Decision **2738-D01-2016**

AUC
Alberta Utilities Commission

ATCO Gas and Pipelines Ltd.

Z Factor Application for Recovery of 2013 Southern Alberta Flood Costs

March 16, 2016

Alberta Utilities Commission
Decision 2738-D01-2016
ATCO Gas and Pipelines Ltd.
Z Factor Application for Recovery of 2013 Southern Alberta Flood Costs
Proceeding 2738

March 16, 2016

Published by the:
Alberta Utilities Commission
Fifth Avenue Place, Fourth Floor, 425 First Street S.W.
Calgary, Alberta
T2P 3L8

Telephone: 403-592-8845
Fax: 403-592-4406

Website: www.auc.ab.ca

Contents

1 Introduction **1**

2 Background **2**
2.1 Overview of the Z factor approach under performance-based regulation 2

3 ATCO Gas's application **5**
3.1 Prudence of costs 6
3.2 Lost revenue 8
3.3 Materiality 9

4 Depreciation **14**

5 Order **21**

Appendix 1 – Proceeding participants **23**

List of tables

Table 1. O&M costs of the 2013 Alberta flood **6**

Table 2. Z factor calculation mid-year rate base of the 2013 Alberta flood ($000) **7**

Table 3. Z factor calculation **11**

Table 4. 2013 Z factor detail **13**

Table 5. Z factor calculation **13**

Table 6. NBV and replacement costs associated with the 2013 and 2005 floods, and the 1987 tornado **15**

ATCO Gas and Pipelines Ltd.
Z Factor Application for Recovery of 2013 Southern Alberta Flood Costs

Decision 2738-D01-2016
Proceeding 2738

1 Introduction

1. This decision provides the Alberta Utilities Commission's determination of ATCO Gas and Pipelines Ltd.'s (ATCO Gas) application to recover $5.662 million through a Z factor rate adjustment to compensate it for the costs it incurred as a result of the 2013 Southern Alberta flood. For the reasons set out in this decision, the Commission approved the recovery of Z factor compensation in the amount of $3.121million. Additionally, the Commission determined that ATCO Gas's depreciation study had contemplated the retirement of assets due to an event similar to the 2013 flood and, therefore, the depreciation expense associated with the assets that were replaced will continue to be recovered from ratepayers.

2. On July 24, 2013, ATCO Gas filed a letter with the Commission advising that it anticipated filing a Z factor application for the recovery of costs associated with the 2013 flood experienced in Southern Alberta. At the time of the letter, ATCO Gas indicated it had incurred substantial costs to maintain safe operation of its distribution system and to restore service as a result of the flood, but had not yet fully analyzed the financial impact, including the cost of rebuilding the distribution system. ATCO Gas stated that it would file a Z factor application with the Commission once it completed its financial analysis of the impacts of the flood.[1]

3. In an acknowledgement letter dated July 26, 2013, the Commission registered Proceeding 2738 for the Z factor application, and stated that the filing announcement and notice of application would not be issued until the application was received.[2]

4. On July 9, 2015, ATCO Gas filed its Z factor application with the Commission. ATCO Gas applied for a total Z factor adjustment of $5.662 million for ATCO Gas South. The Z factor adjustment was composed of revenue requirement amounts associated with capital assets replaced in five specific years ($75,000 for 2013, $379,000 for 2014, $660,000 for 2015, $682,000 for 2016 and $665,000 for 2017), recovery of $2.951 million in operations and maintenance (O&M) costs and lost revenue, and $250,000 for carrying charges. ATCO Gas also sought approval to true-up the Z factor amounts to actuals for each year once the actual costs are known.[3]

5. The Commission issued notice of the application on July 13, 2015. The notice required interested parties to submit a statement of intent to participate (SIP) by July 27, 2015, and to indicate whether further process was required to process the application.

[1] Exhibit 0001.00.ATCOGas-2738, notification of potential Z factor adjustment letter, July 24, 2013.
[2] Exhibit 0002.00.ATCOGas-2738, Commission letter of acknowledgement, July 26, 2013.
[3] Exhibit 2738-X0003, application, paragraph 5.

6. The Commission received SIPs from AltaLink Management Ltd., AltaGas Utilities Inc., the Consumers' Coalition of Alberta (CCA) and the Office of the Utilities Consumer Advocate (UCA). AltaLink and AltaGas indicated that they did not anticipate being actively involved in the proceeding. The CCA indicated an intention to file information requests, review responses, and file argument and reply argument. The UCA requested the opportunity to test the application with a process of information requests before commenting on whether or not it would be objecting to the application.

7. In a letter dated July 29, 2015, the Commission advised it would be considering the application by way of a *minimal written process* and established a process schedule for the application.

8. On September 3, 2015, the UCA submitted a letter requesting that it be allowed to submit intervener evidence in the proceeding by September 15, 2015. On September 9, 2015, the Commission approved the UCA's request and issued a revised process schedule. Further changes to the proceeding schedule, requested by both ATCO Gas and the UCA, were approved by the Commission on September 16, 2015, November 3, 2015, and December 11, 2015. The record of this proceeding closed on December 17, 2015, following receipt of the parties' reply arguments.

9. In reaching the determinations set out within this decision, the Commission has considered all relevant materials comprising the record of this proceeding. Accordingly, references in this decision to specific parts of the record are intended to assist the reader in understanding the Commission's reasoning relating to a particular matter and should not be taken as an indication that the Commission did not consider all relevant portions of the record with respect to that matter.

2 Background

2.1 Overview of the Z factor approach under performance-based regulation

10. On September 12, 2012, the Commission issued Decision 2012-237,[4] approving performance-based regulation (PBR) plans for the distribution utility services of certain Alberta electric and gas companies, including ATCO Gas. The PBR plans were approved for a five-year term commencing January 1, 2013. PBR replaces traditional cost-of-service regulation as the annual rate-setting mechanism for distribution utility rates.

11. The PBR framework provides a formula mechanism for the annual adjustment of rates for those companies under an approved PBR plan. In general, rates are adjusted annually by means of an indexing mechanism that tracks the rate of inflation (I) relevant to the prices of inputs the companies use, less a productivity offset (X) to reflect the productivity improvements the company can be expected to achieve during the PBR plan period.

12. Establishing prices in this way during the term of a PBR plan creates stronger incentives for the companies to improve their efficiency because they are able to retain the increased profits generated by those cost reductions longer than they would under cost-of-service regulation. At the same time, under a PBR regulatory framework, customers automatically share in the

[4] Decision 2012-237: Rate Regulation Initiative, Distribution Performance-Based Regulation, Proceeding 566, Application 1606029-1, September 12, 2012.

expected productivity gains because they are built into rates through the X factor regardless of the actual performance of the companies.

