



## **Direct Energy Regulated Services**

**2018-2020 Energy Price Setting Plan**

**December 21, 2018**

**Alberta Utilities Commission**

Decision 22635-D01-2018

Direct Energy Regulated Services

2018-2020 Energy Price Setting Plan

Proceeding 22635

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## **1 Decision summary**

1. In this decision, the Alberta Utilities Commission provides its findings on an application from Direct Energy Regulated Services (DERS) in which DERS requested approval of its energy price setting plan (EPSP) for the term of May 1, 2018 to April 30, 2020. The Commission has approved the requested term of the EPSP. The Commission has not approved all aspects of the 2018-2020 EPSP as detailed in this decision, and consequently, DERS is required to submit a compliance filing to reflect the Commission's findings and directions.

## **2 Introduction and procedural summary**

2. DERS filed the application on May 5, 2017. In addition to requesting approval of its EPSP, DERS also requested confidential treatment of certain information it identified as commercially sensitive; included in the application as Confidential Schedule E (Protocol for Procurement) and Confidential Appendix E.1 (Daily Target Price Setting Schedule Example).

3. The 2018-2020 EPSP reflects a multi-year rate setting mechanism where the regulated rate option (RRO) energy charges will be determined monthly by procuring energy hedges through block procurement. The 2018-2020 EPSP will carry forward the majority of the EPSP components approved in decisions 2941-D01-2015,<sup>1</sup> 20459-D01-2015<sup>2</sup> and 21295-D01-2017.<sup>3</sup> DERS submitted that its proposed 2018-2020 EPSP is a mechanical plan.<sup>4</sup>

4. As part of the proposed plan, DERS requested inclusion of the after-tax reasonable return approved in Decision 22004-D01-2018,<sup>5</sup> as well as commodity risk compensation (CRC) of \$7.97 per megawatt hour (/MWh) based on the evidence put forward by Gordon Buchanan Lang and Associates Inc. (GBL).

5. In response to DERS-AUC-2017NOV09-040, DERS submitted a revised EPSP,<sup>6</sup> that included changes arising from interrogatories and other corrections. The revised EPSP was composed of:

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<sup>1</sup> Decision 2941-D01-2015: Direct Energy Regulated Services, ENMAX Energy Corporation and EPCOR Energy Alberta GP Inc., Regulated Rate Tariff and Energy Price Setting Plans – Generic Proceeding: Part B – Final Decision, Proceeding 2941, Application 1610120-1, March 10, 2015.

<sup>2</sup> Decision 20459-D01-2015: Direct Energy Regulated Services 2014-2018 Energy Price Setting Plan Compliance Filing, Proceeding 20459, December 21, 2015.

<sup>3</sup> Decision 21295-D01-2017: Direct Energy Regulated Services 2016-2018 Energy Price Setting Plan Second Compliance Filing, Proceeding 21295, August 30, 2017.

<sup>4</sup> Exhibit 22635-X0005, PDF page 6.

<sup>5</sup> Decision 22004-D01-2018: Direct Energy Regulated Services, 2017-2018 Default Rate Tariff and Regulated Rate Tariff, Proceeding 22004, June 12, 2018.

<sup>6</sup> Exhibit 22635-X0045.

- The 2018-2020 Energy Price Setting Plan
- Schedule A – Definitions
- Schedule B – Energy Price Setting Process
- Schedule C – Forecast Load Methodology
- Schedule D – Energy Portfolio Hedge Volume Determination Methodology
- Confidential Schedule E – Protocol for Procurement
  - Confidential Appendix E.1 – Daily Target Price Setting Schedule Example
- Schedule F – Energy Charge Applicable for Each Month During the Plan Term
- Schedule G – Code of Conduct for the Energy Price Setting Plan
  - Appendix G.1 – Procurement Conduct Agreement

6. The Commission issued a notice of application on May 8, 2017, asking interested parties to file their concerns, or support for the application, no later than May 23, 2017. The Commission received submissions from the Consumers' Coalition of Alberta (CCA) and the Office of the Utilities Consumer Advocate (UCA).

7. In a May 26, 2017 letter, the Commission suspended this proceeding pending conclusion of a concurrent proceeding considering DERS' 2016-2018 EPSP second compliance filing.<sup>7</sup> The Commission approved DERS' 2016-2018 EPSP in Decision 21295-D01-2017, issued on August 30, 2017. On September 6, 2017, the Commission recommenced the current proceeding for DERS' 2018-2020 EPSP.

8. In a September 25, 2017 letter, the Commission granted confidential treatment for Confidential Schedule E and Confidential Appendix E.1. The Commission also established a basic written process to consider the application.

9. After time extensions and motions, the process schedule ultimately consisted of information requests (IRs), responses to IRs, intervener evidence, rebuttal evidence, argument and reply argument. The Commission received parties' reply argument on October 3, 2018. After the initial close of record, the UCA filed an October 10, 2018 motion requesting that the Commission strike portions of DERS' reply argument.

10. Upon receipt of comments from parties on the motion, the Commission issued an October 31, 2018 ruling directing DERS to file an amended reply argument. The Commission considers that the close of record for this proceeding was November 1, 2018; the date DERS filed its amended reply argument.

11. In reaching the determinations set out within this decision, the Commission has considered all relevant materials on the public record of this proceeding as well as the

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<sup>7</sup> Proceeding 21295, DERS 2016-2018 EPSP second compliance filing application, submitted January 29, 2016.

confidential filings. The Commission has reviewed all of the relevant confidential material and where general information was included in the confidential filings that does not disclose confidential information about the procurement protocol aspect of the EPSP, the Commission has referred to this general information on the public record. Any information that provides details regarding the procurement protocol aspect of the EPSP has been redacted and included in the confidential portions of this decision as have the confidential views of parties on the application and the related Commission findings. A separate confidential decision will be issued respecting the confidential portions of the decision to parties who have signed confidentiality undertakings in this proceeding.

12. 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.

### 3 Term of the EPSP

13. DERS applied for approval of its 2018-2020 EPSP for the period of May 1, 2018 to April 30, 2020.<sup>8</sup> When it filed its application, DERS noted that the *Regulated Rate Option Regulation* (the regulation) expires on April 30, 2020 and, for this reason, it selected a term for the EPSP that aligned with the regulation's expiry date.<sup>9</sup> Subsequent to the submission of DERS' application, the April 30, 2020 expiry date was removed from the regulation.

14. After the April 30, 2020 expiry date was removed from the regulation, DERS was asked in an IR whether it wanted to apply for a longer term EPSP. DERS responded as follows:

DERS would like to maintain the initially proposed term of May 1, 2018 to April 30, 2020. All analysis conducted for the Application was based on the applied for test period and an extension to the term would potentially alter the risk profile assumed by DERS. Accordingly, adjusting to a longer period than initially proposed would require further evaluation by DERS.<sup>10</sup>

15. DERS argued that a risk profile associated with a term different than what it applied for would likely result in different analytical outcomes.<sup>11</sup>

16. Mr. Beblow, on behalf of the UCA, submitted that the two-year term proposed by DERS is not optimal. The external EPSP development and regulatory costs recoverable from customers will be higher over a two-year term than they would be if the term of the EPSP was longer.<sup>12</sup> He added that a shorter term also results in less opportunity to evaluate the operation of the EPSP. Mr. Beblow and the UCA both submitted that extending the term of the EPSP will reduce regulatory burden.<sup>13</sup>

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<sup>8</sup> Exhibit 22635-X0005, PDF page 3.

<sup>9</sup> Exhibit 22635-X0005, PDF page 5.

<sup>10</sup> Exhibit 22635-X0038, DERS-AUC-2017NOV09-003.

<sup>11</sup> Exhibit 22635-X0164, paragraph 18.

<sup>12</sup> Exhibit 22635-X0090, PDF page 19.

<sup>13</sup> Exhibit 22635-X0090, PDF page 19. Exhibit 22635-X0166, paragraph 147.

17. Mr. Beblow challenged DERS' submission that all the analysis conducted for the application was based on the applied-for test period. He stated DERS conducted research that extended beyond April 30, 2020 and the vast majority of the CRC analysis undertaken by DERS is based on historical trends. He submitted that these historical trends would be completely unaffected by the term of the EPSP. The UCA agreed with Mr. Beblow's submission.<sup>14</sup>

18. Mr. Beblow and the UCA recommended that the term of the EPSP be three years.<sup>15</sup> While Mr. Beblow supported the use of his CRC methodology (the Beblow method) under either a two-year EPSP term or a three-year EPSP term,<sup>16</sup> he did not support a longer EPSP duration if the Beblow method was not utilized.<sup>17</sup> The UCA referred to its significant concerns about the potential for a fixed rate CRC to result in excessive gains for DERS, and because of this, it stated it is extremely hesitant to advocate for a term longer than three years.<sup>18</sup>

19. DERS responded that if Mr. Beblow's priority was to reduce costs and regulatory burden, his recommendation for the term of the EPSP would not be contingent on the CRC methodology used.<sup>19</sup> DERS submitted that the Beblow method of CRC continues to carry the risk that any large losses in the final months of the EPSP may not be recovered through the risk cycle adder. DERS stated this risk is not mitigated by extending the term of the EPSP, and it added that the same applies to both attrition risk and changes in consumption risk.<sup>20</sup>

### Commission findings

20. The Commission is not persuaded that any of the arguments advanced by Mr. Beblow or the UCA warrant extending the term of the EPSP beyond that requested by DERS and considers that DERS has offered a compelling reason not to do so.

21. The Commission agrees with Mr. Beblow and the UCA that extending the term of the EPSP beyond April 30, 2020, would reduce regulatory burden. The Commission also accepts that recovering external EPSP development and regulatory costs over a longer term EPSP compared to a shorter term EPSP would result in the monthly rates being lower, all else being equal. However, weighed against the evidentiary and process concerns expressed by DERS and discussed in paragraphs 23 and 24 below, the Commission is satisfied that neither the marginal effect on rates that would result from recovery of the external EPSP development and regulatory costs over a three-year compared to a two-year EPSP term,<sup>21</sup> nor the reduction in regulatory burden are sufficiently material considerations warranting approval of a three-year term in the circumstances of this application. Though not determinative, the Commission observes that reduction of regulatory burden likewise appears not to have been a key consideration for Mr. Beblow and the UCA, because they conditioned their recommendations for a longer term EPSP on the approval of an adaptive CRC methodology.

22. While the Commission also agrees that more operational experience with the plan and data would be gained over a three-year term compared to a two-year term, the Commission is not

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<sup>14</sup> Exhibit 22635-X0166, paragraph 143.

<sup>15</sup> Exhibit 22635-X0090, PDF page 50; and Exhibit 22635-X0166, paragraph 148.

<sup>16</sup> Exhibit 22635-X0107, UCA-AUC-2018MAR16-001.

<sup>17</sup> Exhibit 22635-X0108, UCA-DERS-2018MAR16-001.

<sup>18</sup> Exhibit 22635-X0166, paragraph 148.

<sup>19</sup> Exhibit 22635-X0128, paragraph 2.

<sup>20</sup> Exhibit 22635-X0051, DERS-UCA-2017NOV10-033.

<sup>21</sup> Exhibit 22635-X0090, PDF page 18.

persuaded that a two-year term will increase the likelihood of over compensation or under compensation given the CRC methodology approved in Section 5 of this decision. There is inadequate information for the Commission to conclude that DERS will be over compensated or under compensated by the approval of a shorter term rather than a longer term.

