In the Court of Appeal of Alberta

Citation: ATCO Gas and Pipelines Ltd. v. Alberta (Energy and Utilities Board), 2005 ABCA 122

Date: 20050329
Docket: 0201-0015-AC
Registry: Calgary

Between:

ATCO Gas and Pipelines Ltd.

Appellant (Applicant)

- and -

Alberta Energy and Utilities Board

Respondent (Respondent)

The Court:

The Honourable Mr. Justice Willis O'Leary
The Honourable Madam Justice Anne Russell
The Honourable Mr. Justice Neil Wittmann

Reasons for Judgment Reserved of The Honourable Madam Justice Russell
Concurred in by The Honourable Mr. Justice O'Leary
Concurred in by The Honourable Mr. Justice Wittmann

Appeal from the Decision of the
Alberta Energy and Utilities Board
Dated the 13th day of December, 2001

Reasons for Judgment of
The Honourable Madam Justice Russell

[1] On December 13, 2001, following a Deferred Gas Account Reconciliation Hearing, the Alberta Energy and Utilities Board (the "Board"), in its Decision 2001-110, found the appellant ATCO Gas and Pipelines Ltd. ("ATCO") acted imprudently in managing its gas supplies for the winter of 2000/2001. As a result the Board ordered ATCO to pay $4 million to its customers to compensate them for missed cost savings. In ***Atco Gas and Pipelines Ltd. v. Alberta (Energy and Utilities Board)***, 2003 ABCA 188, ATCO was granted leave to appeal that decision pursuant to s. 26 of the ***Alberta Energy and Utilities Board Act***, R.S.A. 2000, c. A-17 and section 70 of the ***Public Utilities Board Act***, R.S.A. 2000, c. P-45, on the following issue:

> Did the Board err in law in determining the appropriate standard to be applied with respect to the prudence and reasonableness of the decision of the Applicant utility in the context of this case?

[2] The chambers judge expressly denied leave on the calculation of the $4 million refund.

[3] The City of Calgary ("Calgary") opposed ATCO's application at the Reconciliation Hearing before the Board and was permitted to make submissions on this appeal.

INTRODUCTION

[4] ATCO is a gas distribution utility. It is governed by legislation which authorizes the Board to regulate public utilities and to "ensure that the public pays a fair and reasonable rate for the gas and the owner of the gas obtains a fair and reasonable return on its investment": ***Atco Gas and Pipelines Ltd. v. Alberta (Energy and Utilities Board)*** (2004), 339 A.R. 250, 2004 ABCA 3 at para. 36 ("***Atco Gas***"). Customers of ATCO are charged the actual cost ATCO incurs for the gas it supplies.

[5] The Board has statutory authority to set just and reasonable rates: ***Gas Utilities Act***, R.S.A. 1980, c. G-4, s. 28; ***Public Utilities Board Act***, R.S.A. 1980, c. P-37, s. 81. Gas utility rates, or Gas Cost Recovery Rates (GCRRs) are meant to reflect the market price a utility pays to purchase natural gas. Gas utilities generally apply semi-annually to have GCRRs set by the Board. At the end of a rate period, the Board sets the upcoming rate period's GCRR through a process of reconciling the forecast costs with the actual costs incurred. To account for the risks of fluctuating costs, utilities are allowed to accumulate variances between forecast costs and actual costs: ***ATCO Electric Limited v. Alberta (Energy and Utilities Board)***, 2004 ABCA 215 at para. 26 ("***ATCO Electric***"). That variance is accumulated in a Deferred Gas Account (DGA).

[6] GCRRs are based on forecasts of future prices and costs, as well as any revenue surplus or deficiency incurred from the previous season as a result of the variance between actual costs and

forecast costs. GCRRs are intended to ensure any surplus will be distributed to customers, or to allow the utility to recover any deficiency, depending on the DGA balance. GCRRs are also intended to minimize future variance between actual costs and forecast costs.

[7] Where there is a significant change in gas supply costs between regular applications, a utility is encouraged to apply to the Board for approval of an adjustment to the GCRR in order to minimize the DGA balance: AEUB Order U2000 308. ATCO made such an application in January 2001.

[8] This appeal relates to the reconciliation of ATCO's DGA for the 2000/2001 winter season, and the test applied by the Board in assessing the prudence demonstrated by ATCO in managing its gas supplies during that period.

BACKGROUND

[9] ATCO owns a natural gas storage facility near Carbon, Alberta (the "Carbon facility") which is capable of storing enormous quantities of gas. A certain amount of the gas in storage is needed to provide the minimum pressure required to meet minimum design deliverability. That gas is called 'base gas', or 'cushion gas', and is a rate base asset.

[10] ATCO's practice was to purchase gas and inject it into storage at the Carbon facility during the summer months when demand was low, and to withdraw the stored gas during the winter when demand was high. The gas injected and withdrawn on a cyclical basis is called 'working gas', and is essentially gas inventory.

[11] Because the demand for gas corresponds with price, the practice of injecting and withdrawing working gas can have a favourable effect on prices, referred to as a "physical hedge."

[12] Although ATCO acknowledges the potential cost benefit to customers, it denies engaging in the practice of injecting and withdrawing gas from storage for the purpose of managing gas prices. Rather, ATCO argues its use of storage from the Carbon facility was to meet the operational requirements of the pipeline system, withdrawing gas at variable rates in order to manage fluctuations in demand.