13. However, the PBR regulatory framework recognizes that in competitive markets, exogenous factors that affect only the industry in question, such as an increase in taxes, would be passed through to customers by that industry in its market prices. PBR plans typically include a Z factor to deal with significant events outside the companies' control that are specific to the industry and would not be reflected through the I factor. The Z factor can also be used to account for cost changes caused by unique company-specific events (such as floods or ice storms) outside the company's control and that are not reflected in the inflation factor.[5]

14. In Decision 2012-237, the Commission established the following criteria to be applied when evaluating whether the impact of an exogenous event qualified for Z factor treatment:

> (1) The impact must be attributable to some event outside management's control.
> (2) The impact of the event must be material. It must have a significant influence on the operation of the company otherwise the impact should be expensed or recognized as income, in the normal course of business.
> (3) The impact of the event should not have a significant influence on the inflation factor in the PBR formulas.
> (4) All costs claimed as an exogenous adjustment must be prudently incurred.
> (5) The impact of the event was unforeseen.[6]

15. All of the above criteria must be met in order for an item to qualify for a Z factor rate adjustment.[7]

16. In addition, the Commission clarified that the exogenous event which may qualify for a Z factor may include a company-specific event or impact, as this is consistent with providing a company with a reasonable opportunity to recover its prudently-incurred costs.[8] Further, the Commission held that "… Z factors should be symmetrical in that they should apply to exogenous events with both additional costs that the company needs to recover and also reductions to costs that need to be refunded to customers…."[9]

17. Regarding materiality, there have been two approaches proposed by parties. In the proceeding leading to Decision 2009-035, ENMAX Power Corporation proposed that materiality be considered on the basis of a single event.[10] A number of parties in Proceeding 566, the proceeding leading to Decision 2012-237, proposed a cumulative approach to measuring materiality, whereby the effects of multiple exogenous events in a year are summed and, if they have a material impact on the company, are considered as a single event for the purposes of Z factor evaluation.[11] The Commission did not provide specific direction on which approach

[5] Decision 2012-237, paragraph 18.
[6] Decision 2012-237, paragraph 524. Note: The criteria for a Z factor 1 to 4 were adopted from Decision 2009-035: ENMAX Power Corporation, 2007-2016 Formula Based Ratemaking, Proceeding 12, Application 1550487-1, March 25, 2009, paragraph 247. Criterion 5 was included in the Z factor criteria in Decision 2012-237.
[7] Decision 2012-237, paragraph 525.
[8] Decision 2012-237, paragraph 527.
[9] Decision 2012-237, paragraph 528.
[10] Decision 2009-035, paragraph 231.
[11] Decision 2012-237, paragraph 529.

should be adopted. Rather, it determined that a relatively high materiality threshold was required absent exceptional circumstances, and stated:

> 534. … Given the exceptional nature of a qualifying exogenous event and the equally exceptional measure of authorizing a recovery outside of the I-X mechanism, the Commission considers that the PBR principles require a relatively high threshold and that this threshold should apply to each event unless otherwise permitted in exceptional circumstances.[12]

18. The Commission also determined that the materiality threshold should be based on the impact to return on equity (ROE), stating:

> 535. The Commission considers that the approach to establishing a materiality threshold based on the impact to ROE as proposed by AltaGas is reasonable. However, the Commission finds that the materiality threshold should be higher. In order to establish the threshold the Commission has calculated the impact on ROE that the dollar threshold established for ENMAX represented in 2006 (going-in rates). Accordingly, the Commission establishes the threshold as the dollar value of a 40 basis point change in ROE on an after tax basis calculated on the company‘s equity used to determine the revenue requirement on which going-in rates were established (2012). This dollar amount threshold is to be escalated by I-X annually. The companies are directed to calculate and file the 2012 threshold amount along with supporting calculations in the compliance filing to this proceeding.[13]

19. Regarding the process by which Z factor adjustments would be considered, the Commission directed companies to notify it of all proposed adjustments as soon as possible after the exogenous event is identified, and to submit Z factor applications as soon as possible after the associated cost of the exogenous event has been incurred or the savings have been realized.[14] The Commission further directed that Z factor rate applications be filed as part of the annual PBR rate adjustment filing unless otherwise permitted.[15] Finally, in recognition that some approved Z factor applications may generate costs or savings that can be fully recovered or refunded over a single year or portion thereof, while other events will generate costs or savings requiring treatment over a longer term, the Commission held that the nature of the required Z factor rate adjustment would be considered by the Commission on a case-by-case basis.[16]

20. In accordance with this direction, ATCO Gas applied for a $4.99 million Z factor adjustment placeholder for the 2013 to 2016 period related to the Southern Alberta flood in its 2016 annual PBR rate adjustment filing.[17] The Commission declined to consider the matter in that proceeding because Proceeding 2738 was already underway, stating:

> 65. The merits of ATCO Gas's request for Z factor treatment of flood-related costs are being considered in Proceeding 2738. There are novel and potentially contentious matters that must be determined in that proceeding. On balance, the Commission considers that too much uncertainty surrounds what, if any, portion of the applied-for Z

12 Decision 2012-237, paragraph 534.
13 Decision 2012-237, paragraph 535.
14 Decision 2012-237, paragraph 540.
15 Decision 2012-237, paragraph 541.
16 Decision 2012-237, paragraph 543.
17 Proceeding 20820.

> factor amounts will be allowed to permit inclusion of a placeholder amount in the company's annual rate adjustment determination. Consequently, the Commission declines to approved a Z factor placeholder for ATCO Gas.[18]

21. The Commission has applied the principles and factors set out in Decision 2012-237 in its evaluation of ATCO Gas's application for a Z factor.

3 ATCO Gas's application

22. In June 2013, Southern Alberta experienced heavy rainfall, resulting in severe flooding along the Bow, Elbow, Red Deer and Highwood rivers. ATCO Gas submitted that the flooding damaged portions of ATCO Gas's distribution system.[19] ATCO Gas explained that its flood response consisted of three phases: (1) the initial emergency response phase; (2) the damage assessment phase; and (3) the repair and restoration phase.

23. In the initial emergency response phase, ATCO Gas addressed damaged gas mains and services that had been severed or exposed, responded to leaks and shut off the gas supply in certain areas,[20] and provided resources to Emergency Operations Centres (EOCs) in Calgary, Stoney Tribal – Saton 2, Canmore, and High River. ATCO Gas employees also responded to gas and service inquiries from customers and municipalities.[21] ATCO Gas supplied employees to man these centres from 8 a.m. to 10 p.m., providing information or assisting to dispatch service calls. ATCO Gas stated that the objective of manning the support centres was to answer any gas or service related questions customers and municipal officials had as a result of the flooding. Employees that were considered experts on gas service and able to provide information to customers to support them in their efforts to restore their gas service in a safe manner were engaged to support this first phase.

24. The emergency response phase lasted from June 20 to June 30, 2013.[22] During this period, ATCO Gas was required to turn off customers' gas supply in response to the flood emergency. This resulted in ATCO Gas experiencing lost delivery revenue in the amount of $292,617. It calculated the loss in revenue by accounting for the fixed, variable and demand revenue amount for de-energized customers for the dates the customers were de-energized during the period June 20, 2013 to December 31, 2013.[23]

25. During the damage assessment phase, ATCO Gas assessed the condition of its distribution system, made minor repairs, and implemented temporary solutions to ensure service to customers was maintained where possible.[24] ATCO Gas estimated that this second response phase lasted approximately 60 days, from July 1, 2013 to August 31, 2013.[25]

---

[18] Decision 20820-D01-2015: ATCO Gas and Pipelines Ltd., 2016 Annual Performance-based Regulation Rate Adjustment Filing, Proceeding 20820, December 21, 2015, paragraph 65.
[19] Exhibit 2738-X0003, application, paragraph 3.
[20] Exhibit 2738-X0003, application, paragraph 15.
[21] Exhibit 2738-X0003, application, paragraph 16.
[22] Exhibit 2738-X0025, AG-UCA-2015AUG14-004(a).
[23] Exhibit 2738-X0003, application, paragraph 42.
[24] Exhibit 2738-X0003, application, paragraph 18.
[25] Exhibit 2738-X0025, AG-UCA-2015AUG14-004(a).