23. In opposition to the suggestion that the Commission consider a longer EPSP term, DERS stated that its analysis and that of its experts were based on the risk profile of the term it proposed. Adjusting to a longer period than initially proposed would be associated with a different risk profile, would require further evaluation by DERS and would likely result in different analytical outcomes.<sup>22</sup> DERS asserted that there is no evidence before the Commission on the risk, relative pricing of that risk or the required return margins for any term beyond that of DERS' proposed EPSP.<sup>23</sup>

24. The Commission accepts the representations made by DERS concerning the basis for its analysis and that of its experts with respect to risk and the term of the EPSP. The Commission also observes that the recommendations of Mr. Beblow and the UCA for a longer EPSP term are contingent on the approval of an adaptive CRC methodology. These submissions appear to acknowledge that the risk profile of the plan is linked to its term as asserted by DERS. The Commission agrees. As such, it would not be reasonable to approve a term other than that proposed by DERS in the absence of evidence from DERS concerning its risk profile associated with a longer term and evidence from other parties on the risk profile. A process would need to be established to test the evidence of parties to address the issues.

25. For the above reasons, the Commission denies the recommendations of Mr. Beblow and the UCA that the term of the EPSP be extended to three years. The Commission approves DERS' request that the expiry date of the EPSP be set as April 30, 2020.

26. The Commission notes that the EPSP document does not contain an expiry date. The Commission directs DERS, as part of the compliance filing, to include wording indicating the expiry date of April 30, 2020, in the body of the EPSP document, preferably somewhere in the early pages of the EPSP, and in the definition section of the EPSP included in Schedule A to the EPSP.

## **4 Energy price setting plan**

### **4.1 Load forecast**

27. DERS indicated that the load forecast will be calculated as the product of a site count forecast and an average consumption per site forecast, which is similar to how it is calculated in its 2016-2018 EPSP.<sup>24</sup> The load forecasting methodology is included in Schedule C of the 2018-2020 EPSP.<sup>25</sup> DERS stated that the development of the load forecast continues to be mechanical in nature and employs little to no discretion. DERS submitted that "Throughout the 2018-2020

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<sup>22</sup> Exhibit 22635-X0164, paragraph 18.

<sup>23</sup> Exhibit 22635-X0176, paragraph 142.

<sup>24</sup> Exhibit 22635-X0005, PDF page 5.

<sup>25</sup> Exhibit 22635-X0045, page 12.

EPSP, DERS may incorporate improvements to the forecasting methodology in an attempt to reduce forecast error.”<sup>26</sup>

28. Mr. Beblow raised a concern with the potential effects of the RRO rate cap being ignored in the development of the load forecasts under the 2018-2020 EPSP. His evidence was that with the benefit of the RRO rate cap, the RRO prices will be lower than competitive market prices and, as such, there should be an expectation that customers will return to the RRO.<sup>27</sup> He recommended that DERS incorporate these effects into its forecasts.<sup>28</sup>

29. The UCA indicated that subsequent to Mr. Beblow’s submission, DERS filed further information that demonstrated that the effect on the accuracy of the site count forecast caused by the potential effects of the RRO rate cap is not overly significant. The UCA, therefore, submitted that no adjustments are necessary to the site count factor or the load forecasting methodology.<sup>29</sup>

### Commission findings

30. The Commission compared Schedule C of the 2018-2020 EPSP<sup>30</sup> to Schedule C from the approved 2016-2018 EPSP.<sup>31</sup> There are some differences that the Commission considers it must address, as shown in the following table:

**Table 1. Differences between Schedule C in the 2018-2020 EPSP and Schedule C in the 2016-2018 EPSP to be addressed by the Commission**

Section	2018-2020 EPSP <sup>32</sup>	2016-2018 EPSP <sup>33</sup>
A – first sentence	DERS will continue to utilize the forecasting system deployed across Direct Energy in order to complete its monthly and quarterly forecast.	DERS will continue to utilize the Northstar system in order to complete its monthly and quarterly forecast.
A (3)	SF <sub>RC</sub> = average monthly net growth and attrition factor based on previous 2 year actual site count net growth/attrition calculated at the rate class level for the E1, E2, E5, E6 and E7 rate classes. Given the large variance in growth and attrition numbers within the past 24 months, DERS will use an SF <sub>RC</sub> equal to zero for the E3 and E4 rate classes.	SF <sub>RC</sub> = average monthly net growth and attrition based on previous 2 year actual site count net growth/attrition calculated at the rate class level.
D (1)	Any Forecast Load methodology improvements identified during the term of the EPSP will be filed for acknowledgement with the Commission prior to implementation.	Any load forecasting improvements identified during the term of the EPSP will be filed with the Commission for approval prior to implementation.

31. With respect to the first sentence of Section A, DERS indicated that it transitioned to the Northstar forecasting system in 2018,<sup>34</sup> and has been operating under this system since January 2018.<sup>35</sup> The Commission considers that the proposed revision to the first sentence in Section A is designed to eliminate the requirement for DERS to update the EPSP, in the event it has to utilize

<sup>26</sup> Exhibit 22635-X0005, PDF page 10.

<sup>27</sup> Exhibit 22635-X0090, PDF pages 21-22.

<sup>28</sup> Exhibit 22635-X0090, PDF page 50.

<sup>29</sup> Exhibit 22635-X0166, paragraphs 153-154.

<sup>30</sup> As included in Exhibit 22635-X0045.

<sup>31</sup> The 2016-2018 approved EPSP is included as Appendix 5 to Decision 21295-D01-2017.

<sup>32</sup> As included in Exhibit 22635-X0045.

<sup>33</sup> As included in Appendix 5 of Decision 21295-D01-2017.

<sup>34</sup> Exhibit 22635-X0144, DERS-AUC-2018JUL27-001.

<sup>35</sup> Exhibit 22635-X0150, DERS-UCA-2018JUL27-001.

a different forecasting system other than the Northstar system it currently employs. The Commission finds that this approach is acceptable and eliminates the requirement for DERS to apply to revise the EPSP, to accommodate changes in the name of the forecasting system. The Commission approves DERS' proposed wording in Section A, first sentence of Schedule C, as set out in Table 1 above.

32. For Section A (3), DERS proposed to set the net growth and attrition factors ( $SF_{RC}$ ), for the E3 rate class - large general service customers and the E4 rate class - oilfield service customers, at zero for the term of the 2018-2020 EPSP. DERS explained that the site counts for the E3 rate class were static over the 24-month period from March 2015 to February 2017. It submitted that the proposal for the E3 rate class will make sure that the "forecasted site counts for this rate class are not affected by uncommon large variances in monthly growth and attrition."<sup>36</sup>

33. DERS indicated that the site counts for the E4 rate class over the 24-month period from March 2015 to February 2017 fluctuated between months of large net growth and months of large net attrition. DERS explained that large changes in monthly net growth or attrition can change the  $SF_{RC}$  factor significantly, in both magnitude and direction, in a matter of months. It submitted that if the  $SF_{RC}$  factor is set to zero, this will ensure that the changes in magnitude and direction to the monthly site counts are not reflected in the forecast site counts. Even though the  $SF_{RC}$  factors for these two rate classes will be zero, actual growth and attrition will be reflected because the monthly forecasts are based on the most recent actual site counts.<sup>37</sup>

34. The Commission considers that DERS' proposal to amend Section A (3) of Schedule C does not accord with the largely mechanical nature of the load forecasting methodology employed in the proposed EPSP and the approved 2016-2018 EPSP. The proposed amendment is based on DERS' judgement that the average monthly net growth and attrition factors for rate classes E3 and E4 should be zero over the term of the EPSP, rather than based on the actual experience of the net growth or attrition over the previous two years. The Commission finds that DERS did not adequately support or explain why the load forecasting methodology for these two rate classes should be different from the methodology approved in the 2016-2018 EPSP, or why it should be different from the methodology employed for all the other rate classes. In the absence of further evidence on this issue and given the mechanical nature of the plan, the Commission denies the proposed revision to Section A (3) of Schedule C to the EPSP. The Commission directs DERS, in the compliance filing, to use the same wording for  $SF_{RC}$  that was approved in the 2016-2018 EPSP.

35. In relation to Section D (1) of Schedule C, DERS was asked about its intention to file any improvements to its load forecasting methodology for Commission acknowledgement as opposed to Commission approval. DERS stated that because it will be utilizing a forecasting system that is used across Direct Energy, it needs to accommodate changes as they occur.<sup>38</sup> It added that the proposed change will avoid complications that may arise when Direct Energy transitions systems across its entire North American business. DERS indicated that such transitions are an attempt to improve the forecasting process, and the decision to transition is made on a company-wide basis. DERS submitted that if it were to require Commission approval for such a transition and could not obtain it, it would be at risk of requiring a legacy forecasting

<sup>36</sup> Exhibit 22635-X0038, DERS-AUC-2017NOV09-009.

<sup>37</sup> Exhibit 22635-X0038, DERS-AUC-2017NOV09-009.

<sup>38</sup> Exhibit 22635-X0038, DERS-AUC-2017NOV09-004.

system to be in compliance. In addition, DERS would not be able to share the costs of maintaining such a legacy system with other business units of Direct Energy.<sup>39</sup>

36. The Commission agrees with DERS that requiring Commission approval prior to implementing any load forecasting methodology changes may restrict the ability of DERS to implement changes in load forecasting in a timely manner. Improved load forecasting accuracy will reduce the volume mismatches between the hedged load of fixed block products and the actual load for which DERS bears commodity risk. The Commission, therefore, grants DERS' request for an amendment to Section D (1) of Schedule C to the 2018-2020 EPSP to allow for an acknowledgement rather than an approval, as set out in Table 1 above. The Commission notes that it granted a similar approval for EPCOR Energy Alberta GP Inc. (EEA) as part of its 2018-2021 EPSP.<sup>40</sup> The Commission's approval of EEA's 2018-2021 EPSP includes the following description of what will be filed for acknowledgement:

In the acknowledgement filing, EEA will include:

- i. An explanation of the change to the methodology or adjustment to the inputs to the forecast;
- ii. Supporting analysis for the change to the methodology or adjustment to the inputs to the forecast; and
- iii. A schedule that shows the history of all the changes to the methodology and changes to the inputs to the forecast.<sup>41</sup>

37. It would be beneficial to the Commission that the information described above be filed by DERS in any filing for acknowledgement. The information listed in the previous paragraph from EEA's 2018-2021 EPSP will allow for disclosure of relevant information regarding changes in load forecasting, and will assist the Commission in reviewing the changes filed for acknowledgement. Therefore, the Commission directs DERS, in the compliance filing, to include the wording quoted above from Section C of Schedule C of EEA's 2018-2021 EPSP, as part of Section D of Schedule C to DERS' 2018-2020 EPSP, replacing EEA with DERS in the first sentence.

## **4.2 Procurement protocol**

### **4.2.1 Random procurement period**

38. Paragraphs 38 to 41 are redacted.

### **4.2.2 Determination of the daily target price**

42. Paragraphs 42 to 48 are redacted.

### **4.2.3 Must lift/Must bid criteria**

49. Paragraphs 49 to 53 are redacted.

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<sup>39</sup> Exhibit 22635-X0144, DERS-AUC-2018JUL27-001.

