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Overturning *Stores Block* and Implementing the Capacity Market

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Bill Commented On: *An Act to Secure Alberta's Electricity Future*, [Bill 13 \[Alberta\]](#), first reading, April 19, 2018

This Bill has four main objectives. First (clauses 1-2), Bill 13 overturns the majority decision of the Supreme Court of Canada in a case known as *Stores Block: ATCO Gas & Pipelines Ltd. v Alberta (Energy & Utilities Board)*, [2006 SCC 4 \(CanLII\)](#). Second (clauses 3-35), the Bill will amend a series of energy statutes to provide the necessary legislative framework to implement the government's plan to establish an electricity capacity market to supplement the existing energy market. Third (clause 36), the Bill will afford the Alberta Utilities Commission (AUC) enhanced authority to make orders (including administrative penalties) with respect to electric utilities, regulated rate providers and retailers (and their gas equivalents) where the AUC concludes that there has been a failure to comply with the rules respecting service quality and standards. Fourth, the Bill (clause 57) will afford the Lieutenant Governor in Council the authority under s 142 of the *Electric Utilities Act*, [SA 2003, c E-5.1](#) to allow the AUC and the Alberta Electric System Authority (AESO) to make rules with respect to the expedited construction of transmission. Such rules are currently found in some form in the *Transmission Deficiency Regulation*, [Alta Reg 176/2014](#).

This post deals with the *Stores Block* issues. I will aim to write something on the capacity market amendments when the AESO releases the next draft of its [comprehensive market design \(CMD 2.0\)](#) scheduled for the end of April.

Overturning *Stores Block*: Ten Years is a Long Time to Wait

Stores Block dealt with the power of Alberta's utility regulator (then the Alberta Energy and Utilities Board (AEUB), now the AUC) to direct the disposition of the proceeds received on the sale of utility assets that were no longer required by the utility to provide service. The case involved a non-depreciable asset, land, which ATCO originally acquired in 1922. When it was sold in 2001 there was a significant difference between the value at which the asset was carried on ATCO's books (\$225,000) and the price ATCO received (\$6.25 million). The majority of the Supreme Court of Canada ruled that neither the *Gas Utilities Act*, [RSA 2000, c G-5](#) nor the more general provisions of the *Alberta Energy and Utilities Board Act*, [RSA 2000, c A-17](#) gave the regulator any authority to deal with that upside. The asset was the property of ATCO and the fact that it had been a utility asset did not change that fundamental principle. The AEUB had no authority to direct that the upside be shared between shareholders and utility customers. In the years that followed, the Alberta Court of Appeal applied *Stores Block* to a number of other asset dispositions by ATCO: *ATCO Gas & Pipelines Ltd v Alberta (Energy & Utilities Board)*, [2008 ABCA 200 \(CanLII\) \(Carbon\)](#); *ATCO Gas & Pipelines Ltd v Alberta (Energy & Utilities*

Board), [2009 ABCA 171 \(CanLII\) \(Harvest Hills\)](#); *ATCO Gas & Pipelines Ltd v Alberta (Utilities Commission)*, [2009 ABCA 246 \(CanLII\) \(Salt Caverns I\)](#); *ATCO Gas & Pipelines Ltd v Alberta (Utilities Commission)*, [2014 ABCA 28 \(CanLII\) \(Salt Caverns II\)](#).

While *Stores Block* has been distinguished in other jurisdictions it has continued to be the law of Alberta. Furthermore, the AUC has extended the logic of *Stores Block* to losses, suggesting that if gains associated with the disposition of utility assets accrue to the utility owner and not customers, then the losses that occur when an asset becomes stranded or is no longer required for utility purposes before it has been fully depreciated, should also accrue to the utility owner (see my ABlawg post on the [AUC's Utility Asset Disposition \(UAD\) decision](#)). In *Fortis Alberta Inc v Alberta (Utilities Commission)*, [2015 ABCA 295 \(CanLII\)](#) (and see this [ABlawg post](#)), the Alberta Court of Appeal ruled that this was not an unreasonable approach. That Court further ruled that it was not unreasonable to apply the *Stores Block* principles, developed in the context of the gas utility statutes, to electric utilities in the province. In effect, the Court in *Fortis* ruled that the time for any attempt to distinguish and limit the application of *Stores Block* in Alberta had long since passed, and that if a change were to be effected that change could only be made by the legislature. Justice Paperny reasoned as follows (at paras 160-161):

Absent the pronouncements in *Stores Block*, the Commission would likely have greater flexibility on the issue of who bears the undepreciated cost of assets rendered useless as the result of extraordinary events. There would have been a number of potential policy choices to achieve a just result; the Commission could have distributed gains and allocated losses as it saw fit in each particular circumstance In my view, the legislation [the *Electric Utilities Act*] is on its own broad enough to be interpreted to give the regulator that power.