[13] Commencing in the winter of 2000/2001, ATCO decided the Carbon facility was no longer needed for operational purposes. ATCO says its decision was based in part on previous decisions of the Board, which ATCO interpreted as not permitting it to engage in financial hedging because it would be costly over time and adversely affect retail gas market development. Other factors which led ATCO to discontinue use of the Carbon facility for operational purposes were deregulation in the gas utility industry and an abundance of gas supply in the open market in this province. ATCO claims it had no assurance of a market for its gas supply as a result of those factors. However, the Board found that the proposed deregulation of Carbon was not relevant to ATCO's use of gas storage during the 2000/2001 winter season, when the Carbon facility was still in use.

[14] Prior to the 2000/2001 winter season, ATCO had used a flexible withdrawal strategy, dependent on seasonal fluctuations in demand. During the winter of 2000/2001, ATCO changed to a flat withdrawal strategy, meaning that ATCO withdrew gas from the Carbon facility at set monthly flat rates. ATCO claims that as a result of its withdrawal strategy during that season of unprecedented high gas prices, it generated savings to its customers of about $60 million. However, Calgary contends that savings realized from the sale of gas purchased during the summer months when gas prices were low, does not exonerate ATCO from abandoning a flexible withdrawal strategy during the winter, which would have achieved additional savings. Calgary also notes that ATCO's own expert admitted that flexibility has value in a competitive market.

[15] ATCO says its flat withdrawal strategy was designed to avoid speculation as to future prices in the day-to-day management of gas in storage, in keeping with the Board's cautions against engaging in trading.

[16] In Order U2000-161, the Board determined that the use of financial hedging had not previously been used as a method of gas portfolio management (AB VIII, E7). It rejected arguments that ATCO had acted inappropriately by failing to engage in the purchase of gas for storage and simultaneous sale of it on the forward market for later withdrawal. The Board did so on the basis that such activity would be tantamount to trading, for which it had not given any approval (AB VIII, E-8). However, in that Order, the Board recommended that:

> [ATCO] revisit the issue of using financial hedging to help manage its gas portfolio and provide. . . a comprehensive cost/benefit analysis for its use prior to applying for a winter period Gas Cost Recovery Rate (GCRR) effective November 1, 2000, in order to determine if there is a general consensus among its sales customers for implementation of this form of risk management. (AB VIII, E8-E9)

[17] In a subsequent Order, U2000-183, the Board approved a storage strategy for the April 1, 2000 - March 31, 2001 storage season. That strategy allowed ATCO to buy blocks of fixed price physical gas in the summer and sell blocks of fixed price physical gas for the winter. Order U2000-183 states:

> In . . . Order [U2000-161] the EUB agreed that ATCO GS acted appropriately in the circumstances at that particular time by following the DGA procedures in place, which did not include the use of forward markets or other forms of financial hedging as a method of gas portfolio management. The EUB recommended however that ATCO GS revisit the issue of using financial hedging to help manage its gas portfolio.

[18] Orders U2000-161 and 183 do not support ATCO's position that it was prohibited by the Board from engaging in financial hedging.

[19] ATCO claims its decision to switch withdrawal strategies reflected the fact that the historical need to vary withdrawals in response to operational requirements for the pipeline system no longer existed. ATCO relies in part on expert reports recommending the best solutions for fluctuations in gas prices. Two of those reports are dated March 16 and April 2, 2001. But since ATCO's decision was made prior to the winter of 2000/2001, those reports could not possibly have influenced it. A third report, dated January 14, 2000 may be applicable, but does not expressly support ATCO's decision to cease using flexible withdrawal; it merely outlines the value and risks inherent in using various strategies.

[20] At ATCO's DGA Reconciliation Hearing in 2001, Calgary introduced a report, prepared by its expert VanderSchee, which concluded that had ATCO withdrawn gas at flexible rates in response to price fluctuations during the winter of 2000/2001 rather than withdrawing at a flat rate, it could have saved customers an additional $8.9 million. According to VanderSchee, such a strategy avoids the need to purchase gas at elevated prices by providing a utility with some flexibility to withdraw variable amounts of gas from storage in response to fluctuations in market prices.

[21] ATCO counters that VanderSchee's report was based on hindsight, and that the recommended strategy would have required ATCO to engage in trading.

Board Decision

[22] The Board ruled that ATCO's decision to implement flat withdrawal in the context of the winter period for 2000/2001 was imprudent. In its decision, the Board applied the following test of prudence:

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

[23] The Board noted that both before and during the winter period 2000/2001, gas forecasts predicted higher gas prices. While the Board recognized that ATCO did not have the benefit of the computer program used by VanderSchee, and could not have predicted the actual price fluctuations so as to realize the optimal savings calculated with the benefit of hindsight, in the Board's view, ATCO ought to have employed a strategy similar to that described by VanderSchee. The Board accepted that VanderSchee's method was not a trading strategy.

[24] The Board held that ATCO ought to have done something to mitigate the high gas prices over the 2000/2001 winter season. The Board found that some of the options available to ATCO at the time included: continued withdrawal of gas on a flexible basis depending on market conditions, as had been done in the past; use of the excess deliverability on days when gas prices spiked; sale of that portion it did not intend to use; or development of other strategies to deal with the forecast

high gas prices.

[25] The Board estimated the total savings not realized by ATCO to be $4 million, and ordered ATCO to refund that amount to its customers through reduced rates in the future.