<sup>40</sup> Decision 22357-D01-2018: EPCOR Energy Alberta GP Inc., 2018-2021 Energy Price Setting Plan, Proceeding 22357, March 16, 2018, paragraph 161.

<sup>41</sup> Decision 23916-D01-2018: EPCOR Energy Alberta GP Inc., Application for Amendments to the 2018-2021 Energy Price Setting Plan, Proceeding 23916, October 18, 2018, Appendix 2, PDF page 38.

## 5 Commodity risk compensation

### 5.1 Statutory framework and onus

54. Section 3(1) of the *Regulated Rate Option Regulation* (the regulation) sets out the information the owner must provide when submitting a proposed regulated rate tariff (RRT) for approval:

3(1) An owner's proposed regulated rate tariff provided to its regulatory authority for approval under section 103 of the Act

(a) must include

...(ii) a new RRO rate energy price setting plan,

(iii) the owner's proposed risk margin, and

2. (iv) the terms and conditions under which the owner proposes to offer electricity services,

55. Section 4 of the regulation states that the price setting plan referred to in Section 3(1)(a)(ii) must use "a fair, efficient and openly competitive acquisition process to ensure that the resulting prices for the supply of electric energy are just, reasonable and electricity market based." The Commission must, according to Section 6(1)(d) "have regard for the principle that a regulated rate tariff must not impede the development of an efficient market for electricity based on fair and open competition in which neither the market nor the structure of the Alberta electric industry is distorted by unfair advantages of any participant."

56. A risk margin, which the Commission describes as commodity risk compensation (CRC), is provided for in Section 5(1) of the regulation. That section requires the Commission to ensure that the owner's risk margin is just and reasonable. The definition of risk margin is found in Section (1)(l) of the regulation and means "the just and reasonable financial compensation that an owner's regulatory authority approves for the owner based on the financial risks (i) that remain with the owner, and (ii) that are associated with the supply of electricity services to regulated rate customers." Section 5(3) states that the risks covered by the risk margin must include, all volume risk, all price risk, all credit risk, and all unaccounted for energy and losses. Section 5(4) states that risks covered by the risk margin may include other prudently incurred risks associated with energy and non-energy related costs. Pursuant to Section 6(1)(a), the Commission must have regard for the principle that an RRT, including the risk margin described in Section 5, must provide the owner with a reasonable opportunity to recover the prudent costs and expenses incurred by the owner. The risk margin must not be considered as part of the reasonable return.<sup>42</sup> Under Section 6(1)(c) of the regulation, a risk margin must also provide the owner with "a just and reasonable financial compensation for the risks described in section 5."

57. The onus is on the RRO provider to demonstrate the EPSP filed under Section 3 of the regulation is consistent with the regulation and reasonably supported by the evidence such that it can be approved by the Commission.

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<sup>42</sup> Section 6(1)(b)(ii) of the regulation.

## 5.2 DERS CRC proposal

58. To price its commodity risk and develop its proposed CRC for the 2018-2020 EPSP, DERS commissioned the actuarial consulting firm, Gordon B. Lang and Associates Inc. (GBL). DERS described GBL's insurance-based method of determining CRC as "fair, market based and independent from the determination of risk aversion."<sup>43</sup> GBL prepared a report entitled "Commodity Risk in the Regulated Energy Industry: An Insurance Analysis,"<sup>44</sup> (the GBL report) setting out its recommendation for CRC for DERS.

59. GBL stated that the insurance industry uses five criteria to assess whether a particular risk is an insurable risk. GBL assessed DERS' commodity risk using these five criteria. Based on its review, GBL determined that DERS' commodity risk is an insurable risk and that this form of risk could be analyzed and priced.<sup>45</sup> GBL recommended an appropriate range for CRC to be between \$499,000 and \$832,000 per month, which when applied to DERS' 2016 average monthly load of 104,000 MWh, results in a monthly charge to customers in the range of \$4.78/MWh to \$7.97/MWh.

60. Based on GBL's recommendations, DERS requested approval of a monthly CRC of \$7.97/MWh, for the entire term of the EPSP. DERS indicated:

DERS faces commodity risk that must be priced within this EPSP. Insurance would allow DERS to transfer and remove this commodity risk, but since the market for commodity risk insurance does not exist, DERS is required to self-insure. Self-insurance comes with many risks, challenges and costs. One key risk is that DERS is prevented from increasing the CRC to reflect actual experience for the duration of the EPSP. Should greater than anticipated losses occur, DERS would incur such losses without the ability to pass them on to DERS' customers. Another key element is a lack of a marketplace to mitigate or transfer this risk, due to the unique nature of the risk, so a CRC on the high side of the range is necessary. In addition, based on the fact that DERS is a risk averse entity, and that the recommendation from GBL includes no gross ups for risk tolerance, DERS proposes to set the CRC at \$7.97/MWh for the duration of the 2018-2020 EPSP.<sup>46</sup>

61. GBL's method of determining the CRC for the 2018-2020 EPSP is different than the Commission approved methodology for determining CRC that is currently in place for DERS' 2016-2018 EPSP. The currently approved methodology is commonly referred to as the Beblow method.

62. The Beblow method of determining CRC involves two components, a variable adaptive component and a risk cycle component.<sup>47</sup> The calculation of the variable adaptive component on a monthly basis results in a percentage. This percentage is multiplied by the base energy charge for the month to determine the resulting variable adaptive CRC component for the month. The risk cycle component, commonly referred to as the risk cycle adder (RCA), is calculated quarterly on a \$/MWh basis. If the calculation determines that a risk cycle CRC charge is required, then the resulting risk cycle charge, which is static, will be in place for the subsequent three months.

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<sup>43</sup> Exhibit 22635-X0005, PDF page 27.

<sup>44</sup> Exhibit 22635-X0001.

<sup>45</sup> Exhibit 22635-X0001, page 1.

<sup>46</sup> Exhibit 22635-X0005, PDF page 34.

<sup>47</sup> More details on the Beblow method are included in paragraphs 1191-1195 of Decision 2941-D01-2015.

63. GBL applied two techniques to arrive at its recommended monthly CRC range for DERS. GBL described the process for determining the monthly amount of \$499,000, which is the lower end of its recommended range, as follows:

We aggregated the hourly gains and losses to determine the actual profit and loss for DERS for each month. The results ranged from a maximum profit of \$278,000 in April 2011 to a maximum loss of \$2,717,000 in January 2012, which equates to a spread of almost \$3 million. The mean loss was \$367,000 with a standard deviation of \$529,000.<sup>48</sup>

Based on the pricing in the insurance market, using the mean plus an additive factor based on the standard deviation yields an appropriate market price. We have based the calculation on the observed monthly mean of \$367,000 and standard deviation of \$529,000. Using an approximate additive factor of 25% provides a monthly price of \$499,000.<sup>49</sup>

64. GBL stated that “in a mature insurance market for commodity risk, we would expect the base risk cost to be close to \$499,000.”<sup>50</sup>

65. GBL applied a second technique in determining the monthly recommended amount of \$832,000 as the upper end of the range. GBL used the distribution of DERS’ historical monthly losses to create a probability distribution that reflects DERS’ commodity risk exposure. GBL described how it quantified the commodity risk as follows:

Now that we have an appropriate distribution to quantify losses and the associated probabilities, we can use statistical metrics, such as VaR [value at risk] or CTE [conditional tail expectation] to quantify risk and use the mean and standard deviation to evaluate the price.

Our risk analysis was focused on CTE as this has become a more common risk measure in the actuarial industry and provides a better representation of the overall risk. It is also commonly used in determining insurance reserve amounts.

Since the above distribution is only focused on losses, using a CTE 80 based on the above results would result in the average of the worst 20% of monthly losses, not the worst 20% on an overall basis. To ensure we are accounting for the profits as well, we have adjusted the CTE thresholds applied to the model so that CTE 80 will provide the worst 20% taking into account that approximately 15.7% of the time there is a profit.

Our analysis focused on CTE 60 to CTE 80 as these are the risk measures commonly used to determine the reserve amounts. This provides a range of the amount an insurance company would likely hold to cover a month’s loss due to commodity risk.

Due to the heavy tail apparent in the distribution, the CTE figures are higher than the expected loss to cover the potential for a very high loss in a given month. This means an insurance company would hold \$832,000 to \$1,218,000 for each month to cover the potential claim amount. The CTE amounts are based on the loss distributions shown above, which were compiled based on the monthly losses over the 89 month period. The

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<sup>48</sup> Exhibit 22635-X0001, PDF page 20.

<sup>49</sup> Exhibit 22635-X0001, PDF page 34.

<sup>50</sup> Exhibit 22635-X0001, PDF page 34.

high loss periods, of which many occurred in the 2011 and 2012 calendar years, lead to the high CTE amounts shown above and from an insurance perspective have the propensity to occur again.<sup>51</sup>

66. GBL noted that the CTE amount using CTE 60 was \$832,000, and the CTE amount using CTE 80 was \$1,218,000.<sup>52</sup> GBL stated that “At a minimum, we would expect the insurance company to hold a reserve of \$832,000 in order to cover each month’s potential losses.”<sup>53</sup>

### 5.3 Recommendations from the interveners

67. The UCA recommended the use of the Beblow method as the method for calculating the CRC for DERS’ 2018-2020 EPSP. Mr. Retnanandan, on behalf of the CCA, proposed that the variable adaptive component of the Beblow method remain in place for the 2018-2020 EPSP. He recommended that the risk cycle component of the Beblow method be replaced with a static \$1.00/MWh charge.

### 5.4 Views of the parties

#### 5.4.1 The UCA

68. Mr. Jason Beblow and Dr. Sean Cleary submitted evidence on behalf of the UCA. Mr. Beblow indicated that the GBL insurance-based approach should not be accepted because it builds in a prospective gain on CRC, which translates into additional and unnecessary risk compensation.<sup>54</sup>

69. The UCA argued that the CRC should target profit and loss neutrality to the greatest extent possible. The UCA pointed to the regulation requirement that the risk margin “must not be considered as a part of the reasonable return.”<sup>55</sup> A reasonable person would be more than willing to assume commodity risks where a reasonable mechanism is in place to recover the prudent costs and expenses associated with the assumption of that risk; i.e., the risk margin, and the person is simultaneously entitled to a legislated profit or return consistent with the returns of other comparable retailers; i.e., the reasonable return.<sup>56</sup>

70. The UCA argued the CRC proposed by DERS is far from profit and loss neutral and would result in DERS receiving unreasonable and excessive compensation for commodity risk.<sup>57</sup>

71. The UCA argued that GBL does not have prior experience in pricing commodity risk. Further, when asked about its proposed 25 per cent additive factor used to set the lower bound of the CRC, GBL stated “... pricing metrics for insurance companies are proprietary and not released to competitors or the public, there is no source reference, outside of our personal experience, to specifically reference this pricing scheme.”<sup>58</sup> The UCA asserted that the

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<sup>51</sup> Exhibit 22635-X0001, PDF pages 33-34.

<sup>52</sup> Exhibit 22635-X0001, PDF page 34.

<sup>53</sup> Exhibit 22635-X0001, PDF page 35.

<sup>54</sup> Exhibit 22635-X0090, PDF page 40.

<sup>55</sup> *Regulated Rate Option Regulation*, Section 6(1)(b)(ii).

