruling, the Commission has determined it can discuss the relevant issue and provide its finding without reference to specific confidential information.

120. IPCAA expressed concern with the disputed amount, noting that neither the amount, nor its basis, had been disclosed to the AUC at the time it was still deliberating the application leading to Decision 2008-101.

121. IPCAA submitted that if a TFO knows the project scope has materially changed and/or costs will be well in excess of the original estimate, the TFO should inform the Commission, and the AESO, and demonstrate the need for the increased expenditure in advance. IPCAA further submitted that if the TFO is granted the latitude to spend up to 30 per cent more on any given project without any prior approval, the TFO has no incentive to prudently manage costs, so long as it stays within an over-expenditure of 30 per cent or less.

Commission findings

122. The Commission disagrees with IPCAA's position that the disputed amount should have been brought forward to the Commission during its deliberation prior to the issuance of Decision 2008-101 for the following reasons.

123. The Commission considers that the disputed amount is not sufficiently material to have required that the AESO advise the Commission of the amount, prior to the rendering of the Commission's decision, in order to prove the need for the increase in forecast costs.

124. In that proceeding, the AESO applied to have the KEG project costs approved on a forecast basis with a 30 per cent range allowed for variation. The Commission considers that forecasts that are presented as being uncertain will have variations as a result of information that becomes known after the fact. In approving the AESO's forecast amounts in Decision 2008-101, the Commission's expectation was that the prudence of the final expenditures would be assessed after the fact.

125. Further, the Commission is cognizant of the need to complete upgrades such as the KEG project as quickly as possible to minimize the duration of the disruption of a major generator and to avoid further costs within the Alberta electric system that might ensue as a result of the disruption. The Commission does not consider that the materiality of the disputed amount warranted the additional process that would have been associated with bringing the disputed amount for consideration by the Commission in the proceeding leading to Decision 2008-101.

4.7 Adequacy of project cost information and reporting

126. IPCAA submitted that while the AESO and CPC have all the relevant information required to demonstrate prudence, these parties did not provide it. As a result, IPCAA submitted that the AESO and CPC did not meet their burden of proof to demonstrate the prudence of their expenditures, and interveners have thus been denied the opportunity to test prudence.

127. IPCAA submitted that the Commission should consider the advantages of applicants, including extensive regulatory resources, their control over information, and limits on intervenor funding. Given this, IPCAA submitted that utilities, including the AESO, should provide component by component budget vs. actual comparisons, including variance explanations when filing for approval of additions to rate base or cost recovery in another form. In the current instance, IPCAA submitted that the Commission could remedy this situation by directing the AESO to respond to the information requests included in Appendix A to IPCAA's argument.

128. IPCAA submitted that CPC appeared to have taken advantage of the fact that generation transformers are not TFO assets to avoid provisions in ISO rules that would have required a TFO to competitively procure services. Instead, IPCAA submitted that the AESO appeared to have relieved CPC from the normal requirements under ISO Rules 9.1.3.1 to 9.1.3.6 on the grounds that the CRR substituted for these reports. To level the playing field, IPCAA submitted that the Commission should direct the AESO to respond to the IRs set out in Appendix A of IPCAA's argument.

129. In reply, the AESO noted that it did not require CPC to provide monthly reporting generally required under ISO Rule 9.1.3.1. The AESO submitted that notification of scope and schedule changes pursuant to ISO Rules 9.1.3.2 and 9.1.3.3 were accomplished through verbal coordination. Furthermore, the AESO submitted that the project change proposals and review required by ISO Rules 9.1.3.4 and 9.1.3.5 were not necessary due to the detailed coordination required during the project. In summary, the AESO submitted that the intent of reporting requirements under ISO Rule 9.1.3 was satisfactorily met through other means during the course of the project.

130. IPCAA suggested that “prudence principle 2 and 3” from Decision 2005-120 require the AESO to fully explain and support both overall cost and project cost components. As such, the AESO had a particular onus to explain variances (all well in excess of 30 per cent) for:

- Genesee 1 transformer tap change (56.4 per cent over original estimate)
- Genesee 2 transformer tap change (54.5 per cent over original estimate)
- Genesee 2 engineering, administration and overheads (42.0 per cent over original estimate)

Commission findings

131. The Commission does not agree with IPCAA that the AESO deliberately engaged in limiting access to information on the CRR in order to avoid an adverse prudence assessment. The entire CRR was provided on a confidential basis and provided the necessary information to examine the prudence of the expenditures. The Commission considers that the engagement of a third party to prepare the CRR was a reasonable approach to support prudence of its expenditure.

132. Further, the Commission considers that the KEG project is not a TFO direct assign project within the ambit of ISO Rule 9.1. As noted above, the KEG project was a unique project and not subject to reporting requirements designed for TFO direct-assign projects.

4.7.1 Need for benchmarking

133. IPCCAA noted that, in Decision 2008-101, the Commission accepted the project cost estimate of \$4,534,068 as reasonable, at least in part based on experience with other projects. Given this, IPCAA submitted that it followed that, based on industry norms, the \$4,534,068 estimate should be treated as the benchmark for the prudent cost of the KEG project.

134. In argument, IPCAA disagreed with the Commission’s September 9, 2010, ruling²⁴ regarding IPCAA’s request²⁵ to compare the KEG project costs with similar costs undertaken at Ellerslie and Keephills substations. IPCAA submitted that in the absence of credible proof of prudence from an evaluation of component costs, use of industry norms provides an alternative test. IPCAA noted that it had included a request for a cost evaluation against industry norms in Appendix A to its argument.