RELEVANT LEGISLATION

[26] Both the appellant's and respondents' facta make reference to the ***Gas Utilities Act***, R.S.A. 2000 c. G-5, the ***Alberta Energy and Utilities Board Act,*** R.S.A. 2000, c. A-17 and the ***Public Utilities Board Act***, R.S.A. 2000, c. P-45. The gas sales in question and the decision under appeal took place prior to the coming into force of the 2000 Revised Statutes of Alberta on January 1, 2002 by proclamation O.C. 424/2001. Accordingly, although the R.S.A. 2000 statutes apply with respect to ATCO's application for leave to appeal, which occurred after the proclamation date, the matters before the Board, now under appeal, are governed by the ***Gas Utilities Act***, R.S.A. 1980, c. G-4, as amended ("***GUA***"), the ***Alberta Energy and Utilities Board Act***, S.A. 1994, c. A-19.5 ("***AEUBA***"), and the ***Public Utilities Board Act***, **R.S.A**. 1980, c. P-37, as amended ("***PUBA***"). Therefore, all references in this decision are to those Acts as amended on the relevant dates.

[27] All relevant legislation is listed in Appendix A, attached hereto.

BRIEF CONCLUSIONS

[28] The only question before this Court is one of law relating to the test for prudence set by the Board. The application of the four factors of the pragmatic and functional analysis to that question results in a standard of review of reasonableness *simpliciter*.

[29] Applying that standard, we find the Board's test for prudence reasonable and dismiss ATCO's appeal.

STANDARD OF REVIEW

[30] This is an appeal from the decision of an administrative tribunal. Therefore, this Court must determine, in light of the governing legislation, the appropriate level of scrutiny to be applied on review of that decision: ***Pushpanathan v. Canada (Minister of Citizenship and Immigration)***, [1998] 1 S.C.R. 982 ("***Pushpanathan***") at para. 26; ***Dr. Q v. College of Physicians and Surgeons of British Columbia***, [2003] 1 S.C.R. 226, 2003 SCC 19 ("***Dr. Q***") at paras. 21-22; ***Voice Construction Ltd. v. Construction & General Workers' Union, Local 92***, 2004 SCC 23 ("***Voice***") at para. 15.

[31] The standard of review must be determined by applying the pragmatic and functional analysis developed in ***U.E.S., Local 298 v. Bibeault***, [1988] 2 S.C.R. 1048, which entails consideration of four contextual factors: (1) the presence or absence of a privative clause or statutory

right of appeal; (2) the expertise of the tribunal relative to that of the reviewing court on the issue in question; (3) the purposes of the legislation and the provision in particular; and (4) the nature of the question – law, fact or mixed law and fact: ***Pushpanathan***, *supra* at paras. 29-38; ***Canada (Deputy Minister of National Revenue) v. Mattel Canada Inc.***, [2001] 2 S.C.R. 100, 2001 SCC 36 ("***Mattel***") at para. 24; ***Dr. Q***, *supra* at para. 26; ***Law Society of New Brunswick v. Ryan***, [2003] 1 S.C.R. 247, 2003 SCC 20 ("***Ryan***") at para. 27; ***Voice***, *supra* at para. 16; ***A.U.P.E. v. Lethbridge Community College***, 2004 SCC 28 ("***Lethbridge***") at para. 14. None of those four factors are determinative: ***Pushpanathan***, *supra* at para. 27; ***Mattel***, *supra* at para. 24, but evaluated collectively, they will indicate the appropriate degree of deference to afford the administrative decision-maker.

[32] There are three standards of review, from least to most deferential: correctness, reasonableness, and patent unreasonableness: ***Canada (Director of Investigation and Research) v. Southam Inc.***, [1997] 1 S.C.R. 748 at para. 30; ***Baker v. Canada (Minister of Citizenship and Immigration)***, [1999] 2 S.C.R. 817 at para. 55; ***Ryan***, *supra* at paras. 20 & 24.

[33] Legislative intent underlies each factor in the pragmatic and functional analysis: ***Dr. Q***, *supra*; ***Voice***, *supra* at para. 18. In this case, the governing legislation is the ***GUA***, the ***AEUBA***, and the ***PUBA***. (See Appendix A)

Privative Clause/Right of Appeal

[34] Section 10 of the ***AEUBA*** gives the Board the same jurisdiction and powers granted to the Public Utilities Board ("PUB"). Thus, the Board has jurisdiction to "hear and determine all questions of law or of fact" pursuant to s. 30 of the ***PUBA***.

[35] Section 26 of the ***Alberta Energy and Utilities Board Act***, R.S.A. 2000, c. A-17 and s. 70 of the ***Public Utilities Board Act***, R.S.A. 2000, c. P-45 allow for appeals from decisions of the Board on questions of law or jurisdiction where leave has been granted. Such a statutory right of appeal implies legislative intent to afford the Board less deference on questions of law or jurisdiction: ***Barrie Public Utilities et al. v. Canadian Cable Television Association et al.*** (2003), 304 N.R. 1, 225 D.L.R. (4th) 206 at 217 (S.C.C.) ("***Barrie***"). However, granting leave on a matter of law or jurisdiction will not necessarily attract a correctness standard: ***Barrie***, *ibid*; ***Alberta Energy v. Goodwell Petroleum*** (2003), 339 A.R. 201, 2003 ABCA 277 at para. 23. Matters falling within the Board's expertise will warrant deference even where there is a statutory right of appeal: ***Pezim v. British Columbia (Superintendent of Brokers)***, [1994] 2 S.C.R. 557 at 591 ("***Pezim***"); ***Atco Gas***, *supra* at para. 35.