26. During the repair and restoration phase, ATCO Gas completed permanent repairs and rebuilds on distribution infrastructure in order to restore them to pre-flood condition. ATCO Gas explained that in this phase, although some portion of the work was attributable to O&M tasks such as assessments to ensure affected areas were restored to their pre-disaster condition, the majority of the work completed was capital-related, including installing new mains to replace mains that were washed out, and replacing meters, stations and service lines.[26] Completion of this phase occurred between September 1, 2013, and the end of the third quarter of 2015.[27]

27. As stated earlier, in order to satisfy the criteria for a Z factor, the impact of the event, in this case the 2013 Southern Alberta flood, must be attributable to some event outside management's control, must be material, and must not have a significant influence on the inflation factor in the PBR formula. In addition, all costs claimed as an exogenous adjustment must be prudently incurred and the impact of the event must be unforeseen.

28. In regard to these criteria, the Commission is satisfied that the Southern Alberta flood was an unforeseen event that was outside of management's control and, on the basis of the evidence filed, that the impact of the event did not have a significant influence on the inflation factor in the PBR formula. The Commission's findings on the prudence of the costs incurred and whether the event met the materiality threshold are set out in the subsections below.

3.1 Prudence of costs

29. ATCO Gas explained that it did not track its O&M or capital costs by stage.[28] In response to an information request from the UCA, ATCO Gas provided the following summary of its O&M costs by region and year:

Table 1. O&M costs of the 2013 Alberta flood[29]

	2013				2014		
	($)				($)		($)
Group	Calgary	Foothills	Lethbridge	2013 total	Calgary	2014 total	Grand total
Field operations	1,333,353	21,574	9,876	**1,364,802**	94,383	**94,383**	**1,459,185**
Customer service	1,113,843	14,263	8,625	**1,136,731**	18,047	**18,047**	**1,154,778**
Information technology	62,071			**62,071**			**62,071**
Customer care and billing	60,857			**60,857**			**60,857**
Lost revenue				**214,282**			**214,282**

26 Exhibit 2738-X0003, application, paragraph 19.
27 Exhibit 2738-X0025, AG-UCA-2015AUG14-004(a).
28 Exhibit 2738-X0025, AG-UCA-2015AUG14-004(c).
29 Exhibit 2738-X0025, AG-UCA-2015AUG14-001(a)-(b).

30. ATCO Gas also provided a summary of its capital costs in Schedule 2 of its application:

Table 2. Z factor calculation mid-year rate base of the 2013 Alberta flood ($000)

	Net rate base	Capital expenditures	CWIP	(To)/from CWIP	Net capital addition	Depreciation capitalized	Depreciation expense	Removal	Salvage	Contribution additions	Amortization of contributions	Net rate base	Mid-year rate base
2013	-	2,159	816	(816)	1,343	-	20	255	-	24	-	1,554	777
2014	1,554	4,229	186	630	4,859	-	113	310	-	534	9	6,085	3,820
2015	6,085	810	-	186	996	-	201	50	708	-	16	6,238	6,162
2016	6,238	-	-	-	-	-	216	-	-	-	16	6,038	6,138
2017	6,038	-	-	-	-	-	216	-	-	-	16	5,838	5,938
Per Table 2		**7,198**							**708**	**558**			

Commission findings

31. ATCO Gas incurred $1.46 million in field operations costs due to the vast area affected by the flood and the need to repair the mains, meters, pressure control stations and services that were damaged. ATCO Gas also incurred $1.15 million in customer service costs because of the need to ensure that gas was being safely delivered into customers' homes, and the requirement to visit some homes on multiple occasions.[30]

32. With regard to the O&M costs that have been claimed, the Commission is persuaded by the evidence that ATCO Gas responded to the flood in a measured and staged approach and that it was diligent in returning service to its customers at the earliest opportunity. ATCO Gas completed its second stage (damage assessment) by September 1, 2013, slightly more than two months after the flood occurred. The Commission is satisfied that the timing of these activities, the scope of the work completed, and the O&M costs incurred in response to this event, to enable service to be restored to pre-flood conditions following the event, were reasonable. The Commission therefore concludes that the O&M costs claimed as an exogenous adjustment were prudent.

33. The Commission has also reviewed the capital costs incurred by ATCO Gas in response to this event. ATCO Gas completed nearly 90 per cent of its infrastructure repair and replacement by the end of 2014.[31] The Commission finds the scope of the work performed and timing of the repair and replacement activity to be reasonable. The quantum of the capital costs has also been reviewed by the Commission. The majority of the costs were incurred to restore damaged mains and, by the end of 2014, ATCO Gas had completed 40 individual mains restoration projects.[32] Further, the Commission notes that the two most expensive mains replacement projects (17th Ave. SE and Siksika-Bow River SW) both involved replacing mains which crossed rivers. Replacing river-crossing mains clearly adds a level of difficulty and therefore increased costs. The Commission finds the quantum of capital costs incurred by ATCO Gas in response to this event to be reasonable.

30 Exhibit 2738-X0001, application, paragraph 38.
31 ($2,159,000 + $4,229,000)/$7,198,000 = 89 per cent.
32 Exhibit 2738-X0001, application, paragraph 46.

34. ATCO Gas deducted both government contributions and insurance proceeds in the amounts of $557,883 and $707,646 respectively, from its capital costs. ATCO Gas also stated that it applied for all financial aid available.[33]

35. Accordingly, the Commission is satisfied, based on the evidence before it, that the capital costs incurred by ATCO Gas in response to the event were prudently incurred.

3.2 Lost revenue

36. In addition to the capital and O&M costs claimed, ATCO Gas also applied to recover $214,282 as lost revenue.[34] ATCO Gas calculated this lost revenue by accounting for the fixed, variable and demand revenue amount for de-energized customers, for the dates the customers were de-energized during the period June 20, 2013 to December 31, 2013.[35] ATCO Gas chose to waive the first month of fixed charges for customers that were affected by the flood, at a total cost of $78,335, and did not include this cost in its claim.

37. The UCA opposed ATCO Gas's claim for lost revenue, arguing that the event would qualify as *force majeure* under ATCO Gas's terms and conditions for distribution service (T&Cs). As a result, ATCO Gas would have been permitted the interruption or reduction of service to customers during the event.[36] The UCA further contended that, under both PBR and cost-of-service regulation, ATCO Gas would not be entitled to a guarantee of its forecast revenue. The UCA noted that ATCO Gas proposed to allocate the lost revenue to all ATCO Gas customers, including the affected customers, through the inclusion of the lost revenue in this Z factor application. The UCA stated that ATCO Gas had not filed evidence that the affected customers were unable or unwilling to pay their bills during this period.