Commission findings

135. The Commission will not vary its ruling of September 9, 2010, and require the AESO to provide a comparison with similar costs undertaken at Ellerslie and Keephills. In light of the Commission’s findings throughout this decision that the CRR was adequate in supporting the prudence of the KEG project expenditures and given the relatively small cost of the KEG project (as compared to a direct assign project, for example), the Commission is not persuaded that the value of the additional information that might be gathered would warrant the additional costs that would be accrued. This notion is discussed further in Section 4.10.

4.8 Use of sole source suppliers

136. IPCAA expressed concern with the extent to which major portions of the KEG project relied on the work of single source suppliers. Of particular concern to IPCAA was the fact that

²⁴ Exhibit 85.01, page 6, paragraph 32.

²⁵ Exhibit 80.01.

\$3.1 million, or 57 per cent of total project costs, was provided by a single vendor, ABB Canada Ltd. (ABB).

137. IPCAA indicated that it was concerned that the CRR did not adequately test the reasonableness of the decision to use a single supplier for such a significant component of the project. In particular, IPCAA submitted that the CRR indicated that the sole source arrangement with ABB was entered into after two other suppliers were solicited and declined to submit tenders. The CRR speculated that while other suppliers could have been approached, there was “the likelihood of a similar result.”²⁶ However, IPCAA submitted that the CRR did not explain how the authors of the CRR could have confirmed this assessment after the fact, thereby leading IPCAA to suspect that the comment was based solely on representations by CPC. Furthermore, IPCAA submitted that the CRR provided no explanation as to why only two other suppliers were approached and provided no explanation as to why these potential suppliers had declined to submit tenders.

138. IPCAA noted that the CRR acknowledged that the ABB sole source purchase violated “safeguards against abuse regarding solicitation of single source suppliers and other non-competitive arrangements for major purchases” in EPCOR’s procurement manual. However, IPCAA submitted that the CRR did not indicate that the CRR authors had independently verified the reasonableness of the suggested excuses provided for this violation of the EPCOR procurement manual, which included the impact of the heated economy, the effect of schedule constraints, the availability of other potential suppliers, and the circumstances surrounding the decision of two suppliers to decline to submit tenders.

139. Similarly, respecting other KEG project services provided by single-source suppliers other than ABB, IPCAA submitted that there was no evidence that the CRR authors had tested sole-supplier explanations that the selected suppliers were the only ones capable or the effect of time constraints. If anything, IPCAA submitted that the delay of the KEG project from the fall of 2007 to the spring of 2008 should have created an opportunity for additional competitive procurement.

140. In summary, IPCAA submitted that the choice of a sole source supplier was for CPC’s convenience, with the result that less than competitive terms were adopted. As a result, the AESO and CPC should provide a full justification for the choice of a sole source supplier as requested in the information requests set out in Appendix A to IPCAA’s argument.

141. In reply, the AESO submitted that IPCAA’s concern that 57 per cent of the total costs for the project were provided by a single vendor, appeared to give no consideration to the fact that those costs related to reconfiguration of the unit transformers.

142. The AESO noted that the CRR discussed the fact that this work that would be impractical and inefficient to provide through multiple vendors.²⁷ The AESO also took note of the fact that three suppliers were approached for this aspect of the project, two of which declined to submit tenders. The AESO submitted that IPCAA also ignored the fact that at least 19 vendors were involved in the project overall,²⁸ and that some services were obtained from suppliers who were “the only ones capable of providing the service (transformer testing)” or were already on-site and

²⁶ Exhibit 72.02, page 7.

²⁷ Exhibit 72.02, page 6.

²⁸ Exhibit 72.02, page 6.

therefore able to meet the project's time constraints.²⁹ Given these considerations, the AESO submitted that the Commission's assessment of the KEG project prudence should recognize the reasonableness of decisions made in these circumstances.

Commission findings

143. In a project like the KEG project, it is expected that certain services can only be provided by certain suppliers. The authors of the CRR were satisfied that other suppliers were contacted but declined to provide estimates. The Commission will not require additional confirmation. Given the conclusions of the CRR and the fact that 19 vendors were involved in the project, the Commission does not consider the use of ABB for 57 per cent of the project to be unreasonable.

4.9 Impact of project delays (demobilization/remobilization costs)

144. The AESO submitted that information it provided had shown that about 51 per cent of the total \$0.9 million variance for the project arose from demobilization and remobilization costs associated with a delay from fall 2007 to spring 2008, due in part to the failure of the spare generator transformer in a factory test. Additionally, 27 per cent of the total variance resulted from escalation of primary contractor labour costs also resulting from the rescheduling of the work to occur in 2008. The remaining 22 per cent of the total variance resulted from other factors, including additional equipment monitoring capability and additional detailed coordination required by the AESO beyond the usual requirements that had been included in the cost estimates.

145. IPCAA submitted that \$374,475 of contractual penalties³⁰ which were characterized by the AESO as demobilization and remobilization costs³¹ which represented evidence that the AESO had entered into an uncompetitive arrangement with its supplier. IPCAA submitted that the size of the contractual penalties was surprising given the relatively short delay from fall 2007 to spring 2008. However, because the AESO's information responses did not provide contractual provisions or detailed calculations in support of the penalties, it was not possible to test the prudence of the penalty costs.