[36] This factor suggests that the Board's decision be afforded limited deference.

Relative Expertise

[37] The Board is a specialized tribunal with expertise in the area of gas utility regulation, which includes protecting the public interest by balancing the competing interests of customers and utilities: ***Coalition of Citizens v. Alberta (Energy and Utilities Board)*** (1996), 187 A.R. 205 at para. 14 (C.A.); ***ATCO Ltd. v. Calgary Power* Ltd.**, [1982] 2 S.C.R. 557 at 576; ***Atco Gas***, *supra* at para. 34; ***ATCO Electric*** at para. 53. However, the expertise of the Board relative to that of this Court will depend on the issue in question: ***Pushpanathan***, *supra* at para. 33; ***Barrie***, *supra* at 219.

[38] In this case, the issue for which ATCO was granted leave is the following:

> Did the Board err in law in determining the appropriate standard to be applied with respect to the prudence and reasonableness of the decision of the Applicant utility in the context of this case?

[39] This question could be understood in two ways. Did the Board have jurisdiction to set and apply a standard of prudence in reviewing ATCO's decisions? Alternatively, assuming the Board did have jurisdiction, did the Board employ the proper standard of prudence in respect of ATCO's management decisions? If it is the former, the issue involves legislative interpretation, for which the Board's expertise does not necessarily exceed that of this Court. However, if it is the latter, the issue straddles the line between statutory interpretation and industry-specific practice, in which case, the Board's expertise may very well exceed that of this Court. For the reasons that follow, I conclude the question is one of law and not of jurisdiction.

[40] In support of its position that the proper standard of review is correctness, ATCO argues that any authority the Board has in terms of denying recovery of costs or imposing obligations on ATCO to refund are matters of statutory interpretation, which go to the Board's jurisdiction. However, ATCO was not granted leave on the jurisdictional argument.

[41] ATCO argues the broad applicability of the issue respecting prudence suggests minimal deference, citing ***Chieu v. Canada (Minister of Citizenship and Immigration)*** (2002), 208 D.L.R. (4^{th}) 107 at 120. While conceding the Board has expertise, ATCO says in the absence of a statutory framework, the Board has no expertise with respect to the test for prudence.

[42] ATCO's submissions on the leave question focus predominantly on what ought to be the proper test for prudence, as do submissions by the Board and by Calgary. None of the parties make submissions regarding the Board's jurisdiction to set such a test. Moreover, the issue on which leave was granted was framed as one of law and not as one of jurisdiction. Therefore, focus will be confined to the issue of law as to whether the Board adopted the proper test of prudence.

[43] The Board enunciated its test of prudence in the context of rate-setting. Fixing just and reasonable rates is a matter squarely within the Board's expertise: ***TransAlta Utilities Corp. v.***

Alberta Public Utilities Board (1986), 68 A.R. 171 at para. 22 (C.A.) ("***TransAlta***"); ***Industrial Power Consumers Assn. of Alberta v. TransAlta Utilities Corp.*** (2000), 255 A.R. 194 at para. 4 (C.A.). The issue is polycentric and requires expertise.

[44] Given the nature of the legal issue and the context surrounding it, the expertise of this Court does not exceed that of the Board which suggests the Board must be afforded curial deference.

Legislative Purpose

[45] The purpose of the governing statutory scheme as a whole, and the specific applicable provisions in particular, must also be considered in determining the appropriate standard of review: ***Dr. Q***, *supra* at para. 30; ***Lethbridge***, *supra* at para. 18.

[46] The Supreme Court of Canada spoke generally to the mandate conferred on the Board by the ***GUA*** and the ***PUBA*** in ***ATCO v. Calgary Power***, [1982] 2 S.C.R. 557 at 576:

> It is evident from the powers accorded to the Board by the legislature in both statutes mentioned above that the legislature has given the Board a mandate of the widest proportions to safeguard the public interest in the nature and quality of the service provided to the community by the public utilities.

[47] The general legislative mandate on the Board is to protect the public interest by way of regulating public utilities. A reviewing court should grant deference where the statutory scheme governing an expert tribunal allows the tribunal to balance competing interests and address broad policy concerns: ***Pezim***, *supra* at 591-92; ***ATCO Electric***, *supra* at para. 56.

[48] In reconciling the DGA and setting a 'just and reasonable' prospective GCRR, the Board conducted a prudence review of the Board's management decisions respecting withdrawal from storage. The question is whether the Board applied the correct test for prudence.

[49] Specific provisions of the governing legislation that confer authority on the administrative tribunal can also be indicators of limited review.[1] Although there is no particular provision in any of the governing Acts which refers to a prudence review, the applicable legislative provisions do give the Board authority to fix 'just and reasonable' rates, a specific mandate connected to the

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[1] In ***TransAlta***, *supra* at para. 22, Kerans J.A. stated:

> . . . Sometimes a legislature invites limited review not by purporting to limit the power of the reviewing court but rather by conferring delegated legislative powers on the tribunal. When the delegation is manifest, as when the tribunal is empowered to "make regulations", the matter is beyond dispute. In other cases, the delegation is not so obvious but is found in the description of the powers of a tribunal in terms which are at once imprecise and evocative. The use of elastic adjectives is usually considered by a court as an implicit granting of a power to the tribunal to form its own "opinion" or make "policy" or to exercise a "discretion" - in fine, to make law. The key power of this Board is to fix "fair and reasonable" rates. This is a good example of a grant of a wide discretion.

general legislative purpose: ***Re City of Dartmouth*** (1976), 17 N.S.R. (2d) 425 at 432 (S.C.A.D.). The words 'just and reasonable' suggest that the criteria with which the Board exercises its power is flexible and discretionary, and subject to limited review.