<sup>56</sup> Exhibit 22635-X0168, paragraph 13.

<sup>57</sup> Exhibit 22635-X0166, paragraph 22.

<sup>58</sup> Exhibit 22635-X0051, DERS-UCA-2017NOV10-016(c).

Commission should not rely on GBL's "industry knowledge and experience" in assessing the reasonableness of the range of recommended risk charge for products unfamiliar to GBL.<sup>59</sup>

72. The UCA referred to a submission from GBL that asserted that principles used to price commodity risk are not materially different from those for used for the pricing of more traditional insurance products.<sup>60</sup> Using a textbook relied on and cited by GBL, the UCA argued that there is no independent support to suggest that principles for the pricing of pure risks, which involve no possibility of gain, can equally be applied to speculative risks under which there is the potential for a gain. Past experience suggests that DERS will experience a monthly commodity profit, before the application of CRC.<sup>61</sup>

73. The UCA submitted GBL's approach ignores the potential for offsetting commodity gains, both before and after the application of CRC. This results in a significant over-estimation of DERS' exposure to commodity losses and, correspondingly, an over-estimation of the just and reasonable CRC required by DERS.

74. In considering the analysis conducted by GBL, the UCA pointed out that when asked about other probability distributions that could be used to fit the data available on profits and losses, such as the skewed normal or a skewed Student's t-distribution, GBL stated that it may be possible to use those distributions; however, the fit of the distributions would need to be tested. The UCA argued that GBL failed to consider other probability distributions that would account for both profit and losses. Further, GBL should have focused on finding the distribution that best fit the historical data set that includes both profits and losses.<sup>62</sup>

75. The UCA emphasized that GBL's analysis did not take into account the likelihood of commodity gains after the application of CRC. DERS confirmed it would have experienced an average monthly gain of \$618,594 if its proposed CRC of \$7.97/MWh had been in place over the June 2009 to October 2016 period. The UCA submitted that the GBL approach ignores the potential for offsetting commodity gains, before or after the application of CRC.<sup>63</sup>

76. Dr. Cleary prepared an analysis of the actual commodity gains received by DERS after the application of the actual CRC over the June 2009 to October 2016 period and contrasted this with the CRC that would have resulted under the proposed low end and high end of the GBL range for the same time period.<sup>64</sup> The results of Dr. Cleary's analysis are included in Table 2 below:

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<sup>59</sup> Exhibit 22635-X0166, paragraphs 49-51.

<sup>60</sup> Exhibit 22635-X0038, DERS-AUC-2017NOV09-011(b).

<sup>61</sup> Exhibit 22635-X0166, paragraphs 25-26.

<sup>62</sup> Exhibit 22635-X0166, paragraphs 38-39.

<sup>63</sup> Exhibit 22635-X0166, paragraphs 43-45.

<sup>64</sup> Exhibit 22635-X0096, PDF pages 14-16.

**Table 2. Dr. Cleary's comparison of historical commodity gains after actual CRC and back cast historical commodity gains using the GBL recommended CRC range**

		Monthly Profits	Monthly Profit	Annual Profit	Return on Revenue
Actual CRC	Average	70.79%	\$39,204	\$456,937	0.16%
	Median		\$197,464	\$1,055,708	0.36%
Low End of GBL Range (\$4.78/MWh)	Average	77.5%	\$224,028	\$2,160,477	0.74%
	Median		\$378,238	\$2,063,320	0.70%
High End of GBL Range (\$7.97/MWh)	Average	89.9%	\$618,594	\$6,648,997	2.27%
	Median		\$712,940	\$6,300,157	2.15%

77. Based on this analysis, the UCA argued that had the CRC proposed by DERS been applied in prior periods, DERS would have been vastly overcompensated for commodity risk. If either the low end or high end of GBL's proposed CRC range had been in place for the period of June 2009 to October 2016, DERS would have received an average CRC of between 0.74 and 2.27 per cent of revenues in addition to its established return margin of 1.3 per cent.<sup>65</sup>

78. The UCA compared the annual commodity gains DERS would have received had its recommended CRC of \$7.97/MWh been in place from June 2009 to July 2018, to the corresponding amounts if the Beblow method had been in place over the same time period. The results are included in Table 3 below:

**Table 3. UCA comparison of back cast net commodity gains from June 2009 to July 2018<sup>66</sup>**

Time Period	Net Commodity Gain (Loss) after DERS' Proposed CRC of \$7.97/MWh	Net Commodity Gain (Loss) Using Beblow Method
2009	\$6,214,184 <sup>1</sup>	N/A
2010	\$11,012,236	(\$712,329) <sup>3</sup>
2011	\$4,679,215	\$1,528,268
2012	\$2,613,777	\$2,515,571
2013	\$6,062,051	\$1,630,097
2014	\$6,300,157	(\$569,948)
2015	\$6,992,063	\$847,230
2016	\$8,885,795	\$1,942,597
2017	\$8,999,826	\$206,047
2018	\$4,444,871 <sup>2</sup>	(\$779,505)
<b>Total</b>	<b>\$66,204,175</b>	<b>\$6,608,028</b>

<sup>1</sup> Only includes data from June to December.

<sup>2</sup> Only includes data from January to July.

<sup>3</sup> Only includes data from July to December.

79. The UCA argued that these numbers alone should be sufficient to demonstrate that DERS proposed insurance-based CRC is unjust and unreasonable. The UCA submitted DERS has failed to demonstrate that gains similar in magnitude to those demonstrated in the historical lookback analysis, cannot reasonably be expected to materialize over the term of the EPSP should DERS' proposed CRC be approved. Moreover, "In the face of the real potential for excessive and unwarranted commodity gains should DERS' proposed CRC be adopted, the UCA submits the

<sup>65</sup> Exhibit 22635-X0166, paragraphs 56-63.

<sup>66</sup> Exhibit 22635-X0168, PDF page 15.

Commission must reject DERS' proposed CRC, just as it did in the Generic RRO Decision when faced with similar circumstances."<sup>67</sup>

80. The UCA referred to Decision 2941-D01-2015, in which the Commission acknowledged the following comment from DERS:

1141. Only when the underlying market volatility remains constant can a static risk compensation figure be effective. This would mean that there would be no substantive market rule changes, changes in law or policy, or changes to MSA guidelines that [a]ffect the energy market for the term of the EPSP. [footnote removed]<sup>68</sup>

81. The UCA argued that in a market dictated by increased volatility, DERS should prefer a CRC that is readily capable of adapting to changes in market volatility over time. However, DERS has proposed a fixed CRC, which over the June 2009 to September 2017 period would have only resulted in losses 10 per cent of the months during that time period. Thus, DERS would have been overcompensated for the assumption of commodity risks 90 per cent of the months. As a result, DERS would have no reasonable likelihood of any net commodity loss, but a high probability of a significant gain.<sup>69</sup>

82. The UCA argued an adaptive CRC methodology that adjusts based on actual experience such that the CRC is able to cover a broad spectrum of market conditions without consistently overcompensating or undercompensating the RRO provider, must be preferred to the static CRC advocated by DERS.<sup>70</sup>

83. While DERS suggested that it requires additional risk compensation because it is risk averse, the UCA considered that DERS missed the mark with respect to its discussion on risk aversion, given the Commission's findings in Decision 20416-D01-2015:

The review panel considers that the hearing panel did not say that there was no evidence in the variability and risk between revenues and costs, but it stated that it had no information to determine how the revenues and costs associated with the procurement of load relates to risk aversion.<sup>71</sup>

84. The UCA pointed out that DERS has not established any credible link between the additional compensation requested and its level of risk aversion.<sup>72</sup>

85. The UCA argued that the RCA will not lead to a systematic under-recovery of losses, as the Beblow method relies on both variable risk compensation and the RCA to compensate for commodity risk. Further, the Commission dismissed the argument that the Beblow method does not account for attrition, contrary to the submissions of DERS.

86. The UCA did not agree with DERS' submission that GBL's methodology represents a market-based approach to pricing commodity risk. The UCA stated that a market-based approach

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<sup>67</sup> Exhibit 22635-X0168, paragraph 33.

<sup>68</sup> Decision 2941-D01-2015, paragraph 1141.

<sup>69</sup> Exhibit 22635-X0166, paragraph 69.

<sup>70</sup> Exhibit 22635-X0166, paragraph 70.

<sup>71</sup> Decision 20416-D01-2015: Review and Variance of Decision 2941-D01-2015: Regulated Rate Tariff and Energy Price Setting Plans – Generic Proceeding: Part B – Final Decision, Proceeding 20416, Applications A001, A002, September 3, 2015, paragraph 148.

<sup>72</sup> Exhibit 22635-X0166, paragraph 77.

is one in which pricing is established based on competition and the principles of supply and demand. In contrast, GBL provided an insurance-based approach to pricing commodity risk. The onus lies on the applicant to demonstrate that the CRC is just and reasonable and GBL has not provided any independent support to demonstrate that the statistical methods for pricing traditional insurance products also apply to pricing commodity risk.

87. Further, the UCA argued that unlike losses experienced under property or casualty insurance, commodity losses have the potential to be offset by commodity gains in subsequent months. Thus, commodity risk may be classified as a speculative risk, which according to GBL is generally not insurable.<sup>73</sup>

#### 5.4.2 The CCA

88. Mr. Retnanandan submitted that in order to eliminate the distortions caused by GBL's use of absolute dollar values for commodity gains and losses in a declining volume environment, GBL's distribution should be analyzed based on dollars per MWh. Mr. Retnanandan performed such an analysis,<sup>74</sup> which showed a standard deviation of \$3.93/MWh. Based on his analysis, Mr. Retnanandan submitted that "The adaptive CRC in contrast to a fixed CRC, tends to reduce the variability of the distribution. This means the adaptive CRC approach approved in Decision 2941-D01-2015 if continued would suggest a lower CRC than would be the case based on the GBL analysis."<sup>75</sup>

89. Mr. Retnanandan indicated that an RCA component of CRC is required to mitigate the probability for losses intra month and from year to year. Noting GBL's consideration "that a risk premium based on 25 per cent of the standard deviation would sufficiently address the reduction in the chances of making losses while increasing the chances of making gains,"<sup>76</sup> Mr. Retnanandan noted that 25 per cent of the standard deviation of \$3.93/MWh from his analysis results in a figure of approximately \$1/MWh. Mr. Retnanandan recommended that \$1/MWh be used for the RCA component of the CRC for DERS' 2018-2020 EPSP.<sup>77</sup>

90. The CCA argued that one of the considerations in the design of the CRC is that the structure and level of the CRC should be sufficient to mitigate the occurrence of unsustainable cash flow shortfalls arising from consecutive months of commodity losses. Other considerations are that it should provide an incentive for the RRT provider to forecast accurately and provide price signals to RRO customers. Based on Mr. Retnanandan's evidence, the CCA recommended that the adaptive CRC approved by the Commission in Decision 2941-D01-2015 continue, and an RCA of \$1.00/MWh be awarded as a risk premium, on a prospective basis, to increase the probability of gains versus losses for DERS.<sup>78</sup>

91. The CCA submitted that Mr. Retnanandan's methodology better matches the risk premium to the go-forward risk, considering two important factors. First, GBL's analysis reflected the high variability of the net gain loss distribution arising from the use of absolute historical gain loss dollars, whereas Mr. Retnanandan used gain and loss values per MWh, by month to assess the variability of net gain or loss by removing any noise from factors not related

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<sup>73</sup> Exhibit 22635-X0168, paragraph 23.