146. In consideration of the project delay from the fall of 2007 to the spring of 2008, IPCAA submitted that the CRR provided no information as to whether CPC had sufficient lead time to undertake the project on a timely basis. IPCAA also expressed concern that the authors of the CRR kept no minutes of meetings with CPC senior management and that no independent industry source or AESO staff verified the veracity of CPC statements.

147. IPCAA submitted that while the AESO justified costs attributed to demobilization and remobilization on the basis of the change in schedule from fall 2007 to spring 2008, a letter agreement between EPCOR and the AESO dated March 11, 2008³² provided no indication of costs being incurred prior to that date. Given the date of the estimate in the letter agreement, IPCAA submitted that costs related to demobilizing, remobilizing, and re-engineering should have already been included in the letter agreement estimate.

148. The AESO submitted that the KEG project costs reflect the cost of working within the shortest possible timeframes and the need to coordinate with other generator maintenance

²⁹ Exhibit 72.02, page 8.

³⁰ Exhibit 88.01, IPCAA.AESO-002.

³¹ Exhibit 88.01, attachment, IPCAA.AESO-002.

³² Exhibit 72.02, Attachment B, pages 4-5.

shutdowns. The AESO submitted that while IPCAA's comments did not reflect the time at which and circumstances under which work was arranged, the CRR supports the view that the work completed by CPC was appropriate and reasonable given the circumstances at the time.³³

Commission findings

149. The Commission notes that neither the redacted nor the unredacted versions of the CRR included details about CPC's contract with the supplier in question. Therefore, it was not possible for the Commission to compare demobilization and remobilization costs against the actual contract provisions. The Commission considers the lack of particulars about this contract and the limited evidence within the unredacted CRR to show that the CRR authors had closely scrutinized the rationale for and the particulars of this contract to be a deficiency of the CRR.

150. However, while the Commission has concerns about the limited documentation and discussion of demobilization and remobilization costs within the CRR, the Commission considers that there was nothing to suggest that these costs were not proper direct costs of the KEG project and therefore imprudent. The Commission also considers that the need to complete the upgrades as quickly as possible and to minimize the duration of the disruption of a major generator must be taken into account when assessing these amounts.

151. Considering the reliance of CPC and ultimately the AESO on sole source suppliers, the Commission does not consider the lack of documentation on demobilization and remobilization costs in the CRR to be a sufficient basis to overturn the presumption of prudence in this case. As such, the Commission finds no basis to conclude that the expenditures arising from contractual penalties associated with the KEG project were imprudent.

4.9.1 Adequacy of meeting documentation

152. IPCAA expressed concern that entrance and exit meetings with CPC management and involved personnel were not documented. IPCAA noted that in IPCAA.AESO-003, it had requested that the AESO provide "all the reports, agreements and relevant correspondence relative to the CPC projects (identified as the Genesee Generating Station – 500 kV Transformer Upgrade) between the AESO and CPC and between the AESO and other involved parties such as Revay and Associates." However, IPCAA submitted that the AESO's response appeared to be incomplete, since it would be highly likely that information from CPC to the AESO would have been documented in some form, such as reports or email correspondence. IPCAA submitted that, as the information sought in IPCAA.AESO-003 is relevant in an assessment of prudence, it should be provided. Accordingly, IPCAA indicated that it had raised this matter in the information requests included in Appendix A of its argument.

153. The AESO disagreed with IPCAA's suggestion that it had provided an incomplete response to information request IPCAA.AESO-003 which sought relevant correspondence between the AESO and CPC and between the AESO and other parties. The AESO noted that while IPCAA suggested that its suspicions were warranted on the basis of a statement in an information response where "the AESO notes that they were 'apprised throughout the project of scope and schedule changes'," the AESO submitted that much of the coordination for the project was carried out verbally, usually by telephone, but sometimes through in-person and tele-conference meetings. While certain technical matters related to transmission system

³³ AESO reply, paragraph 14.

reliability, protection, and control were addressed through e-mail correspondence, such matters were not relevant to the project's costs.

154. The AESO submitted that it considers that the letters, invoices, and interim report described in the information response constitute the documents relevant to the costs of the project.

Commission findings

155. The Commission is not persuaded by the argument of IPCAA that there are additional documents intentionally being withheld by the AESO in relation to the KEG project. The AESO provided information in response to IPCAA.AESO-003 and the Commission will not require further response from the AESO.

4.9.2 Examination of overheads

156. IPCAA submitted that the CRR indicated that the report authors made no attempt to verify a monthly financing rate to cover project financing costs and instead only relied on their experience to conclude that they appeared to be competitive with other rates within the industry.

157. IPCAA noted that in response to IPCAA.AESO-004, it was disclosed that for EPCOR in-house direct labour costs of \$254,157, the burden rate for vacation and benefits on direct labour was \$51,414, and an additional overhead charge was allocated to the project of \$290,170 for administration and general expense. IPCAA submitted that the overhead amounts described in the response to IPCAA.AESO-004 did not include \$1,090,053 in respect of engineering and administration costs.³⁴ IPCAA submitted that the fact that some, if not all of these overhead costs were not verified should be considered to be a deficiency of the CRR.