38. The UCA also noted that the affected customers were still enrolled with a retailer during this time period and that the total number of service accounts was therefore unaffected.[37]

39. ATCO Gas responded that Decision 2012-237 does not state that the companies operating under the PBR regime are limited to recovering only capital and O&M costs in a Z factor application. Rather, companies are entitled to apply for recovery of the total impact related to the exogenous event. It argued that the UCA failed to provide any evidence indicating that the applied-for amounts were not the direct result of the flood.[38]

40. ATCO Gas also disputed the UCA's assertion that it did not provide service during this period. As set out in its evidence,[39] ATCO Gas continued to provide distribution service to these customers through repeated site visits and monitoring of the systems serving these premises. ATCO Gas was providing service to its customers and reacting prudently by shutting off customers where there was any potential risk of a gas leak, restoring customer service when it was safe to do so, and closely monitoring all segments of its distribution system to ensure continued safe and reliable operations.

[33] Exhibit 2738-X0018, AG-AUC-2015AUG14-002(e).
[34] Exhibit 2738-X0001, application, Table 1, page 10.
[35] Exhibit 2738-X0001, application, paragraph 42.
[36] Exhibit 2738-X0031, UCA evidence of Mr. Shymanski.
[37] Exhibit 2738-X0031, UCA evidence of Mr. Shymanski.
[38] Exhibit 2738-X0038, ATCO Gas rebuttal evidence, paragraph 6.
[39] Exhibit 2738-X0038, ATCO Gas rebuttal evidence, paragraph 7.

41. Finally, ATCO Gas stated that invoking a force majeure claim with its retailers, assuming such a claim would have been possible, would not have resulted in savings to customers or had an impact on its Z factor claim:

> As the retailer is responsible for billing customers, ATCO Gas's distribution charges are collected from the retailer who in turn will collect it from customers. ATCO Gas does not pay for this arrangement so declaring Force Majeure (assuming it was even possible) would not save any money. Moreover, as ATCO Gas and the retailers continued to provide services throughout the flooding event a Force Majeure claim was not available to ATCO Gas.[40]

Commission findings

42. A Z factor allows for an adjustment to a company's rates to account for the significant financial impact of an event outside of the control of management. The event must not have an economy-wide impact, otherwise the cost of that impact would be reflected and recovered in the I factor. As stated in Decision 2012-237, "… Providing the company with additional revenues through a Z factor adjustment in circumstances where the event has economy-wide impacts would result in a double-counting of the impact of the exogenous event."[41]

43. The concern with double-recovery reflects an understanding that the Z factor is not restricted to recovery of replacement costs and operating costs but can also include revenues that would have otherwise been earned but for the event.

44. The Commission is persuaded by ATCO Gas's evidence that ATCO Gas was still performing its duties as a utility service provider during the flood event. Moreover, the Commission considers that utility service activity would have likely increased due to the need to restore service and monitor system operation as the flood waters receded. Consequently, the Commission concludes that even if ATCO Gas had attempted to invoke a force majeure claim with its retailers, which on the facts may not have been possible, doing so would not have resulted in savings to customers or otherwise had an impact on the ATCO Gas's Z factor request.

45. Although there is no guarantee of forecast revenue under either a PBR framework or cost-of-service regulation, the Commission accepts ATCO Gas's evidence that it lost $214,282 of revenue due to the Southern Alberta flood. ATCO Gas continued to perform its duties as a gas service provider and, but for the flood, would have received revenues from its customers. Accordingly, the revenue lost as a result of the flood, as calculated by ATCO Gas in the amount of $214,282, is eligible for inclusion in the calculation of the Z factor materiality threshold calculation, and is recoverable if the materiality threshold is achieved.

3.3 Materiality

46. In Decision 2012-237, the Commission approved a Z factor materiality threshold as the dollar value of a 40 basis points change in after-tax ROE calculated with the company's equity, which was used to determine the revenue requirement for ATCO Gas's 2012 going-in rates. The threshold is to be adjusted annually by the I-X index.[42]

---

[40] Exhibit 2738-X0038, ATCO Gas rebuttal evidence, paragraph 9.
[41] Decision 2012-237, paragraph 519.
[42] Decision 2012-237, paragraph 535.

47. ATCO Gas's 2013 materiality threshold is $1.187 million. This threshold was approved in the ATCO Gas 2013 capital tracker true-up,[43] for the purposes of its K factor calculation, which uses the same 40 basis point ROE methodology for its calculation.

48. As noted above, ATCO Gas's applied-for Z factor adjustment is $5.662 million. In assessing the Z factor adjustment against the materiality threshold, ATCO Gas compared its total proposed Z factor adjustment of $5.662 million to the 2013 materiality threshold of $1.187 million.[44]

49. The UCA opposed ATCO Gas's approach and requested, through an information request (IR), that ATCO Gas provide a reference to a Commission decision that indicates a utility can apply a Z factor materiality threshold over multiple years, and that an earnings impact calculated over multiple years can be used to meet a single year's materiality threshold. ATCO Gas responded:

> In Decision 2012-237, paragraph 543, the Commission indicated that Z factor costs may require treatment over multiple years.
>
> > "The Commission recognizes that some approved Z factor applications may generate costs or savings that can be fully recovered or refunded over a single year or portion thereof while other events will generate costs or savings requiring treatment over a longer term. The nature of the required Z factor rate adjustment will be considered by the Commission on a case-by-case basis."
>
> This event was an exogenous event which is not included in going-in rates and/or Capital Trackers. The 2013 Southern Alberta floods was a single event that occurred in 2013 that has a multi-year impact. The Commission is clear in Decision 2012-237 that the materiality threshold is to be applied on an event-by-event basis. Therefore the materiality threshold should apply to the impact of the entire event, not just the impact in one year.[45]

50. At the request of the UCA, ATCO Gas subsequently provided the 40 basis point materiality thresholds for the years 2014 to 2017 and a breakdown of the $5.662 million in Z factor adjustment costs on an annual basis.[46]

51. The UCA filed evidence on this issue. Mr. Shymanski, on behalf of the UCA, proposed two alternatives to determine the Z factor materiality threshold. In the first alternative, he proposed that materiality be measured on an annual basis by comparing the costs incurred each year over the five-year time period with the earnings impact for each year, to determine whether the materiality threshold has been achieved each year. Applying this alternative, ATCO Gas's applied-for Z factor would only achieve the materiality threshold in 2013.[47] The earnings impact for each year are as follows:

43 Decision 3267-D01-2015: ATCO Gas and Pipelines Ltd., 2013 PBR Capital Tracker Refiling and True-up and 2014-2015 PBR Capital Tracker Forecast, Proceeding 3267, Application 1610634-1, March 19, 2015.
44 Exhibit 2738-X0001, application, paragraph 10.
45 Exhibit 2738-X0025, AG-UCA-2015AUG14-008(a)-(b).
46 Exhibit 2738-X0025, AG-UCA-2015AUG14-008(c)-(d).
47 Exhibit 2738-X0031, UCA evidence of Mr. Shymanski, page 20.

Table 3. Z factor calculation

	2013	2014	2015	2016	2017	Total
	($000)					
Total Z factor	**3,121**	**517**	**677**	**682**	**665**	**5,662**
Annual materiality	*1,187*	*1,206*	*1,224*	*1,242*	*1,261*	

52. In Mr. Shymanski's view, this approach would be similar to how K factor calculations and their associated materiality test are applied under the capital tracker framework set out by the Commission in Decision 2013-435.[48] For a multi-year capital project, the K factor materiality threshold is applied annually to the incremental revenue requirement amount determined by the capital tracker accounting test. Accordingly, for a utility to receive funding in a given year for a capital tracker, the K factor amount must exceed the materiality threshold in that year. Mr. Shymanski stated that he supported this proposal.