<sup>74</sup> Exhibit 22635-X0087, paragraph 20.

<sup>75</sup> Exhibit 22635-X0087, paragraph 21.

<sup>76</sup> Exhibit 22635-X0087, paragraph 22.

<sup>77</sup> Exhibit 22635-X0087, paragraph 30.

<sup>78</sup> Exhibit 22635-X0165, paragraph 19.

to pure variability of gains and losses. Second, GBL's insurance approach is predicated on the assumption that customers should pay a risk premium to insure DERS against commodity trading gains and losses as well as against the variability of such gains and losses. By using an adaptive CRC to forecast the cost recovery component, Mr. Retnanandan's analysis determined a risk premium that was applicable to the variability of forecast net gains and losses.

92. The CCA argued that GBL's use of absolute gains and losses tends to exaggerate the variability of gains and losses. For these reasons, the CCA recommended that the lower bound of GBL's CRC of \$4.78/MWh be rejected.

93. Considering GBL's recommended upper range for CRC of \$7.97/MWh, which is based on an insurance company holding a reserve of \$832,000 to cover each month's potential loss, the CCA pointed out that "GBL assumes each gain loss event to be a discrete event."<sup>79</sup> In reality net gain and net loss events of an RRT provider occur in chronological sequence, and not as random discrete events.

94. Further, the CCA argued that the \$832,000 reserve requirement is based on applying faulty insurance assumptions to the operations of an RRT provider. It added that there is no evidence on the record to suggest that during the term of the 2018-2020 EPSP, the high loss months would be any higher than those that occurred during the analysis period.<sup>80</sup>

95. Based on these views, the CCA considered that Mr. Retnanandan's proposal for CRC addresses the issue of risk compensation more efficiently than the GBL method. As such, the currently approved adaptive CRC and a risk premium of \$1.00/MWh should be approved for DERS.

### 5.4.3 DERS

96. DERS argued that its CRC proposal is a sound, empirically-based approach to calculating CRC. It provides a prospective, fact-based method to determine the cost of the financial risks faced by DERS. Further, the proposed CRC as supported by the evidence of GBL, meets the requirements of the regulation and covers the risks set out in Section 5(3) of that regulation.

97. In response to intervener challenges to the distribution used by GBL to analyze the commodity gains and losses, GBL confirmed that there were over 50 probability distributions against which the data set could be assessed. GBL stated:

- i. GBL chose to focus on a selection of well-known distributions that GBL believed could potentially fit with the losses and, based on GBL's statistical knowledge, knew the properties would complement the data set.

Following the fitness testing, the results showed that for the modeling of losses any of the distributions already tested could be a good-fit and therefore GBL did not believe it was necessary to spend additional time fitting other distributions.

- ii. When trying to fit a distribution to losses only, GBL considered the exponential, gamma, Weibull, and beta distributions, as these were considered appropriate fits

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<sup>79</sup> Exhibit 22635-X0165, paragraph 36.

<sup>80</sup> Exhibit 22635-X0104.

based on GBL's statistical expertise. As these distributions yielded appropriate fits, the investigation of additional distributions was not required.<sup>81</sup>

98. DERS stated that the GBL approach used for pricing the CRC accounts for the full spectrum of commodity pricing outcomes, including profits and losses. In response to Dr. Cleary's criticism that the GBL approach was flawed because it ignored the potential for profits, GBL explained how it incorporated DERS aggregate profits and losses, as follows:

- (a) The pricing range was based on an analysis of commodity profit or loss incurred by DERS in the historical period. Therefore, as the calculation of the range is based on this profit/loss data directly, the recommendation does incorporate the historical profits and losses experienced by DERS pertaining specifically to commodity risk.

GBL considers historic profits/losses to be aggregate profits/losses because they were not broken down based on the source of the profit/loss. In other words, GBL did not breakdown how much of each year's profit/loss was caused by forecast, shaping, and pricing errors when determining the recommended risk margin.<sup>82</sup>

99. DERS noted that GBL has explained that in pricing risk, the insurance market uses the mean plus an additive factor based on the standard deviation. In its analysis, GBL determined the mean monthly loss was \$367,000, with a standard deviation of \$529,000. Based on that, GBL stated that a reasonable range for the additive factor is between 15 to 40 per cent of the standard deviation and it included an additive factor of 25 per cent.

100. In response to the UCA's argument that DERS' proposed CRC would over compensate DERS by building in a guaranteed prospective gain, DERS stated that the UCA's look back analysis used a timeframe in which there was a downward trend in commodity prices and an associated decrease in volatility. DERS provided the following table showing the probability of monthly gains and losses under the low and high end of the GBL CRC range:<sup>83</sup>

**Table 4. DERS monthly gains/(losses) using the range of CRC recommended by GBL, June 2009 – September 2017**

	A	B	C
		Low End (\$4.78/MWh)	High End (\$7.97/MWh)
1	Probability of Monthly Loss	22%	10%
2	Value of Maximum Monthly Loss (,000)	(\$1,965)	(\$1,464)
3	Value of Maximum Monthly Gain (,000)	\$929	\$1,491

101. DERS argued that Mr. Retnanandan's proposed RCA approach would leave customers with a portion of the risk because DERS would take on only that portion of the risk represented by the fixed RCA of \$1.00/MWh. The remainder of the risk, represented by the adaptive component of the CRC, would then fall on, and presumably be paid for, by customers.<sup>84</sup> Further, Mr. Retnanandan's proposal would ascribe disproportionate weight to profitable months with

<sup>81</sup> 22635-X0150, DERS-UCA-2018JUL27-009(c).

<sup>82</sup> Exhibit 22635-X0144, DERS-AUC-2018JUL27-007(a).

<sup>83</sup> Exhibit 22635-X0128, paragraph 12, Table 3.

<sup>84</sup> Exhibit 22635-X0176, paragraph 14.

lower consumption and allow them to offset large commodity losses that occur in months with larger consumption.<sup>85</sup>

102. DERS asserted that the Beblow method delays the recovery of losses, and in the event of one or two large losses in a single calendar year, DERS could be in a loss position for more than two years.<sup>86</sup>

103. DERS also noted that it will continue to experience net attrition on an annual basis. It submitted that the RCA under the Beblow method results in an under-collection of losses almost equivalent to the percentage of net attrition. DERS demonstrated that, for example, a five per cent net attrition drives an under-collection of four per cent, supporting the conclusion that "... the RCA fails to compensate for the losses incurred during the first cycle."<sup>87</sup>

104. DERS argued that the evidence from GBL satisfies the criteria described in Decision 2941-D01-2015, where the Commission stated that it "... considers that evidence based on all of the statistical properties of the distribution of historical differences between revenues and costs may be important for determining risk compensation, for example, skewness, standard deviation, expected value, and observation frequency."<sup>88</sup> As such, DERS' proposed CRC should be accepted because it is more comprehensive than the Beblow method and provides proper consideration of the statistical properties of the historical differences between revenues and costs.<sup>89</sup>

105. DERS pointed out that the Beblow method exposes customers to the risk of CRC volatility. DERS added that the Beblow method allows the full transfer of risk and price volatility to customers since the CRC that customers pay in any given month does not isolate them from the effect of losses in that month.<sup>90</sup> Therefore, DERS argued that its fixed CRC amount should be preferred over the Beblow method.

106. Regarding the qualifications of GBL, DERS pointed out that GBL has not claimed to be an expert in valuing energy commodity risk in Alberta. Rather GBL is an actuarial consulting firm with knowledge of the insurance industry.

107. With respect to the UCA's position that GBL made no effort to account for the protection provided by commodity gains into the reserve amount held by DERS to offset future losses, DERS responded that insurance premiums are priced such that "over a given period the premiums collected should be sufficient to cover the cost of any losses paid for by the insurer for the insurance product. Once the given period has ended, the insurer will reassess the premiums taking into account their new experience over that period."<sup>91</sup> GBL recommended that premium or the MWh CRC amount be reassessed with each EPSP and premiums will not be changed before the end of the insured period.

108. In response to the UCA's claim that the proposed CRC of \$7.97/MWh would lead to overcompensation, DERS pointed out that the calculations supporting the UCA's claim were

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<sup>85</sup> Exhibit 22635-X0176, paragraph 18.

<sup>86</sup> Exhibit 22635-X0164, paragraph 86.

<sup>87</sup> Exhibit 22635-X0080, DERS-UCA-2018JAN26-002(d).

<sup>88</sup> Decision 2941-D01-2015, paragraph 1097.

<sup>89</sup> Exhibit 22635-X0164, paragraphs 92-94.

<sup>90</sup> Exhibit 22635-X0164, paragraphs 135-136.

<sup>91</sup> Exhibit 22635-X0164, paragraph 75.

over periods of low commodity risk, and it creates an illusion of profitability that should not have occurred in a well-functioning market.<sup>92</sup>

109. DERS argued that if commodity risk continues to materialize at the same level experienced from May 2018 through August 2018, then the RCA would only provide DERS with partial compensation based on the current level of risk, and not offer any relief for the previously incurred losses. As a result, DERS will never have the ability to fully recover its losses, and will be denied a reasonable opportunity to fairly recover the costs and expenses it incurs in carrying the financial risk of providing RRO service.<sup>93</sup>

## **5.5 Commission findings**

### **5.5.1 DERS CRC proposal**

110. For the reasons that follow, DERS has not satisfied the Commission that its proposed CRC methodology results in a just and reasonable CRC that covers the risks associated with the supply of electricity to RRO customers.

#### **Lack of transparency**

111. As part of its recommended lower CRC range of \$499,000, GBL included an additive factor of 25 per cent of the standard deviation associated with the historical monthly net commodity gains/losses of DERS over the 89 months from June 2009 to October 2016. GBL selected the 25 per cent from what it described as a reasonable range of “15%-40%,”<sup>94</sup> based on the risk exposure embedded in the product.<sup>95</sup> When asked specifically to provide any independent support or justification for using an approximate additive factor of 25 per cent in these circumstances, GBL replied as follows:

With over fifty years working in the actuarial industry, many years were spent working with the pricing and reserving of insurance. During work in pricing insurance, GBL has seen a common approach for pricing as a baseline (or average) plus an additive factor for risk variance. This risk variance additive factor will depend on the type of risk and risk characteristics however GBL has seen products priced using an additive factor within the range GBL provided and the 25% specifically. As pricing metrics for insurance companies are proprietary and not released to competitors or the public, there is no source reference, outside of our personal experience, to specifically reference this pricing scheme.<sup>96</sup>

112. GBL noted that the additive factor depends on the type of risk and the risk characteristics, and it has seen products priced using a specific additive factor of 25 per cent. While the Commission acknowledges GBL’s knowledge and experience in the insurance industry, generally, GBL acknowledged that there is limited industry experience pricing commodity risk, that there is no existing insurance market for commodity risk and that it has no previous experience pricing commodity risk. These factors limit the Commission’s ability to understand, test and analyze GBL’s use of 25 per cent as a reasonable additive factor for determining DERS’

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<sup>92</sup> Exhibit 22635-X0164, paragraphs 83-84.

<sup>93</sup> Exhibit 22635-X0176, paragraph 108.

