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Filling the Gap: The Proposed "Disposition of Regulated Property Regulation"

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Disposition of Regulated Property Regulation (Draft) AR 4570 Draft DRReg 2010 03 31 (available by Email request)

On March 31, 2010 the Alberta government issued a draft regulation pursuant to the *Alberta Utilities Commission Act*, S.A. 2007, c. A-37.2 ("*AUCA*"), the *Disposition of Regulated Property Regulation* (Draft) ("Draft Regulation"). The power to enact regulations is contained in s. 75 of the *AUCA*, which gives the Lieutenant-Governor in Council the power to make regulations "adding to, clarifying, limiting or restricting" any of the powers granted pursuant to the *AUCA*. In this case the Draft Regulation is stated expressly to operate as "an addition to" powers granted to the AUC under the *Gas Utilities Act*, R.S.A. 2000, c. G-5 and the *Public Utilities Act*, R.S.A. 2000, c. P-5. (Draft Regulation, s. 2(1)).

Specifically, the Draft Regulation requires that utilities obtain approval from the AUC prior to disposing of any "regulated property" and grants the AUC power to allocate the proceeds from the disposition of that property between ratepayers and the utility. The Draft Regulation differs from the powers otherwise granted to the AUC in three ways. First, it only applies to regulated property – that is, to property that is or was included in the utility's rate base, or that is or was within the standard for including property in the utility's rate base. The approval process under the *Gas Utilities Act* and the *Public Utilities Act* (which are identical) applies to all property owned by the utility. Second, the Draft Regulation only applies to disposition of the property. The other approval process also applies more broadly to sales, leases, mortgages or other encumbrances placed on a property. Third, the Draft Regulation grants to the AUC the power that the Supreme Court of Canada has previously held it had no jurisdiction to make: allocating the proceeds of disposition between ratepayers and shareholders. Moreover, it grants to the AUC the power to allocate those proceeds "regardless of whether customer rates or service levels will be effected (sic) or impacted by the disposition" (Draft Regulation, s. 3(7)).

In its 2006 decision, *ATCO Gas and Pipelines Ltd. v. Alberta (Energy and Utilities Board)* 2006 SCC 4 ("*AGPL*"), the Supreme Court of Canada held that the predecessor to the Alberta Utilities Commission had no power to allocate proceeds of disposition between the utility and ratepayers. It held that the rights to the assets used to provide utility service rested solely with the utility. Any allocation of the proceeds from the sale of such assets was "confiscatory" and the legislation purported to grant the power to allocate proceeds must be "construed cautiously so as not to strip interested parties of their rights without the clear intention of the legislation" (*AGPL* at para. 79). The Court held that neither the general power to approve asset disposition, nor the power to impose conditions in the public interest, were sufficient to grant the Energy and Utilities Board the power to allocate a portion of the proceeds to ratepayers. Further, it held that on the facts of

that case, where there was no harm to ratepayers from the sale of the asset, either in terms of rates or service, it was unreasonable to allocate any portion to the ratepayers, even had the Board had the power to do so.

It is clear that the Draft Regulation proposed by the Alberta government is a direct response to this 2006 decision. It expressly grants the AUC the power to allocate proceeds of the disposition of utility assets. It also grants the AUC the power to do so even if there is no determination of harm to rates or utility service from the sale.

As someone who has been very critical of the 2006 Supreme Court decision, and also of its effect in subsequent Alberta cases (see my previous ABlawg posts here, here and here), I welcome the intervention of the Alberta government into this debate. The structure of utility rates creates opportunities for utilities to speculate with utility assets, leaving them in rate base if they decrease in value and removing them from rate base if they increase in value. Specifically, (a) the regulator reviews the inclusion of assets in rate base in the first instance, but does not review their included inclusion thereafter, so that assets are not removed from rate base even if they are no longer used for utility service; (b) the calculation of depreciation is abstract and inexact; (c) utilities have been protected from numerous risks associated with the ownership of their assets (e.g., deregulation); and (d) utilities operate both regulated and non-regulated businesses. By allowing the regulator to allocate proceeds between ratepayers and utilities, the Draft Regulation would allow the regulator to protect ratepayers from potentially speculative activity and, as well, remove the *ex ante* incentive for such behaviour to occur.

There is, though, one significant problem with the Draft Regulation. There is also one aspect that requires considerable further thought. The significant problem with the Draft Regulation arises from the fact that it is a regulation, rather than an amendment to the *AUCA*, the *Gas Utilities Act* or the *Public Utilities Act*. As noted, in the 2006 *AGPL* decision the Supreme Court held that the Commission had no legislative jurisdiction to allocate proceeds between the utility and the ratepayers. The majority also found that doing so was confiscatory, and that any attempt to allocate proceeds required clear legislative intention. While s. 75 of the *AUCA* allows the Lieutenant Governor in Council to make regulations "adding to" the powers of the Commission, that power is not limitless. To view s. 75 (or a like provision) as providing Cabinet with an unbridled power to amend legislation by way of regulation would be to undermine fundamentally the rule of law. It would permit changes in regulatory authority and policy without the benefit of a democratic process, especially since the enactment of regulations in Alberta involves no meaningful public consultation or process. The power to add to the powers of the Commission must be understood instead as the ability to add to specific powers within the general legislative grant of jurisdiction given to the Commission.

In this case, I am not comfortable that the Draft Regulation falls within the legislative authority of s. 75, particularly given the view of the Court that the allocation was confiscatory, and required clear legislative direction. If I acted for an Alberta utility purported to be subject to the Draft Regulation I would certainly challenge it as *ultra vires* the legislation that is said to authorize it. In my view the government would be prudent to couple the regulation with a legislative amendment.

The aspect of the Draft Regulation that requires further thought is how the Commission will exercise this power if it is successfully granted. While I have been critical of the Supreme Court's decision in *AGPL*, those criticisms do not arise because I thought that the decision of the Energy and Utilities Board was correct (although it may have been reasonable). The Board in

that case allocated the proceeds of property to ratepayers even though the asset was non-depreciable and was one where there was no realistic argument that the utility had behaved in a speculative manner. The asset had been in rate base for decades and had clearly been employed in utility service. The increase in value of the asset was serendipitous, arising from the increase in real estate values in the City of Calgary; it was best understood as a windfall. Who should be entitled to such windfalls? In my view, in the absence of a regulatory reason to allocate some of the proceeds to ratepayers, the increase in the value of an asset should accrue to shareholders of the utility. A windfall is not a regulatory reason; it is simply a benefit that should lie where it falls – in this case with the utility that owns the asset.

What follows from this point more generally? While the Draft Regulation permits the Commission to allocate proceeds even where there is no negative effect on utility rates or service, the Commission should nonetheless only allocate proceeds between ratepayers and the utility where there is a regulatory reason for doing so. This would be the case where there was harm to rates or service, but also where there was a concern that the utility was acting in a speculative manner, or that it might be incented to do so in the future by an absence of sharing in such situations. Absent, however, harm to rates or services, or a legitimate concern with utility speculation, no allocation to ratepayers should be made.

In sum, even if it is right that a regulator be given certain powers, that does not determine how and when the regulator should exercise them. How they should be exercised remains a manner requiring further inquiry and consideration.