53. In the second approach suggested by Mr. Shymanski, he would assess the Z factor materiality on a cumulative annual basis, but the total Z factor adjustment amount would have to exceed the sum of the materiality limits for 2013 to 2017.[49] If this approach were adopted, Mr. Shymanski noted that the sum of the 2013 to 2017 Z factor materiality thresholds would be $6.12 million.[50] Accordingly, he argued the materiality threshold would not have been met using the second approach proposed by the UCA.

54. In its rebuttal evidence, ATCO Gas noted that in paragraph 534 of Decision 2012-237, the Commission stated that the Z factor materiality threshold "… should apply to each event unless otherwise permitted in exceptional circumstances," which, ATCO Gas argued supported its position that materiality should be assessed as a singular threshold rather than multiple thresholds over multiple years.[51] ATCO Gas added that in Decision 2012-237, the Commission acknowledged that a Z factor may generate costs or savings over multiple years[52] and that "… the Commission did not require the materiality threshold to be applied or met in each and every year of a single Z Factor event."[53]

55. ATCO Gas further submitted that given the nature of the capital costs included in its Z factor application, the capital expenditures incurred in a single year have a revenue requirement associated with them in future years for return, tax, and depreciation.[54] It added that if materiality were to be assessed on an annual basis, the timing of the exogenous event which triggers a Z factor would play a role in determining whether it would qualify as such. By way of example, if an event occurred in January of a given year, the event would more likely exceed the annual materiality threshold than would an event which occurs later in the year.[55]

48 Decision 2013-435: Distribution Performance-Based Regulation, 2013 Capital Tracker Applications, Proceeding 2131, Application 1608827-1, December 6, 2013.
49 Exhibit 2738-X0031, UCA evidence of Mr. Shymanski, page 20.
50 Exhibit 2738-X0031, UCA evidence of Mr. Shymanski, page 21.
51 Exhibit 2738-X0038, ATCO Gas rebuttal evidence, paragraph 21.
52 Decision 2012-237, paragraph 535.
53 Exhibit 2738-X0038, ATCO Gas rebuttal evidence, paragraph 22.
54 Exhibit 2738-X0038, ATCO Gas rebuttal evidence, paragraph 26.
55 Exhibit 2738-X0038, ATCO Gas rebuttal evidence, paragraph 27.

56. The CCA argued that the use of a single year materiality threshold to assess the materiality of an event that results in costs over multiple years should be questioned.[56] With respect to the UCA's recommended first alternative materiality approach, the CCA stated strict annual thresholds could result in a utility being "punished" for choosing to defer capital expenditures past the year in which an exogenous event occurred.[57] Instead, the CCA noted that a utility may be encouraged to "ramp up expenditures" in a single year to complete projects, thereby potentially harming customers.[58]

57. The CCA also questioned the second alternative proposed by the UCA and stated that this approach may result in a utility being unable to recover the costs related to an event that would otherwise qualify for Z factor treatment, because if the costs of an event spilled over into the next year, approximately $1.2 million would be added to the cumulative materiality threshold.[59]

58. The CCA instead proposed a materiality threshold approach that employed an arithmetic average of the annual materiality thresholds calculated and used to assess the materiality of the entire potential Z factor adjustment amount. This approach was suggested because it may help to assess the costs of a one-time event with a multi-year cost impact. The CCA provided a calculation on an average materiality threshold in its argument.[60]

59. Overall, the CCA noted that the composition of the Z factor adjustment amount was the primary consideration:

> Therefore the CCA still consider the first determination must be made to verify if the total amount claimed is proper. This can only be done by analysis of the sum of all appropriate parts. Clearly this application is the correct place to address the issue of the amount and provide input into determination of the mechanics of an appropriate materiality threshold; but only after all constituent parts are assessed can the materiality mechanics be defined.[61]

60. With respect to ATCO Gas's proposed materiality threshold approach, the UCA explained that adoption of that approach would be contrary to the "relatively high threshold"[62] which was put forth by the Commission and recommended the Commission maintain a relatively high threshold for Z factor materiality by not assessing the multi-year cost of an exogenous event against a materiality threshold for a single year.[63]

Commission findings

61. In Decision 2012-237, the Commission established Z, Y and K factors to recognize that certain prudently incurred costs may not be recoverable through the I-X mechanism. However, the Commission recognized that the application of the Z, Y and K factor adjustments must be limited in scope because adjustments of this nature have the effect of lessening the efficiency

---

56 Exhibit 2738-X0042, CCA argument, paragraph 44.
57 Exhibit 2738-X0042, CCA argument, paragraph 40.
58 Exhibit 2738-X0042, CCA argument, paragraph 40.
59 Exhibit 2738-X0042, CCA argument, paragraph 42.
60 Exhibit 2738-X0042, CCA argument, paragraphs 45-46.
61 Exhibit 2738-X0042, CCA argument, paragraph 49.
62 Decision 2012-237, paragraph 534.
63 Exhibit 2738-X0041, UCA argument, paragraph 102.

incentives that are central to a PBR plan. This is why the Commission established materiality thresholds for Z and K factors.

62. Accordingly, a Z factor adjustment should only be permitted when it is determined that the impact of an event that is outside of management's control has had a sufficiently significant impact on the operation of the company, so that the costs of the event cannot be reasonably recovered through the revenues provided under the I-X mechanism. Consequently, the Commission approved a Z factor materiality threshold as the dollar value of a 40 basis points change in after-tax ROE used to determine the revenue requirement for the company's going-in rates. The materiality threshold is then adjusted annually by the I-X index.

63. Given that the Z factor materiality threshold is established on the basis of ROE, which is measured on an annual basis, and the materiality threshold is adjusted on an annual basis, and recognizing that the I-X is also adjusted annually, the Commission finds that the Z factor materiality threshold should be applied on an annual basis. This is consistent with the regime established for the K factor, whereby the accounting test and the materiality thresholds are applied on an annual basis.

64. In the case of ATCO Gas, the 2013 materiality threshold is $1,187,000, which is then escalated by I-X every year. Because the Commission has previously found these cost amounts to be prudent, the recovery of a Z factor cost in the amount of $3,121,000 for 2013 is approved. The breakdown of the Z factor amount of $3,121,000 is detailed in the table below:[64]

Table 4. 2013 Z factor detail

	($000)
Revenue requirement – capital	75
O&M and lost revenue	2,839
Carrying charges	207
Total Z factor	3,121

65. As seen in the table below, applying the annually adjusted 2013 materiality threshold for each of 2014 to 2017 to the cost impact for each of the same years indicates that the materiality threshold has not been met for any of those subsequent years. Consequently, the Commission denies Z factor treatment for the flood-related costs incurred in each of 2014 to 2017.