<sup>94</sup> Exhibit 22635-X0001, PDF page 10.

<sup>95</sup> Exhibit 22635-X0001, PDF page 10.

<sup>96</sup> Exhibit 22635-X0051, DERS-UCA-2017NOV10-016.

CRC. All this serves to limit the weight the Commission might otherwise afford to this aspect of GBL's evidence.

113. Further, the Commission continues to agree with its previous comments on the limitations associated with reviewing results from proprietary analysis or proprietary data:

355. While there is nothing inherently wrong with using proprietary data in regulatory proceedings, procedural fairness requires that parties must be provided with the opportunity of a fair hearing in which each party is given the opportunity to respond to the evidence against its position. This requirement clearly requires parties and the Commission to be able to fully understand, test and respond to the evidence filed in a proceeding. Further, the Commission has the obligation to provide reasons for its decisions. It can only do so if it is able to fully understand, test and analyze the evidence filed before it.<sup>97</sup>

### **GBL's determination of the upper range for CRC**

114. The Commission recognizes that risk measures like standard deviation or conditional tail expectation, as employed in GBL's report, are well known and, depending on the circumstance, are generally accepted measures of risk. Nonetheless, the Commission has concerns with GBL's analysis and approach.

115. The Commission is concerned with the method by which GBL elected to focus only on the loss data. GBL plotted the actual monthly commodity gains and losses from the June 2009 to October 2016 period. The plotted data resembled a Gamma distribution but the support of the Gamma distribution is non-negative; as a result, a Gamma distribution cannot be fitted to data that includes both profits and losses, if profits and losses involved positive and negative numbers. As a result, GBL shifted the data to incorporate both profits and losses. Based on these adjusted data, GBL was able to determine a fitted Gamma distribution.

116. In order to determine if the Gamma style distribution was the appropriate fit, GBL plotted the cumulative distribution function using the actual profit and loss data, not the adjusted data. Because this cumulative distribution function did "not follow the anticipated path based on ... known distribution functions," GBL decided to focus only on the loss data.

117. When offered "known distribution functions" that had the possibility of fitting the actual profit and loss data, such as a skewed normal or a skewed Student's t, GBL indicated it was possible that these other distributions could be used to incorporate the effects of both gains and losses. GBL also stated that it was unknown whether these distributions would closely fit the gains and losses and that further testing would be required to determine goodness-of-fit. Neither DERS nor GBL examined these known distributions.<sup>98</sup>

118. In view of these facts, the Commission does not accept GBL's process for deciding to focus only on the loss data. The Commission agrees with the UCA, who submitted that GBL failed to consider other probability distributions that would account for both profit and losses. The Commission also agrees with the UCA's submission that GBL should have focused on finding the distribution that best fit the historical data set that includes both profits and losses,

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<sup>97</sup> Decision 2012-237: Rate Regulation Initiative, Distribution Performance-Based Regulation, Proceeding 566, Application 1606029-1, September 12, 2012.

<sup>98</sup> Exhibit 22635-X0001, PDF page 33. Exhibit 22635-X0144, DERS-AUC-2018JUL27-008.

rather than focusing only on the distribution of the losses, and making a subsequent arithmetic calculation to account for the profits.

119. GBL explained its adjustment to the CTE analysis to account for profits as follows:

(a) Since the loss distribution is only a distribution of approximately 84.3% of the total results (as approximately 15.7% of the time there is a profit), the worst 20% of the loss curve would truly represent the worst 16.9% overall (20% x 84.3%). Therefore, to determine the worst 20% overall, GBL would have to look at the worst 23.7% of the loss curve (20% / 84.3%). The worst 23.7% on the loss curve would equate to the worst 20% on an aggregate basis. Therefore CTE 80 was computed as the average of the largest 23.7% of losses or the average of the losses in the 76.3 percentile.<sup>99</sup>

120. GBL has not demonstrated sufficiently whether this arithmetic calculation, which accounts for the fact that approximately 15.7 per cent of the time there are profits, reflects the dollar amount of these profits. Instead, it adjusts the worst percentage of losses that are used in determining the various CTE amounts. Consequently, it is unclear whether the resulting CTE amounts sufficiently account for the dollar amount of the gains.

### **The use of an insurance based reserve methodology to determine the upper bound of the CRC**

121. GBL indicated that its analysis “focused on CTE 60 to CTE 80 as these are the risk measures commonly used to determine the reserve amounts.”<sup>100</sup> GBL noted that the reserve amount associated with a CTE 60 was \$832,000 and the reserve amount associated with a CTE 80 was \$1,218,000. GBL commented that:

Due to the heavy tail apparent in the distribution, the CTE figures are higher than the expected loss to cover the potential for a very high loss in a given month. This means an insurance company would hold \$832,000 to \$1,218,000 for each month to cover the potential claim amount. The CTE amounts are based on the loss distributions shown above, which were compiled based on the monthly losses over the 89 month period. The high loss periods, of which many occurred in the 2011 and 2012 calendar years, lead to the high CTE amounts shown above and from an insurance perspective have the propensity to occur again.<sup>101</sup>

122. GBL used \$832,000 as the upper bound of its recommended CRC range. This is the amount associated with a CTE 60, based on GBL’s analysis. GBL stated that “At a minimum, we would expect the insurance company to hold a reserve of \$832,000 in order to cover each month’s potential losses.”<sup>102</sup>

123. Mr. Retnanandan expressed a concern with the high end of the CRC recommended by GBL. He submitted the following:

GBL states, an insurance company would expect to hold a reserve of \$832,000 in order to cover each month’s potential losses. However, since the amount is a reserve to be called upon in the event of losses, collection of this amount through the CRC in every month is

<sup>99</sup> Exhibit 22635-X0051, DERS-UCA-2017NOV10-016(a).

<sup>100</sup> Exhibit 22635-X0001, PDF page 34.

<sup>101</sup> Exhibit 22635-X0001, PDF page 34.

<sup>102</sup> Exhibit 22635-X0001, PDF page 34.

not warranted. If anything, it is the carrying cost of this reserve that needs to be factored into the CRC calculation rather than the reserve amount itself. Assuming a 6.01% cost of capital as per DERS' non-energy application the carrying cost on the above noted reserve would amount to \$0.043 per MWh, which is not a significant number.<sup>103</sup>

124. The Commission considers that Mr. Retnanandan's submission has merit. Under the CRC methodology proposed by DERS, it is forecast to receive \$832,000 in CRC every month during the term of the 2018-2020 EPSP. DERS did not explain how this forecast collection of \$832,000 every month would result in it holding "a reserve of \$832,000 in order to cover each month's potential losses," as recommended by GBL.

125. Reserve accounts in the regulated utility industry, such as hearing cost reserves and reserves for injuries and damages, are generally used to prefund expected future costs. The reserve accounts are subsequently adjusted to account for the actual costs, with the result being that customers only pay for the actual prudent costs incurred by the utility. Customers are also given credit for any prefunding through the use of no cost capital, as described by Mr. Retnanandan. The utility does not have the opportunity to benefit financially from the establishment of a reserve account. Reserve accounts have properties that are similar to deferral accounts, except they are generally prefunded.

126. The Commission finds that the CRC of \$7.97/MWh requested by DERS does not function like a typical reserve account for a utility. The main distinguishing feature is that there is no reserve adjustment mechanism during the EPSP period that would account for the actual commodity losses. If no losses arise over several months, and DERS continues to collect \$832,000 on a monthly basis, the amount to be held in reserve could deviate widely from \$832,000. This could result in customers paying for a reserve amount that is well in excess of \$832,000, even to the point where DERS would not suffer a loss even if it were to face its largest known monthly commodity loss..

127. DERS acknowledged that a CRC based on the reserve concept used in the insurance industry may over collect the forecast risk amount and would need to be reassessed. DERS stated the following:

75. ... If premiums exceed costs at the beginning of a period, an insurer will hold a reserve to protect themselves from the case where costs exceed premiums later in the period. Once the given period has ended, the insurer will reassess the premiums taking into account their new experience over that period. If the insurer is holding substantial reserves at the end of the period, premiums will likely be decreased at that time to account for the positive experience. Most importantly, premiums will not be changed before the end of the insured period.<sup>104</sup>

...

77. In this case, GBL has recommended that the "premiums" charged by DERS, that is, the per MWh CRC amount, be reassessed with each EPSP. [emphasis removed]<sup>105</sup>

<sup>103</sup> Exhibit 22635-X0087, paragraph 29.

<sup>104</sup> Exhibit 22635-X0176, paragraph 75.

<sup>105</sup> Exhibit 22635-X0176, paragraph 77.

128. The Commission considers the reserve concept associated with GBL's CTE approach, to be inconsistent with the Commission's responsibility to set just and reasonable rates. To the extent that losses in any given month do not exceed the proposed reserve amount, the CRC amount collected in the following month would not be adjusted. This could result in CRC rates that are not just and reasonable.

129. For these reasons, the Commission considers that the use of an insurance-based reserve methodology to determine the CRC for DERS is not acceptable.

130. While DERS indicated that it would examine the CRC amount as part of each EPSP application, (reassess the premium charged by DERS with each EPSP), the Commission finds that this will not address the potential financial benefits that could accrue to DERS during the term of the 2018-2020 EPSP, if the \$7.97/MWh CRC is approved.

### **Fixed versus adaptive CRC**

131. DERS requested a fixed rate CRC of \$7.97/MWh for the entire term of the 2018-2020 EPSP to mitigate what it identified as two shortcomings associated with the use of the Beblow method: (1) under compensation for financial risk; and (2) the magnitude of risk exposure due to market volatility. DERS argued that its proposed fixed rate CRC would more fairly compensate it for the financial risks it assumes and expose DERS to less risk. This proposition is not sufficiently supported on the record.

132. As discussed in greater detail below, because of its fixed nature, the CRC requested by DERS is incapable of responding to changes in market volatility. In contrast, the Commission has previously determined that the adaptive nature of the Beblow method will ensure that the RRO provider is sufficiently remunerated for bearing commodity risk. In Decision 20416-D01-2015 the Commission stated:

146. In consideration of the legislative framework, the hearing panel approved a methodology that was submitted on the record of the proceeding by Mr. Beblow (the expert for the UCA) which provides coverage for systematic losses. This methodology is not the same as the methodologies urged upon the Commission by Direct Energy and EPCOR. Nevertheless, the record of the impugned proceeding shows that even though there is no specific element or line item in the Beblow method that identifies a value for variability or volatility risk, the Beblow method is designed to sufficiently cover commodity risks. The hearing panel chose a method that does not separately identify all risk elements and assign a number or methodology to each element.<sup>106</sup> [emphasis added]

133. In the judgement of the Commission, no new, persuasive evidence was offered in this proceeding to cause the Commission to come to a conclusion contrary to that stated above.

134. A fixed rate CRC is not designed to respond to unexpected changes in market volatility that may occur and were not accounted for in determining the fixed rate CRC. These unexpected and unaccounted for changes in market volatility could result in less volatility than expected, or more volatility than expected. If the market volatility is more than expected, then DERS may suffer more losses than expected, with no ability to adjust its CRC to address this matter. In this

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<sup>106</sup> Decision 20416-D01-2015: Review and Variance of Decision 2941-D01-2015:Regulated Rate Tariff and Energy Price Setting Plans – Generic Proceeding: Part B – Final Decision, Proceeding 20416, September 3, 2015.

event, DERS may not have a reasonable opportunity to recover costs prudently incurred or receive just and reasonable compensation for the commodity risk assumed. If the market volatility is less than expected, then as described above, the result will be that customers may be paying CRC that is not just and reasonable. A fixed CRC in the form proposed by DERS does not necessarily mean that DERS is exposed to less risk.