[50] The Board has authority to fix just and reasonable rates, taking into account retrospective considerations respecting revenues and costs: ***GUA***, ss. 28(a) and 32(a); ***PUBA***, ss. 81(a) and 83(a). The Board also has authority to fix just and reasonable standards to be observed by utilities: ***GUA***, s. 28(c); ***PUBA***, s. 81(c).

[51] The discretion to determine what is just and reasonable includes the discretion to define justness and reasonableness: see ***Memorial Gardens Association (Can.) Ltd. v. Colwood Cemetery Co.*** [1958] S.C.R. 353 at 357; and ***TransAlta****, supra* at para. 24, citing ***Edmonton, Jasper Place et al v. Northwestern Utilities Ltd.*** (1960) 34 W.W.R. 241 (Alta. S.C.A.D.). Such discretion suggests a legislative intent to give deference to the Board's methodology in fixing rates and standards. Support for that premise is found in ***Newfoundland Light & Power Co. v. P.U.C. (Bd.)*** (1987), 25 Admin. L.R. 180 (NFCA). There the Court rejected the argument that the Board had exceeded its jurisdiction in determining a just and reasonable rate of return by failing to adopt a particular methodology. That decision was cited with approval in ***Newfoundland (Board of Commissioners of Public Utilities) (Re)*** (1998), 164 Nfld. & P.E.I.R. 60 at para. 29 (NFCA) by Green J.A., who stated:

> . . . The Board therefore has a broad discretion to adopt appropriate methodologies for the calculation of allowable rates of return. So long as the methodologies chosen are not inconsistent with generally accepted sound public utility practice and the purposes and policies of the Act, and can be supported by the available opinion evidence, the determination of what constitutes a just and reasonable return in a given case will generally be within the province of the Board and will not normally be interfered with.

[52] ATCO's customers are charged with the actual cost of gas supplied by ATCO. Actual costs incurred by a utility are reflected in the DGA balance. Those costs depend in part on that utility's management strategy, including the execution and management of a hedging plan. Assessing management decisions may necessarily factor into a reconciliation hearing and the Board's determination and implementation of just and reasonable rates: see Costello, K., "Should Commissions Pre-Approve a Gas Utility's Hedging Activities?" (***NRRI***, 34th Annual Regulatory Conference: Tampa, Florida, December 10, 2002).

[53] The Board's determination of the test governing its review of ATCO's management decisions accords with the general legislative mandate to serve the public interest by balancing the consumer's interest in just and reasonable rates with the utility's interest in earning a reasonable rate of return. In light of the discretionary nature of the specific rate-setting provisions, this factor

suggests that deference be given by this Court.

Nature of the Question

[54] Leave to appeal is granted only on questions of law or jurisdiction, which would generally favour less deference. However, as the question relates to the management of a utility and marketing strategies, it is one for which the Board has greater expertise than does this Court. Where the question of law is at the core of the administrative decision-maker's expertise, some deference is owed to that decision-maker: ***Voice***, *supra* at para. 29.

[55] ATCO argues the Board erred in its articulation and application of the prudence test, in finding ATCO imprudent. The application of the test is an issue of mixed fact and law. Because the governing legislation grants a right of appeal with leave only on questions of law or jurisdiction, questions of mixed fact and law can only come before this Court where there is an extricable legal question: see ***Housen v. Nikolaisen***, [2002] 2 S.C.R. 235 at para. 36. The Board's application of its prudence test is an issue inextricably bound to the facts and is therefore not properly before us. The question of whether the prudence test set by the Board was correct, is extricable and is a question of law. Because it is a question which falls within the discretion granted to the Board by its governing legislation, some deference must be afforded.

Conclusion on Standard of Review

[56] In the context of this case, only one of the four ***Pushpanathan*** factors, the statutory right of appeal, indicates a less deferential standard. Otherwise, the Board's expertise and the governing legislation suggest the Board be given a high degree of deference, given the nature of the issue.

[57] In a decision released after oral argument concluded in this case, this Court found that because the legal question engaged was of general import, the appropriate standard to be applied to the Board's decision concerning entitlement to carrying costs is in the mid-range of judicial review spectrum, that is reasonableness. But the Court also found that "the Board enjoys expertise superior to this Court in determining the appropriate methodology for calculating prudent costs of financing a particular segment of a utility's operations": ***ATCO Electric***, *supra* at para. 62. Thus, Fraser C.J.A. concluded the appropriate standard to apply to that decision is patent unreasonableness. However, here, the Court is not being asked to review a methodology of calculation of rates, but rather whether the Board erred in determining the appropriate standard in reviewing the reasonableness of managerial decisions.

[58] Considering the four contextual factors in this case, and the import of the prudence test to the utilities industry, I conclude the appropriate standard of review is reasonableness *simpliciter*. Applying that standard, the Court must ask "whether there is a rational basis for the decision . . . in light of the statutory framework and the circumstances of the case": ***Cartaway Resources Corp. (Re)*** (2004), 319 N.R. 1, 2004 SCC 26 at para. 49.