Commission findings

158. As discussed in the Commission's finding on Section 4.5, the Commission considers that the CRR provides an independent assessment of the KEG project and that project expenditures, including project overheads, were examined in detail. As such the Commission does not agree with IPCAA that the CRR is deficient in respect of its examination of the allocation of direct overheads to the project.

4.9.3 Consistency of project cost escalators

159. IPCAA submitted that there is a material inconsistency in the AESO's explanation of the effects of escalation in its response to IPCAA.AESO-002, as summarized in the table reproduced below:

Table 1. Escalation summary

	Genesee 1	Genesee 2	Genesee 3	All Units
Escalation of Labour Costs (Source: IPCAA.AESO-002)	\$ 111,550	\$ 66,850	\$ 71,250	\$ 249,650
Escalation (Source: IPCAA.AESO-002 Attachment)	\$ 0	\$ 0	\$ 54,443	\$ 54,443
Unexplained Difference	\$ 111,550	\$ 66,850	\$ 16,807	\$ 195,207

Source: IPCAA argument, page11.

³⁴ In footnote 61 to its argument, IPCAA indicates that the amount of \$1,090,053 was calculated by subtracting \$290,170 of overhead charges from \$1,380,223 of actual engineering and administration charges and overheads (provided in Exhibit 88.02, page 2).

160. IPCAA noted the apparent inconsistent treatment of escalation as between IPCAA.AESO-002 and IPCAA.AESO-002 Attachment was of interest because the \$915,453 difference between the final KEG project costs and the initial estimate is the same in both variance explanation breakdowns. In light of this apparent inconsistency, IPCAA sought a full explanation of the differences, including detailed supporting calculations.³⁵

161. The AESO submitted that the small amount of inflation included in the original estimate reflected the expected cost increase from when the estimate was prepared to when the work was expected to be done. The AESO further explained that the escalation amounts shown in IPCAA.AESO-002 reflected the actual change in labour costs from when the estimate was prepared to when the work was actually done, including the impact of the delay attributable to the failure of the spare generator transformer. With these explanations, the AESO submitted that there was no inconsistency in the information provided to IPCAA.

Commission findings

162. The Commission has reviewed the figures presented in the variance breakdowns provided by the AESO in IPCAA.AESO-002 and IPCAA.AESO-002 Attachment. The Commission notes that, like the allowance for “Contingency (estimate 15 per cent)” provided in the IPCAA.AESO-002 Attachment spreadsheet, the \$54,443 amount for “escalation” is represented as a component of the original GT3 Transformer cost estimate which does not show up as a corresponding “actual” in IPCAA.AESO-002 Attachment. The Commission accepts the AESO’s explanation that the \$54,443 amount represents a small inflation component included in the original estimate to reflect expected cost increases as determined at the time the original estimate was prepared.

163. The Commission notes that while the IPCAA.AESO-002 response and IPCAA.AESO-002 Attachment show identical amounts for the components of project cost variance related to demobilization and remobilization costs, the breakdowns for other variances are completely different between IPCAA.AESO-002 and IPCAA.AESO-002 Attachment.³⁶

164. The Commission considers that, while the different categorization of variances as between IPCAA.AESO-002 and IPCAA.AESO-002 Attachment may have created some confusion, the Commission accepts that the \$ 249,650 amounts for “Escalation of Labour Costs” and \$54,443 for “Escalation” in IPCAA.AESO-002 Attachment and IPCAA.AESO-002 respectively simply represent different breakdowns of the cost data that are not in conflict.

4.9.4 Disposition of surplus materials

165. IPCAA noted that the CRR indicates that certain surplus materials such as lighting arrestors deemed not applicable to other projects were wasted or destroyed. However, IPCAA submitted that the CRR provides no explanation as to why these materials were not returned to suppliers for a refund.

³⁵ IPCAA argument, page 11.

³⁶ Whereas IPCAA.AESO-002 Attachment shows amounts for “Planned scope of work,” “Engineering and administration,” “Overhead (estimate 9%),” “Overhead (estimate 9%),” “Contingency (estimate 15%),” and “Escalation”, IPCAA.AESO-002 breaks down variance amounts not related to demobilization/remobilization costs only as between “Escalation of labour costs” and “Other cost variances.”

Commission findings

166. The Commission notes that IPCAA's brief discussion of its concern with respect to surplus materials relates entirely to the limited amount of discussion these materials are given in the CRR. However, the Commission considers the fact that the CRR discussion is limited to be an insufficient basis to find imprudence in the handling of the surplus materials.

4.10 Relief requested by IPCAA

167. IPCAA submitted that in light of the substantial and material concerns raised in its argument, the Commission should deny all or a significant portion of the \$1 million cost overrun.

168. Specifically, considering the large number of concerns raised in argument about the prudence of the KEG project costs, and considering that a transformer failure that triggered a delay in the KEG project schedule was already known at the time CPC submitted a revised schedule to the AESO on February 29th, 2008, IPCAA recommended that the Commission apply a disallowance of at least 50 per cent of the cost overrun, or \$500,000.

169. Alternatively, in the event that the Commission determines further information is needed to consider the merits of a disallowance, IPCAA recommended that the AESO be required to respond to information requests set out in Appendix A to IPCAA's argument and that the Commission set out further procedural steps after the responses have been provided.

170. The AESO submitted that IPCAA had provided no substantive or material basis for its request for the Commission to deny all or a significant portion of the \$1 million cost overrun for the KEG project.