Table 5. Z factor calculation[65]

	2013	2014	2015	2016	2017	Total
	($000)					
Total Z factor	**3,121**	**517**	**677**	**682**	**665**	**5,662**
Annual materiality	*1,187*	*1,206*	*1,224*	*1,242*	*1,261*	

66. Last, the Commission notes that the 2013 cost of $3,121,000 includes carrying charges in the amount of $207,000. The awarding of carrying charges in this instance is warranted, because ATCO Gas would have self-financed both the capital and O&M portion of these costs as they

64 Exhibit 3738-X0031, A8.
65 Exhibit 2738-X0025, AG-UCA-2015AUG14-008 attachment.

were incremental to other costs embedded in going-in rates. Further, the requirements of Rule 023[66] have also been satisfied in this case.[67]

67. With regard to the capital-related costs incurred in the years 2014 to 2017, which have not been approved for Z factor treatment, the determination of the Commission in this decision does not preclude ATCO Gas from bringing forward an application for additional funding for these capital costs by way of a K factor, provided the Commission's criteria for capital tracker treatment are satisfied.

4 Depreciation

68. As a result of the flood, ATCO Gas removed and replaced damaged assets from its distribution system. By way of IRs to ATCO Gas, the Commission sought to clarify whether the removal of those damaged assets should be considered an extraordinary retirement as classified by the Uniform Classification of Accounts for Gas Utilities (UCAGU). Specifically, the UCAGU states that an extraordinary retirement is one "from causes not reasonably assumed to have been anticipated or contemplated in prior depreciation or amortization provisions."[68]

69. As determined by the Commission in Decision 2013-417,[69] the Utility Asset Disposition (UAD) decision, assets that are no longer used to provide utility service as a result of extraordinary circumstances must be removed from rate base when they cease to provide service, regardless of whether they have been fully depreciated. The risk that they may not be fully depreciated is to be borne by the utility and its shareholders, not ratepayers. If, however, the asset retirement is considered to be ordinary, the under-recovery or over-recovery of capital investment are for the account of customers under the amortization of reserve differences.[70]

70. In response to a Commission information request, ATCO Gas stated that the retirement of assets damaged by the flood should not be considered extraordinary given the definition provided, and referenced above, in the UCAGU. ATCO Gas explained that two prior events, the 2005 Southern Alberta flood and the 1987 tornado, resulted in destroyed asset retirements that were included in ATCO Gas's past depreciation studies.[71] A copy of ATCO Gas's 2009 depreciation study prepared by Gannett Fleming Inc. was provided and ATCO Gas noted that:

> ATCO Gas has identified two major events - the 2005 Southern Alberta floods as well as the 1987 tornado – which caused assets to be retired in the ordinary course which were included in the historical data provided to Gannett Fleming for purposes of determining the depreciation parameters in above noted depreciation study. Neither event was specifically identified and removed in the depreciation study. As the assets retired as a result of these two events were not excluded from past studies, ATCO Gas did consider previous retirements of the same type, nature and characteristics as the 2013 Southern Alberta floods in its prior depreciation studies.[72]

66 Rule 023: *Rules Respecting Payment of Interest*.
67 Regulatory lag has been greater than 12 months and the revenue impact is greater than $1,000,000.
68 UCAGU, Section 8, page 9.
69 Decision 2013-417: Utility Asset Disposition, Proceeding 20, Application 1566373-1, November 26, 2013.
70 Decision 2013-417, paragraph 304.
71 Exhibit 2738-X0018, AG-AUC-2015AUG14-005(a).
72 Exhibit 2738-X0018, AG-AUC-2015AUG14-005(b).

71. At the request of the Commission, ATCO Gas filed the net book values (NBV) and replacement costs from the 2013 flood, the 2005 flood and the 1987 tornado, while noting that the definition of an extraordinary retirement "makes no reference to the replacement cost of the assets as being a determining factor."[73]

Table 6. NBV and replacement costs associated with the 2013 and 2005 floods, and the 1987 tornado[74]

Event	NBV of retired assets	Replacement costs of retired assets
	($)	
2013 Southern Alberta flood[75]	496,747	5,932,969
2005 Southern Alberta flood	210,933	2,066,561
1987 Alberta tornado	57,108	253,345

72. ATCO Gas, by way of its IR responses to the Commission, further explained the factors by which the UCAGU examines an extraordinary retirement:

> … it should be noted that the definition of an Extraordinary Retirement as provided in the Uniform Classification of Accounts makes no reference to the replacement cost of the assets as being a determining factor. Rather, it focuses on whether the retirement of the assets no longer used or required to be used for utility service would unduly deplete or inflate the accumulated depreciation accounts associated with these assets. ATCO Gas can confirm that is not the case with regard to the 2013 Southern Floods, as demonstrated by the table below which provides the historical costs of the assets retired and the balance in the Accumulated Depreciation account prior to those retirements by asset account. In aggregate, the costs in question represent less than one-tenth of one percent (0.09%) of the aggregate accumulated depreciation for all affected asset groups…[76]

73. Furthermore, in an IR response to the UCA, ATCO Gas explained:

> The damaged/destroyed assets have been retired in the ordinary course of business. As such, the assets have been assumed to be fully depreciated and their retirement has no impact on ATCO Gas's rate base value.[77]

74. ATCO Gas further discussed whether the impact of the asset retirements was considered in this application or Proceeding 20604, the ATCO Gas 2014 true-up and 2016-2017 capital tracker proceeding:

> Although the retirement of the assets themselves has no impact on the rate base value, the reduction to the original cost of the assets as a result of the retirement does result in a reduction to depreciation expense. For the Capital Tracker Applications, ATCO Gas has identified the Alberta Floods as a separate program in the continuity schedules of the

73 Exhibit 2738-X0018, AG-AUC-2015AUG14-005(c).
74 Exhibit 2738-X0018, AG-AUC-2015AUG14-005(c).
75 Exhibit 2738-X0018, AG-AUC-2015AUG14-004(c). ATCO Gas noted that this is an estimated NBV given that the assets are depreciated within a mass property account. Furthermore, ATCO Gas is not seeking recovery of the NBV through the Z factor, rather the NBV are dealt with through the amortization of reserve differences.
76 Exhibit 2738-X0018, AG-AUC-2015AUG14-005(c).
77 Exhibit 2738-X0025, AG-UCA-2015AUG14-010(b)-(c).

> accounting test. This ensures there is no double-counting of capital expenditures between the 2013 Southern Alberta Floods and any of ATCO Gas's other capital programs. The reduction in depreciation expense as a result of the retirements however, would be shown in the program(s) where the original assets would have originally resided. Therefore, although ATCO Gas is requesting the recovery of depreciation on the replacement assets through this Z Factor Application, it is also showing a reduction in depreciation expense for the retired assets through the accounting test included in the capital tracker applications.[78]

75. On behalf of the UCA, Mr. Shymanski filed evidence on the treatment of the retired assets resulting from the 2013 flood. He recommended that the Commission determine that the assets retired due to the flood be considered extraordinary retirements and consequently, that any undepreciated costs associated with those assets be the responsibility of the shareholders of ATCO Gas.[79] Mr. Shymanski submitted that although ATCO Gas was asked by way of an IR for details from its last depreciation study that would indicate a flood event was contemplated, ATCO Gas had not provided any indication that an event like the 2013 flood was contemplated and the depreciation study provided had "… no reference to a flood of the magnitude of the 2013 event nor the two other events [the 1987 tornado and 2005 flood] listed by ATCO Gas in the study."[80]