But *Stores Block* has been interpreted in Alberta as preventing such distribution. In the absence of *Stores Block* and the subsequent jurisprudence from this Court, other policy choices would have been open to the regulator. Although it would be tempting to confine the application of these decisions only to gas utilities, (to minimize what I consider to be deleterious effects on the regulation of utilities in Alberta), the legal principles in *Stores Block* remain good law. As such, the distinction the electric utilities wish to make is far less compelling. The Commission's decision, having regard to its legislation and the law of this province as set down by the Supreme Court and this Court, is reasonable.

The Government has now decided that the rigidity of *Stores Block* requires some adjustment and that we need to return to the days when the province's utility regulator had more discretion to balance the interests of shareholders and utility customers—both with respect to the unearned increment associated with a rising a property market, and, at least in some exceptional circumstances, where a utility's assets become stranded.

The government has chosen to achieve this result in Bill 13 by adding a new section 17.1 to the *Alberta Utilities Commission Act*, [SA 2007, c A-37.2](#). The amendment has three main operative sub-sections. Subsections (2) and (4) are linked by what is effectively a definition of relevant "matters" in subsection (4).

(2) In approving a tariff or fixing just and reasonable rates, tolls or charges, or schedules of them, of an owner of a utility under the Electric Utilities Act, the Gas Utilities Act or the Public Utilities Act, the Commission may, in a manner that gives consideration to the public interest, including having regard to any social, economic and environmental effects,

(a) allocate among that owner of a utility and the customers of that owner of a utility

- (i) the direct and indirect costs, including, without limitation, unrecovered capital investment, as determined by the Commission, and
- (ii) the direct and indirect benefits, including, without limitation, revenues generated by or proceeds of sale associated with property, as determined by the Commission,

arising in, or determined in relation to, a prior period, whether or not rates have been finalized for that period, or a present or future period, *in connection with a matter described in subsection (4)*, and

(b) direct the owner of a utility to make adjustments to its tariff, rates, tolls or charges, or schedules of them, on a prospective basis that the Commission considers necessary to give effect to a determination under clause (a).

(4) *The matters referred to in subsection (2)(a)* are as follows:

- (a) a sale, lease, mortgage or other disposition of property of the owner of a utility;
- (b) a removal or withdrawal of property from service to the public by the owner of a utility;
- (c) a removal of property from rate base where the Commission has determined under subsection (3)(a) that the property is no longer used or required to be used to provide service to the public. (emphasis added)

It is not immediately obvious, but subsection (4) is the controlling subsection as between these two provisions insofar as the Commission may only make an “allocation” as between the owner of the utility and customers with respect to “a matter” listed in subsection (4). These matters relate to: dispositions of property; removal or withdrawal of property from service to the public by the owner; and, a removal from the rate base by the Commission.

Where there is a triggering “matter” (which may also require an application – see subsection (9) discussed further below) the Commission, taking into account the public interest, including social, economic and environmental effects, may make an allocation of, *inter alia*, unrecovered capital costs for an asset, and the proceeds of sale of an asset. It appears that the Commission is to give effect to this allocation through its authority to set just and reasonable rates on a prospective basis.

Subsection (3) deals with the discrete issue of the Commission’s power to remove an asset from the rate base of a utility. The Commission has always assumed that it had this power as part of its responsibility to set just and reasonable rates and the Court has effectively confirmed that: *Alberta Power Limited v Alberta Public Utilities Board*, [1990 ABCA 33 \(CanLII\)](#) and *Salt Caverns*.

Additional subsections make it clear that the owner of a utility is not entitled to compensation where the Commission makes an order allocating part of the proceeds of sale to consumers (subsection (6)) and that the Commission (subsection (7)) can make rules:

... respecting the considerations the Commission may take into account when making an allocation of direct and indirect costs or benefits under this section, including, without limitation, the criteria the Commission may consider when determining the public interest for the purposes of this section.

This latter part of this clause may be so broad that it is an invalid sub-delegation of authority.

Commentary

I make four points in this commentary: (1) Why did this take so long? (2) Is it a good idea to encourage the Commission to develop rules on the allocation of costs and benefits? (3) The need for an application? and (4) The complexity of the provision.

Why Did This Take So Long?