171. In addition, the AESO submitted that through the application, the CRR, and its information responses, it had provided substantial and complete information constituting "acceptable documentation to validate the quantum" of "actual direct costs" as required by Decision 2008-101, and further submitted that the information provided demonstrated the prudence of KEG project costs. Accordingly, the AESO submitted that there was no justification for IPCAA's request that the AESO be required to respond to eight additional information requests attached as Appendix A to IPCAA's argument.

Commission findings

172. As discussed in Section 4.4 above, the Commission applies a presumption of prudence to AESO expenditures. This presumption of prudence applies notwithstanding the burden of proof on the AESO pursuant to S. 121(4) of the EUA to demonstrate that its tariff is just and reasonable.

173. The bulk of IPCAA's argument for its requested disallowance is premised on IPCAA's view that the AESO failed to adequately demonstrate the prudence of specific KEG project line items. The Commission finds that IPCAA's request does not properly take into account the presumption of prudence that should be applied to an AESO expenditure of this type, particularly in light of the Commission's findings that the KEG project is unique, that the CRR was adequate in supporting the prudence of the KEG project, and the need to balance the materiality of project variances with the cost of obtaining additional information.

174. The Commission has also considered IPCAA's request for further process steps in light of information assembled by IPCAA as a result of its review of the unredacted CRR. Given that

the disputed amount is not material and that there is only a small probability that obtaining additional information through further process would lead the Commission to conclude that the disputed amount was incurred imprudently, the Commission finds that it is not in the public interest to require further process. For all of these reasons, the Commission declines IPCAA's request for additional process to further examine the KEG project costs.

4.11 Recovery method for KEG project costs

175. The AESO submitted that, in accordance with the Commission's order in Decision 2008-101, it had included \$3.3 million of recorded project costs for 2008 in its 2008 deferral account reconciliation application. The AESO submitted that it had noted during the 2008 deferral account reconciliation proceeding that as the project was not yet completed, further costs were expected to be incurred in 2009.

176. The AESO further noted that in Decision 2009-191 in respect of the AESO's 2008 deferral account reconciliation, the Commission directed the AESO to include any costs not already accounted for in that application in its next deferral account application. Accordingly, after receiving and paying an additional invoice for \$2.2 million from EPCOR Power Development Corporation, the AESO included the \$2.2 million of additional project costs for 2008 in its 2009 deferral account reconciliation application.

177. IPCAA indicated that it opposed recovering the full amount of the KEG project cost (\$5.5 million) as an adjustment to the AESO 2008 revenue requirement. Instead, IPCAA proposed that costs should be treated as capital expenditures on CPC's or EPCOR's books or through the AESO cost recovery method over time. IPCAA submitted that the AESO's proposed expense treatment would create intergenerational inequities as compared to recovery of project costs over the remaining lives of generation facilities and may not comply with s. 121(2) of the EUA.³⁷ Based on the weighted average age and remaining lives of Genesee units 1, 2, and 3, IPCAA submitted that the KEG project costs should be amortized over 25 years.

178. TCE indicated that it supported IPCAA's proposal to recover \$5.5 million cost of the KEG project over the remaining lifetime of project assets rather than charging it to customers in one year.

179. The AESO noted that its proposed treatment of the KEG project costs as a 2008 production year cost was discussed in both the application leading to the initial approval of the KEG project expenditures in Decision 2008-101 and that the Decision 2009-191 had already approved the inclusion of the majority of the KEG project costs as a 2008 cost on a final basis.

180. The AESO also opposed IPCAA's proposal to amortize the expenditure over a long period of time on the basis that it is small relative to the AESO's overall revenue requirement, it has not amortized capital costs for other parties and because IPCAA's amortization proposal would add unnecessary complexity to the recovery of this cost.

181. IPCAA submitted that Decisions 2008-101 and 2009-191 did not specify how the KEG project costs were to be recovered and thus did not preclude a recovery method that matched project costs to the remaining life of the assets. Furthermore, IPCAA submitted that a potentially premature approval of \$3.3 million of costs in the 2008 deferral account reconciliation

³⁷ IPCAA does not explain the basis for its view that the AESO's proposed treatment may not comply with s. 121(2) of the EUA.

proceeding (before total costs of project known) should not preclude the Commission from treating the entire \$5.5 million as a rate base amount recovered over 25 years and treating \$3.3 million as a credit in the 2009 deferral account reconciliation.

Commission findings

182. While the Commission is not precluded from directing the AESO to recover large expenditures over longer periods of time, the Commission considers that IPCAA's proposal to amortize the KEG project costs is not warranted because the AESO does not own an asset that it can amortize as result of its KEG project expenditures. In addition, the Commission considers that the relatively small size of the AESO's expenditure on the KEG project in relation to the size of the AESO's overall revenue requirement does not give rise to sufficient intergenerational inequity concerns so as to warrant the additional administrative complexity contemplated by IPCAA.

5 Allocation of deferral account balances to customers

183. The AESO described its processes and procedures for allocating deferral account balances to individual customers and the associated settlement of imbalances in Sections 2.7 and Section 9 of the application.

184. Summarizing its processes in argument, the AESO noted that, as in previous deferral account applications, deferral account balances and adjustments were allocated to customers in accordance with procedures discussed in Section 9.1 of the application.