76. Mr. Shymanski further stated that the replacement costs of the damaged assets associated with the 2013 flood were more than double the 2005 damaged asset replacement costs, and 23 times the replacement costs of assets damaged by the 1987 tornado. He did not consider the 1987 tornado or the 2005 flood events to be similar to the 2013 flood and stated the remaining NBV should be to the account of the shareholders.[81]

77. In its rebuttal evidence, ATCO Gas responded to Mr. Shymanski's statements that the 1987 tornado and 2005 flood were not referenced in the last depreciation study, stating:

> … assets affected by the 2005 Southern Alberta floods as well as the 1987 tornado were retired in the ordinary course which was included in the historical data provided to Gannett Fleming for purposes of determining the depreciation parameters in the last Depreciation Study of ATCO Gas. As such, neither event was specifically identified for exclusion in the Depreciation Study.[82]

78. Furthermore, with respect to Mr. Shymanski's comparison of the replacement costs associated with damaged assets resulting from the 1987, 2005 and 2013 events, ATCO Gas stated that replacement costs of an asset are not included in the UCAGU's definition of an extraordinary retirement:

> An extraordinary retirement results in a loss (or gain) to the extent that the net charges (or credits) would unduly deplete (or inflate) the accumulated depreciation or amortization accounts. A loss (or gain) is comprised of the differences between plant ledger value plus

78 Exhibit 2738-X0025, AG-UCA-2015AUG14-12(d).
79 Exhibit 2738-X0031, UCA evidence of Mr. Shymanski, paragraph A27, page 21.
80 Exhibit 2738-X0031, UCA evidence of Mr. Shymanski, paragraph A31, page 27.
81 Exhibit 2738-X0031, UCA evidence of Mr. Shymanski, paragraph A31, pages 28-29.
82 Exhibit 2738-X0038, ATCO Gas rebuttal evidence, paragraph 35.

> cost of removal less salvage and insurance recoveries and the related depreciation or amortization determined in an equitable manner.[83]

79. ATCO Gas reiterated its position that the assets retired as a result of the 2013 flood did not unduly deplete the accumulated depreciation accounts and, consequently, nothing further should be required. Mr. Shymanski did not provide evidence to support his position that the amount of NBV and replacement costs of damaged assets should determine whether an event is considered extraordinary. Further, Mr. Shymanski did not consider asset vintage or inflation when examining the costs of replacing the assets across the three events.[84]

80. ATCO Gas also filed the rebuttal evidence of Mr. Kennedy of Gannet Fleming, who prepared the previous ATCO Gas depreciation study in 2009 for its 2011 and 2012 general rate application (GRA). Mr. Kennedy stated that for the 2009 depreciation study, the average service life estimates included "all of the prior storm related retirements" and that no retirements were removed from the depreciation data used in that study.[85] The following empirical tests, the results of which were attached as appendices to his rebuttal evidence, were also conducted by Mr. Kennedy to assess whether the 2013 flood was considered in the 2009 depreciation study:

> Using the retirement database used for the Depreciation Study filed in AG's 2011-2012 GRA, I layered the aged retirements from the 2013 Southern Alberta Floods to the retirement database and assumed that they occurred in 2009. My objective was to determine if the actual 2013 Southern Alberta Floods were a known event for AG's 2011-2012 GRA, would they have affected the depreciation results for both the actuarial observed life table and resulting observed life table curve. This was done for AG's three largest accounts affected by the 2013 Southern Alberta Floods (i.e. Services - Account 47300, Mains – Account 47500, and Meter Equipment Electronic – Account 47801).
>
> …
>
> The results indicate very minimal change in the observed life table (i.e. "PCT SURV BEGIN OF INTERVAL") values for the revised results compared to the original results for all three accounts. In addition, I plotted the "Original" curve to the "Revised" curve for a visual effect of the change from layering the 2013 Southern Alberta Floods to the original 2009 database. Please see attached Appendix 2. The results are almost indistinquishable [*sic*] between the original and revised databases. Based on this analysis and results, it is clear that if the events of the 2013 Southern Alberta Floods were known for AG's previous depreciation study, their life parameter effect on the depreciation parameter recommendation would have been nil.[86]

81. Mr. Kennedy concluded that the 2013 flood retirements were a result of a force of nature that had been considered in the 2009 depreciation study and that it was not necessary to consider the replacement costs of the assets in establishing the depreciation parameters in his analysis, and accordingly, the retirements should be considered ordinary.[87]

---

[83] UCAGU, Section 8.
[84] Exhibit 2738-X0038, ATCO Gas rebuttal evidence, paragraphs 41-43.
[85] Exhibit 2738-X0037, rebuttal evidence of Mr. Kennedy, paragraph 7.
[86] Exhibit 2738-X0037, rebuttal evidence of Mr. Kennedy, paragraph 8.
[87] Exhibit 2738-X0037, rebuttal evidence of Mr. Kennedy, paragraph 9.

82. The UCA argued that the evidence provided by Mr. Kennedy as part of ATCO Gas's rebuttal evidence was new evidence and "wholly inappropriate" to be submitted at the time of rebuttal evidence.[88] The UCA stated that it had asked an IR to ATCO Gas to provide any documents that showed the flood was contemplated in the depreciation study and that had Mr. Kennedy's analysis been provided during the IR stage, the UCA could have responded in its evidence or requested additional IRs. The UCA asked the Commission to strike the evidence from the record of this proceeding.[89]

83. Notwithstanding this request, in response to Mr. Kennedy's evidence that the two prior storm events were considered in the depreciation study, the UCA submitted:

> For example, if Mr. Kennedy had been specifically aware of the two prior storm related events - the 1987 Edmonton tornado and the 2005 Southern Alberta flood - as he suggests, he could, and perhaps should, have applied his novel methodology to separately test if these events would have had an impact on historical results in the last depreciation study. However, there is no indication that Mr. Kennedy separately identified or considered these storm related events. Instead, he now simply states, with no independently verifiable proof, that the prior storm related retirements must have been included in the last depreciation study as they were not specifically excluded.[90]

84. The UCA further argued that even if it were to accept that the 1987 tornado and 2005 flood events were included in the depreciation study, that would not be determinative of the issue. It quoted excerpts from Decision 2014-297 (Errata) (Slave Lake decision),[91] which considered whether retirements resulting from fires in Slave Lake were considered extraordinary in the case of ATCO Electric Ltd. The UCA referenced paragraph 66 of Decision 2014-297 (Errata) where the Commission found that:

> In the Commission's view it is the characteristics of the event that are relevant to the determination of whether the event had been contemplated or anticipated by a prior depreciation study. If the characteristics of the Slave Lake fires event are sufficiently different to distinguish the Slave Lake fires from the events considered in the previous depreciation study such that the characteristics of the Slave Lake fires cannot be said to have been reasonably contemplated or anticipated in the determination of the depreciation parameters in that study, then the Commission would consider the event to give rise to an extraordinary retirement and the $400,000 notional net book value of the destroyed assets would be for the account of the shareholders.