135. Considering whether DERS is fairly compensated for the risks it takes, in response to an IR in this proceeding, Mr. Beblow stated:

... that recent market data is a good indication of risks currently being faced by the provider and using actual data provides a good estimate that can be applied to future periods. The Beblow CRC is not attempting to reflect the full distribution of risks faced by an RRO provider, it is attempting to address the risks of the market currently faced by the RRO provider. While, these historical risks may not perfectly reflect the short term future period, the adaptive nature of the Beblow CRC along with the RCA component will ensure that the RRO provider is sufficiently remunerated over diversified volatility and pricing scenarios as per my evidence in this proceeding.<sup>107</sup> [emphasis added]

136. The UCA presented evidence comparing the net gain that would have been realized by DERS using the CRC amounts under the Beblow method and DERS' proposed \$7.97/MWh over the 2009-2018 period. Under DERS' proposed CRC, it would have realized net commodity gains of \$66 million compared to \$6 million under the Beblow method. While DERS argued that this and other similar time periods in the look-back analysis were biased as low commodity prices and low volatility existed during that time frame, the Commission considers that the \$60 million difference far outweighs the bias identified by DERS that may be claimed as a result of the time period used.

137. In consideration of all of the above, the Commission remains satisfied that the Beblow method, which results in a CRC value that changes every month, is preferable to DERS' fixed rate CRC proposal.

138. The Commission has also previously considered whether the CRC, which is meant to address commodity price and volume risks, should be static (fixed) or adaptive (variable) in order to be able to respond to changing market conditions. In Decision 2941-D01-2015, the Commission espoused the benefits of an adaptive CRC as follows:

1192. The proposed adaptive component reduces the probability of the RRO providers earning excessive commodity gains, and would ensure that consumers pay CRC that is continually reflective of market risk.

139. In Decision 20448-D01-2017, the Commission further explained the properties of the Beblow variable component of the CRC method:

... The question to be answered by the Commission is whether or not the variable component of the CRC should respond to changes in the level of the base energy charges. The Commission considers that the base energy charge is reflective of the forward market prices for electricity during the time period that the hedges, which underpin the base energy charge, were executed. In Decision 2941-D01-2015, the Commission considered it was important that any changing market conditions be reflected in the variable component of the CRC on a timely basis. The Commission

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<sup>107</sup> Exhibit 22635-X0108, UCA-DERS-2018MAR16-008.

considers that changes in the forward market prices and, consequently, changes in the base energy charges, are reflective of changing market conditions. Therefore, the Commission finds it important that changes in the level of the base energy charge should be included in the variable component of the CRC. This is reasonably accomplished using the “Beblow method.”<sup>108</sup>

140. In its application, DERS implicitly acknowledged the limitations of a fixed rate CRC. Among the reasons advanced by DERS for why it should receive CRC at the upper bound of the GBL recommended range DERS stated the following:

One key risk is that DERS is prevented from increasing the CRC to reflect actual experience for the duration of the EPSP. Should greater than anticipated losses occur, DERS would incur such losses without the ability to pass them on to DERS’ customers.<sup>109</sup>

141. DERS also stated the following:

Furthermore, DERS notes that CRC of \$5.79/kWh was included in its September 2018 RRO as a result of three consecutive months of Commodity Losses after CRC for May, June and July of 2018, summing to \$1,037,268.<sup>110</sup>

142. The Commission recognizes these losses occurred. However, these losses factored into the RCA calculation and resulted in an RCA amount of \$4.32/kWh, as demonstrated in the monthly rate filings from September 2018 to November 2018. The Commission considers this demonstrates the timely manner in which the current CRC method adapts to changing market conditions.

### **Overall conclusion on DERS’ proposed CRC**

143. For all the above reasons, the Commission denies the CRC methodology proposed by DERS. The Commission continues to hold the view that an adaptive CRC better aligns with a CRC that covers risk associated with energy related costs for providing RRO service, that is, a just and reasonable financial compensation for commodity risk. The adaptive nature will better account for volatility over time, making it preferable over DERS’ proposed fixed CRC.

144. As the Commission is unable to approve DERS’ proposed CRC, its consideration of the options presented by the interveners, namely the Beblow method, and the modified Beblow method proposed by the CCA, is detailed in the sub-sections that follow.

### **5.5.2 Mr. Retnanandan’s proposal**

145. As described in Section 5.4.2 Mr. Retnanandan recommended that the RCA be fixed for the EPSP term at \$1.00/MWh. He opined that this alternative approach to RCA provides better incentives to the RRO provider concerning forecast accuracy and minimizes the risk of losses.

146. As evidenced by the CCA, its proposal for \$1.00/MWh is based on the use of a 25 per cent additive factor of the standard deviation, which was recommended and used by GBL in its analysis. Given the Commission’s previously stated findings concerning the lack of visibility

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<sup>108</sup> Decision 20448-D01-2017, paragraph 506.

<sup>109</sup> Exhibit 22635-X0005, PDF page 34, lines 10-12.

<sup>110</sup> Exhibit 22635-X0164, paragraph 84.

into this 25 per cent additive factor, the Commission finds that it is similarly unable to assess the reasonableness of the CCA's proposed RCA.

147. This conclusion is also consistent with comments previously made by the Commission about the relative merits of a subjective standard deviation approach and the RCA as calculated under the Beblow method. In Decision 2941-D01-2015, the Commission stated:

1219. The Commission finds that Mr. Beblow's proposal for the fixed, risk cycle component provides a reasonable method for the RRO providers to forecast what their expected net systematic gains and losses will be over the subsequent 12 months, by using information about the net systematic gains and losses from the previous 12 months. The Commission prefers this approach rather than the subjective standard deviation based adjustments proposed by the other parties.<sup>111</sup>

148. DERS argued the CCA based its recommendation on data that was biased. Specifically, the time period in the CCA's analysis had significantly diminished volatility levels that were uncharacteristic of the Alberta market.<sup>112</sup>

149. The Commission agrees that past market volatility was at low levels. However, as previously discussed by the Commission, a fixed CRC whether it be the total amount or one component as suggested by the CCA, has the potential of undercompensating or overcompensating the RRO provider depending on the nature of the losses or gains. Thus, the Commission is not persuaded to approve a fixed RCA as proposed by the CCA.

150. Further, in considering the differences between the CCA's proposal and the Beblow method, the UCA pointed out that:

The key distinction is that the CCA's recommended RCA incorporates a "standard deviation based adjustment" such that it will always be a positive value, whereas the RCA under the Beblow Method has the potential to be zero if market conditions so warrant.<sup>113</sup>

151. The Commission considers that the UCA's statement highlights the importance of a variable RCA, since it adjusts to compensate the RRO provider for the risks that it is facing. When those risks diminish, the RCA also diminishes.

152. Based on the Commission's inability to assess the reasonability of the 25 per cent additive factor in the CCA's proposed RCA and the fixed nature of the CCA's proposed RCA, the Commission cannot approve Mr. Retnanandan's proposal.

### 5.5.3 Beblow method

153. As previously noted, the Beblow method of CRC is the Commission-approved methodology currently in place for DERS' 2016-2018 EPSP. The UCA provided evidence and submissions that the Beblow method of CRC should continue for DERS' 2018-2020 EPSP.

154. DERS argued against the continued use of the Beblow method on grounds that it undercompensates DERS for its commodity risk and increases rate volatility for customers.

<sup>111</sup> Decision 2941-D01-2015, paragraph 1219.

<sup>112</sup> Exhibit 22635-X0128, DERS' rebuttal evidence, page 9, Figure 1.

<sup>113</sup> Exhibit 22635-X0168, paragraph 8.

DERS argued that the Beblow method undercompensates it for commodity risk because, the Beblow method of CRC:

- (a) is premised on an assumption that DERS is a risk neutral entity,<sup>114</sup> contrary to clear evidence that DERS is risk averse as a standalone business<sup>115</sup>
- (b) fails to price risk but instead attempts to reimburse for historical losses<sup>116</sup>
- (c) cannot provide fair compensation in the expected circumstances of increasing commodity prices, increasing volatility and cumulative losses<sup>117</sup>
- (d) potentially leaves DERS in a cumulative loss position over a number of years because of a lag in the RCA's collection time and does not account for expected net site attrition (it does not account for a smaller customer base in the following year)<sup>118</sup>

155. DERS also submitted that another flaw in the Beblow CRC method is the fact that it exposes customers to the risk of a fluctuating CRC amount.<sup>119</sup>

156. For the reasons that follow, DERS has failed to satisfy the Commission on any of the above grounds.

### **Risk aversion**

157. DERS has failed to demonstrate or offer any persuasive support for its contention that the Beblow method and the Commission's approval of it for the purposes of DERS' 2016-2018 EPSP, is premised on the assumption that DERS is a risk neutral entity.

158. In Decision 2941-D01-2015, the Commission stated, "there is no way to decide the level of risk aversion of the RRO providers."<sup>120</sup>

159. In Decision 2941-D01-2015, the Commission stated:

1084. All parties agreed that when faced with systematic losses, so that the expected value of the percentage difference between revenues and costs is negative, the RRO providers should receive compensation so that the expected value, after compensation, for the percentage difference between revenues and costs, is zero.

1085. The UCA refers to this property as profit and loss neutrality. All parties agreed that the RRO providers should be compensated for risk, which includes the uncertainty of the differences between revenues and costs, so that the RRO providers do not experience losses on average.

1086. The Commission considers that requiring RRO providers to sustain prudently incurred systematic losses, so the expected value of an uncertain level of revenues and costs is negative, results in a cost for which there should be compensation that is included in the risk margin.

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<sup>114</sup> Exhibit 22635-X0005, PDF page 8.

<sup>115</sup> Exhibit 22635-X0005, PDF page 24.

<sup>116</sup> Exhibit 22635-X0005, PDF page 27.

<sup>117</sup> Exhibit 22635-X0005, PDF page 26.

<sup>118</sup> Exhibit 22635-X0005, PDF page 25.

<sup>119</sup> Exhibit 22635-X0164, paragraph 95.

<sup>120</sup> Decision 2941-D01-2015, paragraph 1098.

Without this compensation, the Commission considers that the RRO providers would not have a reasonable opportunity to recover prudent costs and expenses. Ignoring these costs for inclusion in the value of risk compensation would not be reasonable. [footnote removed]

160. The Commission further stated:

1098. Based on the evidence provided in this proceeding, the Commission finds that there is no fact-based way in which to decide which of the parties is correct, so there is no way to decide the level of risk aversion of the RRO providers. While Dr. Evans states that investors are risk averse, neither he nor any of the other parties have submitted any evidence confirming or denying this statement. In addition, no evidence has been submitted that allows the Commission to determine any of the costs incurred by the RRO providers due to the variability in the difference between revenues and costs, associated with the procurement of load, if in fact the RRO providers are risk averse.