185. The AESO further noted that Section 9.2 of the application described the preparation of customer allocation summaries and detailed reports included as Appendices G, I, J and K to the application. As with previous deferral account reconciliations, the AESO noted that customer confidentiality was protected by assigning a number to each AESO direct-connect customers. In addition, after distributing the applicable identifier numbers to each customer, the AESO noted that applicable reports and other supporting information provided in Microsoft Excel format were distributed to each customer. In addition, in recognition of the large volume of data on which many calculations are performed and the limited ability of customers to verify reconciliations beyond calculations applicable to their individual accounts, the AESO noted that PricewaterhouseCoopers prepared a report on specified procedures used by the AESO to allocate deferral account balances to individual customers.

186. In summary, the AESO submitted that as the allocation of deferral account balances and adjustments to customers was completed in the same manner as in previous deferral account reconciliation applications and as no information requests raised concerns with the allocation, the allocation to customers should be approved as filed.

187. The AESO noted that further to a request made concurrent with the filing of the application on April 15, 2010, that charges and refunds due to customers be settled on an interim refundable basis as soon as possible, the AESO noted that on May 13, 2010, the Commission issued Decision 2010-209 approving the requested interim distribution of the deferral account balances. In addition, the AESO noted that on July 7, 2010, a compliance notice was provided to the Commission which confirmed that the financial settlement with customers ordered in Decision 2010-209 had been completed.

Commission findings

188. The Commission notes that, as in past deferral account reconciliation applications, the AESO provided extensive information on the allocation of deferral account balances to individual AESO customers. Additionally, as with past applications, the AESO indicated its willingness to make additional details regarding how allocations were determined available to individual customers. No parties other than the AESO discussed the allocation of deferral account balances to individual customers in argument or reply.

189. In view of these considerations, the customer allocations for the 2004-2009 periods as set out in appendices G, I, J and K of the application are approved as filed.

6 Future deferral account reconciliations

190. The AESO discussed its proposals for future deferral account reconciliation applications in Section 2.8 of the application. The AESO noted therein that in its 2008 application, it had described several specific expectations regarding processes it anticipated following for future deferral account reconciliations. The AESO submitted that these expectations had generally been met for the 2009 application and that it expected to follow the same approach for future applications. However, the AESO noted that the application did not seek approval or direction in respect of these matters.

191. The AESO noted that consultations held with stakeholder working groups in November 2009 and March 2010, discussions were held about potential approaches for responding to directions set out in Decision 2009-191 to investigate a Commission concern about the number of times that additional reconciliation is required in respect of deferral account years already considered by the Commission in its review of prior applications.

192. In addition, the AESO noted that in light of the Commission's comments in Decision 2009-191, it had investigated the use of a "termination and roll-up" approach under which full reconciliations would only be provided for only the most recent three years with transactions occurring in any earlier years being "rolled-up" into the oldest year for which a full reconciliation was being completed. However, the AESO indicated that it had rejected this approach in consideration of several disadvantages, including:

- reduced precision of the deferral account balance allocations, especially for Supply Transmission Services related amounts
- reduced transparency of balance allocations
- little reduction in AESO resource requirements
- concern that material amounts allocated in respect of a "terminated" year would require re-reconciliation

193. The AESO noted that it also considered other potential approaches beyond the termination and roll-up method, but ultimately concluded that alternative approaches to the current practice of multiple full reconciliations would be impractical while balances in the AESO deferral account remain relatively large and volatile. However, the AESO also noted that it had proposed certain changes in its 2010 GTA which might reduce the size and volatility of its deferral accounts.

194. Despite rejecting the simplified approaches discussed above, the AESO considered that the Commission concern expressed in Decision 2009-191 could be addressed by adopting a modified review and approval process under a continuation of the multi-year retrospective deferral account reconciliation approach. In particular, as an alternative to full regulatory reviews of second and later reconciliations, the AESO proposed a compliance review approach under which the Commission would expressly approve each first reconciliation of a deferral account year but with a third party providing formal compliance reviews in respect of second and earlier reconciliations.

195. Under the compliance review approach, the third party would provide assurance that second and later reconciliations follow the calculations and allocation methodology approved for a first reconciliation. In addition, the AESO proposed that in the event that deferral account balances exceeded a materiality threshold proposed to be ± 1 per cent of the AESO's annual revenue requirement subject to deferral account reconciliation, a re-reconciliation would be brought before the Commission. The AESO also proposed to reserve the right to request Commission approval of any specific deferral account re-reconciliation in the event that the AESO considered that unusual circumstances warranted such a request.

196. In consideration of the above described proposal, the AESO indicated that it specifically sought the Commission's approval to:

- continue to provide annual deferral account reconciliation applications that include full reconciliations of all production years to which transactions in the application year relate
- provide compliance reviews of second and later deferral account reconciliations that remove the need for Commission approval of those reconciliations when deferral account balances, both individually and in aggregate, are less than ± 1 per cent of the AESO's annual revenue requirement subject to deferral account reconciliation and when no unusual circumstances warrant a request for specific Commission approval of a second or later reconciliation
- financially settle the first reconciliation as well as second and later reconciliations on an interim basis without specific Commission approval upon filing of the compliance review for a deferral account reconciliation application

197. However, in argument, the AESO noted that, as a result of delays in processing the 2009 deferral account reconciliation, it was withdrawing its request for approval to conduct its 2010 deferral account reconciliation under the new approach set out in Section 1.4 of the application. Instead, the AESO indicated that it intended to prepare and file its 2010 deferral account reconciliation application in the same manner as its 2009 application.