85. The UCA explained that Mr. Shymanski outlined in his evidence how the characteristics of the 2013 flood differed from the previous 1987 tornado and 2005 flood events in comparing the magnitude of the NBV of the retired assets across the three events, as well as the amount of replacement costs associated with the retired assets.[92] The UCA argued that the magnitude of the NBV and replacement costs are relevant given the Commission's prior decisions on extraordinary retirements:

88 Exhibit 2738-X0041, UCA argument, paragraphs 117-118.
89 Exhibit 2738-X0041, UCA argument, paragraph 119.
90 Exhibit 2738-X0041, UCA argument, paragraph 121.
91 Decision 2014-297 (Errata): ATCO Electric Ltd. 2012 Distribution Deferral Accounts and Annual Filing for Adjustment Balances, January 8, 2015.
92 Exhibit 2738-X0041, UCA argument, paragraph 125.

> For example, in Decision 2014-297, the Commission explicitly considered the amounts which had previously been charged by ATCO Electric Ltd. to its Reserve for Injuries and Damages ("RID") account in respect to storm related events, some or all of which represented replacement costs, as a critical part of its determination that the retirements in issue were in fact extraordinary. Regardless of the definition of extraordinary retirement under the UCAGU, it is clear that the Commission considers replacement costs relevant to its assessment of any potential stranded assets.[93] [footnotes removed]

86. The UCA further argued that the UCAGU definition of an ordinary retirement resulting from "causes reasonably assumed to have been contemplated in prior depreciation provisions, and normally may be expected to occur when plant reaches the end of its expected service life" implies that the NBV of the assets being retired is relevant given that they represent the remaining undepreciated costs.[94]

87. In summary, the UCA stated that ATCO Gas had not provided independently verifiable evidence that the 2013 flood had been contemplated in the depreciation study. Furthermore, it was the view of the UCA that the characteristics of the 2013 flood were markedly different from the prior events and could not have been reasonably contemplated in the depreciation study. The UCA also submitted that ATCO Gas could not have it both ways. That is, it could not insist that the flood was an unforeseen event for the purposes of meeting the Z factor criteria and at the same time argue that this was an ordinary retirement event. Accordingly, the UCA recommended that the asset retirements associated with the 2013 flood be considered extraordinary retirements and to the account of the shareholders.[95]

88. In its reply argument, ATCO Gas opposed the UCA's request that Mr. Kennedy's rebuttal evidence be struck from the record of this proceeding. It argued that because Mr. Shymanski filed intervener evidence on the depreciation study, it should be permitted to submit evidence in response. In addition, ATCO Gas indicated that Mr. Kennedy's rebuttal evidence was provided to corroborate ATCO Gas's IR responses that the depreciation study had considered the 2005 flood. Because Mr. Kennedy had authored the 2009 depreciation study, he was able to independently confirm that the 1987 and 2005 events were included in that study. ATCO Gas submitted that the UCA's request to strike the evidence should be disregarded.[96]

89. The CCA did not comment on the issue of depreciation in its argument and reply argument.

Commission findings

90. The Commission will not strike the rebuttal evidence of Mr. Kennedy from this proceeding. It was the Commission that raised the issue of depreciation through its interrogatories to ATCO Gas because the treatment of these assets is a matter to be considered by it. In pursuing this issue, the Commission must ensure that it has the best information before it, which in this case includes the evidence of Mr. Kennedy, who authored ATCO Gas's 2009 depreciation study. ATCO Gas should have been alerted to this matter and included depreciation evidence in its initial application and its failure to do so may have procedurally disadvantaged

---

93 Exhibit 2738-X0041, UCA argument, paragraph 130.
94 Exhibit 2738-X0041, UCA argument, paragraph 131.
95 Exhibit 2738-X0041, UCA argument, paragraphs 134-136.
96 Exhibit 2738-X0048, ATCO Gas reply argument, paragraphs 29-31.

the UCA. However, the Commission does not consider that the public interest would be served by excluding relevant evidence solely for procedural reasons. If the UCA had wanted to file additional information or seek the opportunity to ask further questions on Mr. Kennedy's evidence, it could have brought forward a motion for this relief.

91. With regard to the assessment of whether the retirement of these assets is in the normal course, the Commission is persuaded by the evidence of ATCO Gas and Mr. Kennedy that the 2009 depreciation study included the impact of the 2005 flood and the 1987 tornado events.

92. The facts of this case are distinguishable from those in the Slave Lake decision that led to the Commission finding that the "fires could not reasonably have been anticipated or contemplated in the determination of the parameters used in the previous depreciation study dated as at December 31, 2008" and that "for regulatory purposes the Slave Lake fires give rise to an extraordinary retirement of the destroyed assets." As set out by the Commission in the Slave Lake decision:

> 66. … it is the characteristics of the event that are relevant to the determination of whether the event had been contemplated or anticipated by a prior depreciation study. If the characteristics of the Slave Lake fires event are sufficiently different to distinguish the Slave Lake fires from the events considered in the previous depreciation study such that the characteristics of the Slave Lake fires cannot be said to have been reasonably contemplated or anticipated in the determination of the depreciation parameters in that study, then the Commission would consider the event to give rise to an extraordinary retirement.[97]

93. In the Slave Lake decision, the Commission reviewed the history of losses experienced by ATCO Electric over a 10-year period and determined that the nature of these past losses, which generally involved costs in the range of $1 million to $2 million, were sufficiently different from the Slave Lake region fire which required replacement costs of assets of $23.7 million. In this proceeding, the Commission finds that the characteristics of the 2013 flood event are of a similar nature to the 2005 flood event that was incorporated in the 2009 depreciation study. Relying on this finding of fact, the Commission concludes that the 2013 flood does not give rise to an extraordinary retirement of the destroyed assets and therefore the undepreciated net book value of $496,747 will continue to be recovered from ratepayers.

94. Lastly, in response to the argument that an ordinary retirement event for the purposes of depreciation does not meet the unforeseen impact criteria for a Z factor, the Commission finds that these are two distinct matters. A depreciation study is developed to predict retirements of a group of assets over their life on the basis of past retirement events. That past events have been incorporated into depreciation studies does not negate the impact of the actual event on the operations of the company. While a storm may not be an unusual event, the impact of a particular event could very well be unforeseen and if that impact is sufficiently material, a Z factor may be warranted.

97 Decision 2014-297 (Errata), paragraph 66.

5 Order

95. It is hereby ordered that:

(1) ATCO Gas is approved to recover a Z factor cost in the amount of $3,121,000 for the 2013 Southern Alberta flood.

Dated on March 16, 2016.

Alberta Utilities Commission

(original signed by)

Mark Kolesar
Vice-Chair

(original signed by)

Anne Michaud
Commission Member

(original signed by)

Neil Jamieson
Commission Member

Appendix 1 – Proceeding participants

Name of organization (abbreviation) **Company name of counsel or representative**
ATCO Gas and Pipelines Ltd. (ATCO Gas) Bennett Jones LLP
AltaLink Management Ltd.
AltaGas Utilities Inc.
Consumers' Coalition of Alberta (CCA)
Office of the Utilities Consumer Advocate (UCA) Reynolds, Mirth, Richards & Farmer LLP

Alberta Utilities Commission Commission panel M. Kolesar, Vice-Chair A. Michaud, Commission Member N. Jamieson, Commission Member Commission staff C. Wall (Commission counsel) J. Graham (Commission counsel) B. Whyte P. Howard J. Work J. Bezuidenhout