ANALYSIS

Did the Board err in law in determining the appropriate test to be applied with respect to the prudence and reasonableness of the decision of the Applicant utility in the context of this case?

[59] The Board concluded ATCO acted imprudently because it "could have, and ought to have, maximized the value of the 'excess' deliverability by using it on days when prices were spiking or by selling the deliverability it did not intend to use . . .", and by failing to do so, ATCO "was not acting in the best interests of customers . . ." In reaching that conclusion the Board adopted the following test of prudence:

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

[60] The Board cited its earlier Decision 2000-01, wherein it stated:

> [The concept of prudence]. . . has been recognized as a tool available to regulators, and in most instances involves an evaluation of whether or not a decision reflects good judgment and discretion and is reasonable in the circumstances which were known, or reasonably should have been known when the decision was made.

[61] ATCO maintains that the proper test for prudence requires the presumption of managerial prudence, and that the Board erred by failing to presume management had acted prudently. Although the Board did not expressly presume prudence, it may have done so implicitly by determining to uphold ATCO's decision unless it was satisfied that ATCO acted unreasonably: AB I, p. F21. But ATCO also submits that mere unreasonableness or error in judgment is not sufficient to establish imprudence and that a regulator is not entitled to step into the role of a manager. In ATCO's view, if any error was made at all, it was a mere error of judgment and not outside the realm of what any reasonable business person would do. Any such error would not constitute negligence and could thus not properly constitute imprudence.

[62] In the course of ATCO Pipelines 2003/2004 General Rate Application (Tab 18 ATCO's authorities), Calgary disputed any presumption of prudence in regulatory law that ATCO Pipelines' forecasts are reasonable, which in its view would be a reversal of the onus of proof. Further, Calgary says there is no logical reason to apply a presumption of correctness to a utility budget. Instead, Calgary says the utility has the onus of establishing the reliability of its forecast expenditure. Calgary says there is no major difference between the Board's and ATCO's articulation of the test for prudence, and that ATCO's main complaint is with the application of the test.

[63] Calgary also notes that the test applied by the Board has been applied by the Ontario Energy Board, which addressed the test for prudence in the context of rate regulation in the transportation industry in RP - 2001-0029. That Board acknowledged that a presumption of prudence on the part of a regulated utility is implicit in the framework underlying rate regulation. The Ontario Energy Board said that in considering the prudence of any action, it is engaged in a retrospective review of the reasonableness of the utility's action at a given point, and the forseeability of any changes in circumstances is critical to that review. At para. 2.36 that Board stated:

> A poor outcome does not govern the assessment of prudence. Prudence is however, called into question if the commitment was made casually, that is without a reasonable level and scope of analysis, or recklessly, or primarily for some ulterior non-utility or ulterior corporate purpose. (Calgary authorities Tab 18 p. 21)

[64] The term "prudence" is well known in the utility rate-making industry and has a significant history. Included in Calgary's materials is a 2002 paper from The National Regulatory Research Institute of Ohio State University (the "NRRI") entitled, "State Commission Regulatory Considerations Concerning Security-Related Cost Recovery in Utility Network Industries", which references a 1985 NRRI publication: *The Prudent Investment Test in the 1980's* (the "*Prudent Investment Test*"). *The Prudent Investment Test* describes the history of the concept of prudence and its use in regulated public utilities. The authors describe the concept of prudent investment as: "a regulatory oversight standard that attempts to serve as a legal basis for adjudging the meeting of utilities' public interest obligations, specifically in regard to rate proceedings": ch. 2, p. 20. The 2002 NRRI paper cited by Calgary and *The Prudent Investment Test* at 93, both suggest that before a regulator investigates the prudence of a utility, the presumption of prudence must be rebutted.

[65] As a standard in public utility regulation, prudence is described as a concept borrowed from legal principles, such as negligence. In other words, the public utility will be held to a managerial duty of care:

> What is prudent is deemed to be ascertainable through the reasonable efforts of competent managers with sound and reasonable judgment. That risk is involved in managerial decision making is judicially acknowledged. But, the deliberate exposure to substantial risk in the exercise of managerial discretion is by its very nature imprudent, for risk is to be avoided, if not altogether, at least insofar as possible under the circumstances: *The Prudent Investment Test*, p. 47.

[66] A presumption of prudence triggers an onus of proof on the party impugning managerial decisions. However, if that presumption is rebutted, a public utility's decision will be reviewed, applying an objective test of reasonableness to the facts and circumstances surrounding the decision, without relying on hindsight: *The Prudent Investment Test*, p. 93

[67] In determining whether a company had exercised proper discretion in matters requiring business judgment, the U.S. Supreme Court in ***State of Missouri ex re, Southwestern Bell Telephone Company v. Public Service Commission of Missouri*** 262 U.S. 276, 289 (1923), stated:

> The Commission is not the financial manager of the corporation and it is not empowered to substitute its judgment for that of the directors of the corporation; nor can it ignore items charged by the utility as operating expenses unless there is an abuse of discretion in that regard by the corporate officers.

[68] In support of its submission that for actions to qualify as imprudent they must be dishonest or obviously wasteful, ATCO cites the dissenting judgment of Justice Brandeis, in footnote 1 at 289 of that case:

> The term prudent investment is not used in a critical sense. There should not be excluded from the finding of the base, investments which, under ordinary circumstances, would be deemed reasonable. The term is applied for the purpose of excluding what might be found to be dishonest or obviously wasteful or imprudent expenditures. Every investment may be assumed to have been made in the exercise of reasonable judgment, unless the contrary is shown.