198. TCE submitted that it supported the AESO's proposals set out in Section 2.8 of the application for the reasons set out by the AESO therein. TCE also submitted that, as a large customer, accurate deferral account reconciliation calculations are important because deferral account adjustments are affected by consumption levels and consumption levels can vary significantly from year to year.

199. In respect of the Commission proposal for which the AESO provided comments in its response to AUC-AESO-001, TCE submitted that it agreed with the AESO that it may be difficult for both the AESO and interveners to assess prudence of the types of costs included in a deferral account reconciliation application several years after the costs have been incurred. In addition, TCE submitted that while current deferral account reconciliation applications are

structured in a manner that allows customers to perform reconciliations to their own accounting information, corporate data archiving practices may make it more difficult for individual customers to conduct their own settlements if multiple year reconciliations were to be combined into a single application.

200. For the above reasons, TCE supported the AESO's position that further stakeholder discussions should occur before the Commission directs the AESO to make material changes to the current approach.

201. The UCA expressed concern that the AESO may not be accurately interpreting or applying Commission decisions. In particular, the UCA submitted that while the AESO suggests that Decision 2007-104 findings respecting requirement for ATCO Electric to refund future income taxes that ATCO Electric had collected from customers as part of a transition to a flow-through method to compute federal and provincial income taxes had the effect of adjusting ATCO Electric's TFO tariff for the years 2003 through 2007, Decision 2007-104 related to ATCO Electric's 2007-2008 tariff application, and not any prior year. The UCA noted that the AESO's interpretation of Decision 2007-104 was not consistent with a Commission ruling on issues of prospectivity and retroactive rate making set out in Decision 2009-214.³⁸

202. The UCA submitted that it was concerned with the continual re-reconciliation of years, with no end. In this regard, the UCA noted that the AESO makes adjustments going as far back as 2006 in the application, and noted that after adjusting for changes in TFO wires costs attributable to discrete Commission decisions, the residual prior year amounts being reconciled are minimal. The UCA noted in particular that for distribution-connected customers, AESO deferral account balances for prior years are not reallocated back to prior year customers but are actually allocated to current customers.

203. The UCA submitted that the effort required to re-reconcile deferral account balances between \$0.1 million and \$0.8 million may not be worth the benefits. While acknowledging that the AESO cannot retain a surplus or deficit, there is a point at which material adjustments cease and re-reconciliation is not needed. Given this, the UCA submitted that alternatives, including the collection of adjustments from current customers, should be considered.

204. In reply, the AESO submitted that the UCA had not demonstrated that the efficiency of deferral account reconciliation processes would be materially improved through the alternate treatment of small deferral account balances. In particular, the AESO submitted that even if the UCA's alternate process for small balances were to be adopted, as noted by TCE, there would still be a need to reconcile years for which deferral account balances are not small. Accordingly, the AESO submitted that removing two or three years from a reconciliation application would not appreciably improve the efficiency of the reconciliation process but could decrease accuracy and transparency.

205. The AESO submitted that it was unclear why the fact that distribution utilities recover deferral account balances on a prospective basis using the current consumption of each customer should be related to the AESO's approach to reconciling its deferral accounts. In this regard, the AESO noted that the fact that the AESO has reconciled deferral accounts respectively for several years has not impacted the reconciliation approach adopted by distribution utilities. As such, the

³⁸ Decision 2009-214: ATCO Gas 2008-2009 General Rate Application Phase I Income Tax Module, Application No. 1553052, Proceeding ID. 11, November 12, 2009, paragraph 101.

AESO expected that even if it were to implement an alternative approach to reconciling its own deferral accounts, this change would not impact the reconciliation approach used by distribution utilities.

Commission findings

206. As discussed in Section 3 above, it is apparent that a significant driver of the re-reconciliation of AESO deferral account years results from the AESO's practice of ensuring that final TFO tariff revenue requirements for particular calendar years are allocated to AESO customers in respect of the same calendar years under the AESO's tariff.

207. The Commission considers that while the AESO has adopted a consistent practice of rigorously allocating TFO tariff reconciliations to corresponding AESO tariff years, the Commission does not consider this practice to be mandatory.

208. Noting in particular the UCA's observation that AESO deferral account balances for prior years are collected from current distribution-connected customers rather than being reallocated back to prior year distribution-connected customers, the Commission considers that some consideration should be given to projecting at least some prior-year AESO revenue to cost imbalances forward rather than requiring all imbalances to be precisely re-reconciled.

209. However, the Commission also acknowledges the concern of TCE that, because consumption levels for larger customers may vary significantly from year to year, large customers may have a concern that a significant misallocation of costs could occur if material AESO deferral account balances were to be projected forward rather than being precisely reconciled to a customer's consumption for the year to which the deferral account balances relate. The Commission considers that the concern about a potential misallocation of costs may relate, in part, to the fact that Rider C under the AESO's tariff is charged on an energy (\$/MWh) basis.