There was some discussion of amendments to Alberta's utility legislation shortly after *Stores Block*. For example, my colleague Alice Woolley, in a supplementary case comment to her original comment on *Stores Block*, argued that "It would give greater regulatory certainty, and clearly authorize the desirable and fair result in this and like cases, were the Board's jurisdiction clarified by the legislature to allow it to allocate proceeds as a condition of an asset disposition where necessary to ensure that future rates are just and reasonable." (Alice Woolley, "The Importance of *ATCO Gas and Pipelines*: A response to H. Martin Kay" [\(2007\) 45 Alberta Law Review 515](#) at 519)

My own somewhat cynical view as to the reason for the delay is that the utilities were fine with *Stores Block* so long as it cut only one way and the early post-*Stores Block* Court of Appeal decisions seemed to do just that, to the undoubted benefit of the ATCO family of companies. When it became clear that the AUC considered that *Stores Block* also had implications for the treatment of stranded assets, *Stores Block*, all of a sudden, became much less attractive, especially when the Court of Appeal confirmed in *Fortis* that the AUC's UAD decision was reasonable. Public choice theory would suggest that public utility owners can mobilize far more effectively to lobby for amendments than disparate consumer interests. It would be interesting to file an access to information request to identify utility lobbying efforts over this period looking at both the substance and intensity of those efforts pre and post the AUC's UAD Decision and *Fortis*.

Is it a Good Idea to Encourage the Commission to Develop Rules on the Allocation of Costs and Benefits?

As noted above, subsection (7) affords the Commission the authority to make rules with respect to allocations. I am not convinced that the Commission should take up this invitation. It may be much better for it to build up a body of jurisprudence on a case-by-case basis to provide

guidance to parties. The Commission's process that led to its UAD Decision was long, involved and no doubt expensive, and it hardly seems necessary or appropriate to revisit that process. There will be much in the submissions made to the AUC during that process, as well as in the Commission's own decision and reasons, that will remain relevant to the exercise of the Commission's discretion, even though the ground rules under which the Commission will now operate have materially changed.

The Need for an Application?

As noted above, this new section applies to the "matters" listed in subsection (4), but in addition subsection (9) stipulates that "This section applies to matters referred to in subsection (4) *that are identified in an application that is filed with the Commission ...*" (emphasis added). It is not clear to me if this is designed as an additional hurdle to the application of the section and thus if it could be used, for example, to afford a utility some discretion in triggering the Commission's allocation power. On balance, I don't think that this is a reasonable reading of the provision since the balance of the subsection goes on to deal with the timing of the application of the section. This makes it clear that the subsection is designed to deal with the entry into force of the provision and to prevent what might otherwise be a rush to dispose of valuable utility assets under the current rules.

The Complexity of the Provision

I have sometimes discussed with my Energy Law students over the years how they would amend Alberta's utility statutes to reverse *Stores Block* and restore the status quo. Pre-*Stores Block* successive utility regulators took the view that they could apportion the proceeds of sale from an asset in excess of book value as between consumers and shareholders and did so in accordance with something called the TransAlta formula. It had always struck me that the easiest way to achieve this result would be to focus on the statutory power that the regulator is exercising when it approves the sale of an asset by a utility. In the case of gas utilities this is s 26(2)(d) of the *Gas Utilities Act*, [RSA 2000, c G-5](#) (*GUA*). This section requires the AUC's approval for any disposition of an asset by a designated gas utility outside the ordinary course of business. This triggers the application of the so-called "no-harm test" (which is not explicitly referenced in the statute), the potential imposition of terms and conditions to mitigate any harm, and, finally, the controversial and contested part – allocation of the proceeds of sale.

Thus, a possible amendment s 26 of the *GUA* to restore the status quo might read as follows:

In considering an application for the sale, lease, mortgage, disposition, encumbrance, merger or consolidation of any of the property of an owner of a gas utility designated under subsection (1) outside the ordinary course of the owner's business, the Commission may impose such terms and conditions as it considers necessary to protect the interests of customers of that gas utility, and may make such allocation of the proceeds of sale of that asset as seem to it to be just and reasonable.

There is a parallel provision in the *Public Utilities Act*, [RSA 2000, c P-45](#), s 101 (*PUA*) which could be similarly amended. This provision in the *PUA* also applies to owners of designated

electric utilities (see this [post](#) on the Berkshire Hathaway acquisition of AltaLink and s 116 of the *PUA*).

This is evidently a much simpler and more targeted amendment than we find in Bill 13. It deals with the precise issue at stake in *Stores Block* and does not go beyond that. This has both positive and negative consequences. Its principal positive consequence is simplicity although it also has the advantages that it references a no-harm or protection principle and focuses on “just and reasonable” as the key value rather than the even more general term “public interest”. But it must be acknowledged that this draft is perhaps too narrow (and this is a negative consequence) given the way that events have unfolded since *Stores Block* and the AUC’s UAD decision. In particular, the above provision is much narrower than the drafting in Bill 13 in the following ways: (1) the provision only addresses the issue of gains, not stranded assets, (2) the provision only applies to designated utilities, and (3) the provision only applies to dispositions outside the ordinary course of business (likely not a significant concern). The most serious omission of my draft is that it fails to expressly address the possibility that it might be just and reasonable, in exceptional circumstances, to allow a utility owner to recover from customers undepreciated capital investments (in whole or in part) when a utility asset is stranded or removed from the rate base. This perhaps explains why the government has taken a more complex approach in Bill 13.

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