[69] In ***West Ohio Gas Co. v. Public Utilities Commission of Ohio (No. 1)***, 294 U.S. 63, 68 (1935), at p. 25 the U.S. Supreme Court held that:

> A public utility will not be permitted to include negligent or wasteful losses among its operating charges. The waste or negligence, however, must be established by evidence of one kind or another, either direct or circumstantial.

The Court continued at p. 26:

> Good faith is to be presumed on the part of the manager of a business. . . In the absence of a showing of inefficiency or improvidence, a court will not substitute its judgment for theirs as to the measure of a prudent outlay.

[70] There, the Court concluded that imposition of a penalty was wholly arbitrary in the absence of evidence showing any warning to the company that fault was imputed to it and that it must give evidence of care.

[71] The Board concedes that the standard of prudence is similar to the standard of care required in assessing negligence, but argues that with respect to a regulated public utility, the test is not what a reasonable businessman would have done in the circumstances, but rather what a reasonable public utility would have done. In ***Acker v. United States***, 298 U.S. 426, 431 (1936), cited in *The Prudent Investment Test* at 32, regarding management judgment, the U.S. Supreme Court held that:

> ...[T]he charge is for a public service, and regulation cannot be frustrated by a requirement that the rate be made to compensate extravagant or unnecessary costs...

[72] The Board's broad discretion to set just and reasonable utilities rates must be exercised in the public interest, which requires consideration of both sides of the rate paying equation: ***ATCO Electric***, *supra* at 132. That process implicitly entails scrutiny of management decisions. With respect to negotiated settlements Fraser C.J.A. held in ***ATCO Electric*** at para. 145 that the Board "is entitled to assume that what the utility has negotiated and agreed to is in fact in the utility's best interests." However, in the context of rate setting, the starting point for scrutinizing management decisions is the presumption that it is in the utility's interest to make prudent decisions which also reflect the interests of its customers, by avoiding needless expenditure. That presumption will matter only when the scales are evenly balanced.

[73] In this case, in determining to uphold ATCO's decision unless satisfied ATCO had acted unreasonably, the Board correctly acknowledged the presumption of prudence. The test it articulated to be applied in reviewing the prudence and reasonableness of ATCO's decisions is reasonable.

CONCLUSION

[74] ATCO's complaint with the Board's application of the prudence test involves questions of fact, and is not properly before this Court. The only matters at issue on this appeal are whether the Board properly acknowledged a presumption of prudence, and properly articulated the test of prudence, in assessing ATCO's management decisions. The Board's articulation of the prudence test is consistent with its previous decisions and with the line of authority addressing the concept of prudence in the context of public utilities. Given the governing legislation and the circumstances of this case, there is a rational basis for the test of prudence articulated and relied on by the Board in its decision.

[75] Accordingly, the appeal is dismissed.

Appeal heard on April 21, 2004

Reasons filed at Calgary, Alberta
this 29th day of March, 2005

Russell J.A.

I concur:

O’Leary J.A.

I concur:

Wittmann J.A.

Appearances:

H.M. Kay, Q.C.
L.E. Smith, Q.C.
For the Appellant

J.R. McKee
A.E. Domes
for the Respondent

P.L. Quinton-Campbell
R.B. Brander
for the Third Party

Appendix "A"

Current Legislative Provisions

Alberta Energy and Utilities Board Act, R.S.A. 2000, c. A-17

> **26(1)** Subject to subsection (2), an appeal lies from the Board to the Court of Appeal on a question of jurisdiction or on a question of law.
>
> **(2)** Leave to appeal may be obtained from a judge of the Court of Appeal only on an application made
>
> (a) within 30 days from the day that the order, decision or direction sought to be appealed from was made, or
>
> (b) within a further period of time as granted by the judge where the judge is of the opinion that the circumstances warrant the granting of that further period of time.
>
> . . . . .

Public Utilities Board Act, R.S.A. 2000, c. P-45

> **70(1)** Subject to subsection (2), on a question of jurisdiction or on a question of law, an appeal lies from the Board to the Court of Appeal.
>
> **(2)** Leave to appeal shall be obtained from a judge of the Court of Appeal on application made within one month after the making of the order, decision, rule or regulation sought to be appealed from, or within any further time that the judge under special circumstances allows, and on notice to the parties and to the Board, and on hearing those of them that appear and desire to be heard, and the costs of the application are in the discretion of the judge.
>
> . . . . .

Applicable Repealed Legislative Provisions

Alberta Energy and Utilities Board Act, S.A. 1994, c. A-19.5 [repealed] ("***AEUBA***")

> **10(1)** Fort he purposes of carrying out its functions, the Board has all the powers, rights and privileges of the ERCB and the PUB that are granted or provided for by any enactment or by law.
>
> . . . . .