210. In this regard, the Commission also notes the following finding from Decision [2010-606](#):³⁹

313. Instead of bringing forward alternatives and discussing the interactions between tariff updates and deferral account reconciliations within this tariff application, as suggested by the Commission in Decision [2009-151](#),⁴⁰ the AESO opted instead to include discussion of potential changes to deferral account reconciliations within its 2009 deferral account reconciliation application and consider Rider C within the context of its GTA. This has arguably limited the opportunity for the Commission to coordinate the design of deferral account applications, tariff updates and the design of Rider C within this proceeding.

314. The Commission has subsequently received the AESO's 2009 deferral account reconciliation application (Proceeding ID 589) and will consider any alternatives proposed by the AESO within Proceeding ID 589. The Commission takes note, however, of comments made by the DUC in relation to the AESO's proposed annual tariff update approach in which the DUC expresses support for annual tariff updates in part based on a

³⁹ Decision 2010-606: Alberta Electric System Operator 2010 ISO Tariff, Application No. 1605961, Proceeding ID. 530, December 22, 2010.

⁴⁰ Decision 2009-151: AltaLink Management Ltd. and TransAlta Corporation 2009 and 2010 Transmission Facility Owner Tariffs, Application No. 1587092, Application No. 1594573, Proceeding ID. 102, October 2, 2009.

concern that the energy based denomination of Rider C may contribute to periodic misalignments between the amounts that AESO customers should pay and the amounts they are required to pay for services under the tariff.

315. In consideration of the above, the Commission remains interested in understanding whether potential changes in the design of Rider C could contribute to a reduction in the frequency of tariff update applications and/or deferral account reconciliations. Accordingly, the Commission directs the AESO to discuss proposed changes to the design of Rider C no later than its next GTA unless already addressed in another context such as in relation to a future AESO deferral account reconciliation application.

211. As noted in the above, the Commission remains of the view that deferral account reconciliation processes and the design of Rider C should be aligned. Accordingly, the Commission directs the AESO to consult with stakeholders for the purpose of determining whether AESO deferral account balances related to years that have already be subject to at least one reconciliation may be projected forward rather than being precisely re-reconciled. For greater certainty, the AESO is specifically directed to consider whether prior year AESO deferral account reconciliations arising from Commission decisions in respect of TFO tariffs should be re-reconciled or projected forward. The Commission further directs the AESO to discuss whether changes in the design of Rider C could be made for the purposes of minimizing the need to re-reconcile AESO deferral account balances. The AESO is directed to provide a report on its discussions with stakeholders in respect of this matter at the time of its next major GTA.

7 Outstanding directions

212. In Section 11 of the application, the AESO summarized its responses to the following Commission directions set out in either Decision 2009-151 and Decision 2009-191:

- direction at paragraph 529 of Decision 2009-151 regarding the recovery of costs for the cancelled Genesee-Langdon 500 kV project
- direction at paragraph 43 of Decision 2009-191 regarding the KEG project costs not dealt with in that decision
- direction at paragraph 57 of Decision 2009-191 to consider Commission concern about repeated reconciliation of deferral account years

Commission findings

213. In Section 3.1.1 of the application, the AESO explained the \$35 million payment to AltaLink in the 2009 deferral account reconciliation. The Commission considers that the AESO has complied with the direction to give effect to the \$35 million backstop arrangement and to provide a full description of the details. The Commission also notes that no interested party in the proceeding raised any issues with respect to the AESO's treatment of this amount.

214. The additional cost of \$2.2 million paid in 2009 for the KEG transformer conversion project was discussed by the AESO in Section 4.2.1 of the application. In Section 4 of this decision, the Commission has considered the explanation provided by the AESO regarding the costs of the KEG transformer conversion. The Commission accepts that the AESO has provided the explanation required related to the final costs of the KEG project.

215. In Section 6 of this decision, the Commission has considered the discussion submitted by the AESO regarding the repeated reconciliations of deferral account years. As discussed in Section 6, the Commission has directed the AESO to consult with stakeholders further on the possibility of projecting the TFO tariff related adjustments on a forward basis rather than backward.

8 Order

216. It is hereby ordered that:

The interim settlements of the AESO 2009 deferral accounts reconciliation approved in Decision 2010-209 are confirmed as applied for by the AESO.

Dated on February 10, 2011.

The Alberta Utilities Commission

(original signed by)

Mark Kolesar
Panel Chair

(original signed by)

Bill Lyttle
Commission Member

Appendix 1 – Proceeding participants

Name of Organization (Abbreviation) Counsel or Representative (APPLICANTS)
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Alberta Utilities Commission Commission Panel M. Kolesar, Panel Chair B. Lyttle, Commission Member Commission Staff V. Slawinski (Commission Counsel) J. Halls K. Schultz
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Appendix 2 – Summary of Commission directions

As noted in the above, the Commission remains of the view that deferral account reconciliation processes and the design of Rider C should be aligned. Accordingly, the Commission directs the AESO to consult with stakeholders for the purpose of determining whether AESO deferral account balances related to years that have already be subject to at least one reconciliation may be projected forward rather than being precisely re-reconciled. For greater certainty, the AESO is specifically directed to consider whether prior year AESO deferral account reconciliations arising from Commission decisions in respect of TFO tariffs should be re-reconciled or projected forward. The Commission further directs the AESO to discuss whether changes in the design of Rider C could be made for the purposes of minimizing the need to re-reconcile AESO deferral account balances. The AESO is directed to provide a report on its discussions with stakeholders in respect of this matter at the time of its next major GTA. Paragraph 211