Gas Utilities Act, R.S.A. 1980, c. G-4, as amended. [Repealed] ("***GUA***")

> **16** When it is made to appear to the board, on the application of any owner of a gas utility or of any municipality or person having an interest, present or contingent, in the matter in

respect of which the application is made, that there is reason to believe that the tolls demanded by an owner of a gas utility exceed what is just and reasonable, having regard to the nature and quality of the service rendered or of the gas supplied, the Board

> **(*a*)** may proceed to hold any investigation that it thinks fit into all matters relating to the nature and quality of the service or the gas supplied, or to the performance of the service and the tolls or charges demanded therefor,
>
> . . .
>
> **(*c*)** may disallow or change, as it thinks reasonable, any tolls or charges that, in its opinion, are excessive, unjust or unreasonable or unjustly discriminate between different persons or different municipalities, but subject however to any contract existing between the owner of the gas utility and a municipality at the time the application is made that the Board considers fair and reasonable.
>
> . . .

25(1) No owner of a gas utility shall

> **(*a*)** make, impose or extract any unjust or unreasonable or unjustly discriminatory or unduly preferential individual or joint rate, commutation rate or other special rate, toll, fare, charge or schedule for any gas or service supplied or rendered by it within Alberta,
>
> . . .
>
> **(*c*)** adopt, maintain or enforce any regulation, practice or measurement that is unjust, unreasonable, unduly preferential, arbitrarily or unjustly discriminatory or otherwise in contravention of law, or provide or maintain any service that is unsafe, improper or inadequate, or withhold or refuse any service that can reasonably be demanded and furnished when ordered by the Board,
>
> . . .

28 The Board, either on its own initiative or on the application of a person having an interest, may by order in writing, which shall be made after giving notice to and hearing the parties interested,

> **(*a*)** fix just and reasonable individual rates, joint rates, tolls or charges or schedules of them, as well as commutation and other special rates, which shall be imposed, observed and followed thereafter by the owner of the gas utility,
>
> . . .
>
> **(*c*)** fix just and reasonable standards, classifications, regulations, practices, measurements or service which shall be furnished, imposed, observed and followed thereafter by the owner of the gas utility,
>
> . . .
>
> **(*e*)** require an owner of a gas utility to supply and deliver gas to the persons, for the purposes, at the rates, prices and charges and on the terms and conditions that the

Board directs, fixes or imposes.

. . .

32 In fixing just and reasonable rates, tolls or charges, or schedules thereof, to be imposed, observed and followed thereafter by an owner of a gas utility,

> **(*a*)** the Board may consider all revenues and costs of the owner that are in the Board's opinion applicable to a period consisting of
>
> > **(*i*)** the whole of the fiscal year of the owner in which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules of them,
> > **(*ii*)** a subsequent fiscal year of the owner, or
> > **(*iii*)** 2 or more of the fiscal years of the owner referred to in subclauses (I) and (ii) if they are consecutive
>
> and need not consider the allocation of those revenues and costs to any part of that period,
>
> **(*b*)** the Board may give effect to that part of any excess revenue received or any revenue deficiency incurred by the owner that is in the Board's opinion applicable to the whole of the fiscal year of the owner in which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules of them, that the Board determines is just and reasonable,
>
> **(*c*)** the Board may give effect to that part of any excess revenue received or any revenue deficiency incurred by the owner after the date on which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules of them, that the Board determines has been due to undue delay in the hearing and determining of the matter, and
>
> **(*d*)** the Board shall by order approve the method by which, and the period (including any subsequent fiscal period) during which, any excess revenue received or any revenue deficiency incurred, as determined pursuant to clause (b) or (c), is to be used or dealt with.

. . . . .

Public Utilities Board Act, R.S.A. 1980, c. P-37, as amended. [Repealed] ("***PUBA***")

30 The Board may, as to matters within its jurisdiction, hear and determine all questions of law or of fact.

. . .

81 The Board, either on its own initiative or on the application of a person having an interest, may by order in writing, which shall be made after giving notice to and hearing

the parties interested,

> (a) fix just and reasonable individual rates, joint rates, tolls or charges or schedules thereof, as well as commutation, mileage or kilometre rate and other special rates, which shall be imposed, observed and followed thereafter by the owner of the public utility;
> . . .
> (c) fix just and reasonable standards, classifications, regulations, practices, measurements or service which shall be furnished, imposed, observed and followed thereafter by the owner of the public utility;
> . . .

. . .

83(1) Subject to subsection (2), in fixing just and reasonable rates, tolls or charges, or schedules thereof, to be imposed, observed and followed by an owner of a public utility,

> (a) the Board may consider all revenues and costs of the owner that are in the Board's opinion applicable to a period consisting of
>
> > (i) the whole of the fiscal year of the owner in which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules thereof,
> > (ii) a subsequent fiscal year of the owner, or
> > (iii) 2 or more of the fiscal years of the owner referred to in subclauses (i) and (ii) if they are consecutive,
>
> and need not consider the allocation of those revenues and costs to any part of such a period,
> . . .
> (b) the Board may give effect to that part of any excess revenue received or any revenue deficiency incurred by the owner that is in the Board's opinion applicable to the whole of the fiscal year of the owner in which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules thereof, as the Board determines is just and reasonable.
>
> (c) the Board may give effect to such part of any excess revenue received or any revenue deficiency incurred by the owner after the date on which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules thereof, as the Board determines has been due to undue delay in the hearing and determining of the matter, and
>
> (d) the Board shall by order approve the method by which, and the period (including any subsequent fiscal period) during which, any excess revenue received or any revenue deficiency incurred, as determined pursuant to clause (b) or (c), is to be used or dealt with.

1981, c. E-4.1, s. 17; 1984, c. 60, s. 4; 1988, c. S-13.75, s. 9; 1995, c. 11, s. 14.