1099. Accordingly, given the record of the proceeding, the Commission considers that for the purposes of this proceeding, it will use its judgment in determining whether or not the RRO providers will receive compensation for variability and, if they do, in determining a reasonable value for that compensation. The Commission will use its judgement to determine whether the RRO providers have a reasonable opportunity to recover prudent costs and expenses.

161. DERS has, therefore, failed to satisfy the Commission that its current CRC methodology is based on an assumption of risk neutrality.

### Pricing risk

162. DERS submitted that the Beblow method fails to price risk but instead attempts to reimburse for historical losses. GBL characterized the Beblow method of CRC as a “retroactive re-imbursement of losses.” GBL clarified that:

... under the Beblow method, as losses are incurred, DERS will be paid an amount intended to recover some, but not necessarily all, of the incurred losses with the recovery calculation being based on actual losses over a twelve-month period.<sup>121</sup>

163. The CCA also criticized the Beblow method because it viewed that the "effect the RCA approved by the Commission is not a prospective risk premium, but would be contingent upon incurrence of losses in the previous calendar year."<sup>122</sup>

164. The argument that the Beblow method results in a recovery of past losses and retroactive rates was expressly considered and rejected by the Commission in Decision 2941-D01-2015 and in the subsequent review and variance decision, Decision 20416-D01-2015.<sup>123</sup> Those concerns have, therefore, been determined by the Commission and DERS has failed to offer any evidence or argument that would warrant a departure from the Commission’s findings in those decisions concerning the prospective nature of the Beblow method of CRC.

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<sup>121</sup> Exhibit 22635-X0144, DERS-AUC-2018JUL27-003(b).

<sup>122</sup> Exhibit 22635-X0165, CCA argument, paragraph 8.

<sup>123</sup> Decision 20416-D01-2015: Review and Variance of Decision 2941-D01-2015: Regulated Rate Tariff and Energy Price Setting Plans – Generic Proceeding: Part B – Final Decision, Proceeding 20416 Applications A001, A002, September 3, 2015, paragraph 196.

### Commodity losses, increasing prices and increasing volatility

165. DERS argued that there is insufficient evidence that the Beblow method reacts to volatility and delivers compensation over time. DERS asserted that Mr. Beblow did not provide a forward-looking analysis or evidence pertaining to other possible pricing and volatility scenarios, but rather evaluated a single scenario, a “historical lookback” analysis<sup>124</sup> of July 2011 through September 2017, which DERS characterized as a period reflecting a “declining trend in both the size and volatility of losses.”<sup>125</sup> Because the Beblow method bases its CRC rate on the previous 12 months of losses, DERS argued the Beblow method would continually undercompensate DERS in periods of increasing price and volatility. DERS submitted that its market evidence supports that price and volatility will rise over the term of the EPSP. It also relied on the cumulative commodity losses incurred during its first six months of operating under the Beblow CRC method as evidence that in periods of increasing volatility, the Beblow method would undercompensate it for losses.<sup>126</sup>

166. The Commission is not persuaded by these arguments.

167. DERS stated that the Beblow method “bases its CRC rate on the previous twelve months of losses,”<sup>127</sup> and because of this, the Beblow method will continually undercompensate DERS in periods of increasing prices and volatility. While the variable component of the CRC rate under the Beblow method may be based on the commodity gains/losses experienced in the past 12 months, the results are expressed as a percentage, and this percentage is applied to the base energy charge for the prompt month. If the base energy charge in the prompt month has increased compared to the base energy charges experienced over the previous 12 months, then the resulting CRC rate for the prompt month will reflect the increasing prices. The base energy charge for the prompt month should also be reflective of any increases in volatility that are expected for the prompt month. If the actual increases in volatility experienced during the prompt month are more than those reflected in the base energy charge, and this results in unexpected commodity losses for DERS, (as experienced by DERS during its first six months of operating under the Beblow CRC method), these unexpected commodity losses would be captured in a subsequent RCA calculation, as was the case for DERS when its RCA for September-November 2018 was \$4.23/MWh.

168. The Commission further observes that the Beblow method was tested in the generic RRO proceeding leading to Decision 2941-D01-2015, where the Commission stated:

... The Commission finds that this methodology is reasonable for determining the CRC for both DERS and EEA, since both of these RRO providers manage their commodity risk through the procurement of forward market hedging products.<sup>128</sup>

169. In the same decision, the Commission also found that the weighted average of the commodity gains and losses used in the adaptive component of the Beblow method allows for changing market conditions to be reflected on a more timely basis.<sup>129</sup>

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<sup>124</sup> Exhibit 22635-X0128, paragraph 18.

<sup>125</sup> Exhibit 22635-X0164, paragraph 80.

<sup>126</sup> Exhibit 22635-X0128, paragraph 20.

<sup>127</sup> Exhibit 22635-X0164, paragraph 81.

<sup>128</sup> Decision 2941-D01-2015, paragraph 1214.

<sup>129</sup> Decision 2941-D01-2015, paragraph 1216.

170. Accordingly, DERS' argument that the Beblow method provides insufficient compensation in periods of increasing prices and increasing volatility is not persuasive.

171. While not determinative, the Commission also observes that that DERS' 2018-2020 EPSP includes a provision that allows the Commission to reopen the EPSP. That provision states, "DERS or another person directly harmed or prejudiced by the change of the EPSP may apply to the Commission for an order re-opening and modifying the EPSP to the extent required to address the change."<sup>130</sup>

### **The RCA's lag in collection time and failure to account for expected net site attrition**

172. DERS has failed to satisfy the Commission that the Beblow method provides insufficient compensation as a result of the RCA's lag in recovery time.

173. DERS argued that one of the main flaws with the Beblow CRC method is the delay in reimbursing DERS for losses. DERS relied on its evidence that a large single loss could put DERS in a cumulative loss position for nearly two years, while absorbing two large losses could leave DERS in a loss position for more than two years.<sup>131</sup> DERS argued that its evidence reflects that there are potential periods of cumulative losses ranging from 22 to 32 contiguous months and that, therefore, under the Beblow method, DERS is at risk of large cumulative losses over long periods of time.

174. The Commission has examined the underlying data<sup>132</sup> for the three scenarios presented by DERS in the table presented after paragraph 86 of its argument,<sup>133</sup> and notes that each of the three scenarios was prepared based on calculating the RCA on an annual basis. In Decision 21295-D01-2017, the Commission approved the use of the Beblow method of CRC for DERS' 2016-2018 EPSP, which includes calculating RCA on a quarterly basis. The Commission has also subsequently approved this same CRC methodology for DERS for its 2018-2020 EPSP. Therefore, because DERS' analysis does not reflect the use of a quarterly RCA, the Commission assigns no weight to the submissions of DERS that the main flaw of the Beblow method is its delay in reimbursing DERS for losses.

175. The Commission considers that DERS quarterly RCA acts to mitigate lag because the RCA fixed \$/MWh amount related to the energy sales is adjusted quarterly.

176. Another of DERS' concerns with the RCA under the Beblow method is that the net attrition due to a smaller year over year customer base implies less energy consumption in the following year.<sup>134</sup> DERS provided its historical attrition rates for 2011-2016 in support of its position;<sup>135</sup> and asserted that it is reasonable to expect that it will continue to experience net attrition on an annual basis. It alleged that this exposes it to what DERS described as the 'one-sided impact of the RCA.'<sup>136</sup> DERS asserted its analysis demonstrates that the RCA mechanism would result in under collection of past losses almost equivalent to the percentage of net attrition between the period the RCA is calculated and the period over which it is collected.

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<sup>130</sup> Exhibit 22635-X0002, page 2.

<sup>131</sup> Exhibit 22635-X0164, paragraphs 86-87.

<sup>132</sup> Exhibit 22635-X0081.

<sup>133</sup> Exhibit 22635-X0164.

<sup>134</sup> Exhibit 22635-X0005, PDF page 25.

<sup>135</sup> Exhibit 22635-X0005, PDF page 25.

<sup>136</sup> Exhibit 22635-X0164, paragraph 91.

Consequently, in DERS' submission the Beblow method is neither just nor reasonable and fails to provide DERS with fair or adequate financial compensation.

177. The Commission previously commented on the Beblow method's ability to compensate for risk, including attrition risk, as follows:

The Commission agrees with these findings that the risk methodology approved does not separately identify all risk elements and assign numbers to the elements. The Commission considers that the "Beblow Method" continues to provide sufficient coverage of commodity risk, even though it does not separately identify specific risks, including attrition risk, to be recovered in the CRC.<sup>137</sup>

This example provided by EEC does not support the conclusion that the "Beblow method" of CRC does not account for attrition, because it is based on the assumption that there will be a net commodity loss over a 12-month period, even when the variable component of the CRC is factored in. Under the "Beblow method" the possibility exists that there will be a net commodity gain over a 12-month period, after the variable component of the CRC is factored in. In this situation of a net commodity gain, in accordance with the "Beblow method," the fixed component of CRC would be zero, and EEC would keep the net commodity gain. If there is a net commodity gain and consequently no fixed risk component charged, then the situation described by EEC about attempting to recover losses over a period of decreasing sales volumes is not applicable.<sup>138</sup>

178. DERS has failed to provide sufficient evidence to establish that the Beblow method does not account for the risks related to DERS' RRO service in the test years, e.g., whether there is a change in the rate of net attrition expected in the test years that would support a conclusion that the Beblow method does not sufficiently account for the risks to be recovered in the CRC.

179. The Commission further observes that contrary to the argument advanced by DERS, GBL's evidence was that it did not expect large fluctuations in DERS customer base or attrition.<sup>139</sup>

### **Fluctuating CRC and rate volatility**

180. DERS asserted the Beblow method exposes customers to the risk of a CRC that fluctuates each month and therefore to rate volatility. The Commission acknowledges that the CRC fluctuates under the Beblow method; however, the CRC only represents a small portion of the monthly energy charge. For example, DERS' CRC for September 2018 was \$5.79/MWh,<sup>140</sup> however, the total energy charge for RRO residential customers was \$84.72/MWh. Thus, the

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<sup>137</sup> Decision 20448-D01-2017: ENMAX Energy Corporation, 2016-2018 Energy Price Setting Plan, Proceeding 20448, January 30, 2017, paragraph 523. The decision also quotes the generic RRO review and variance decision, Decision 20416, paragraphs 145-146. Paragraph 146 states in part, "Nevertheless, the record of the impugned proceeding shows that even though there is no specific element or line item in the Beblow method that identifies a value for variability or volatility risk, the Beblow method is designed to sufficiently cover commodity risks. The hearing panel chose a method that does not separately identify all risk elements and assign a number or methodology to each element."

<sup>138</sup> Decision 20448-D01-2017, paragraph 515.

<sup>139</sup> Exhibit 22635-X0001, PDF page 13.

<sup>140</sup> Exhibit 22635-X0176, paragraph 109.

CRC portion of the RRO monthly energy charge in September 2018 was less than seven per cent.

181. The Commission is of the view that the base energy charge is the primary driver of RRO energy rates and has the greatest effect on customers. Thus changes in the monthly base energy charge would amount to a greater risk of volatility for customers than a fluctuating CRC. Also, if the CRC amount remains below DERS' proposed \$7.97/MWh, customers derive greater benefit from paying a fluctuating CRC than the proposed fixed amount, notwithstanding a measure of rate volatility.

182. The Commission also notes that in its report, GBL stated that its analysis did not include "The Cap on RRO prices: Starting in June of 2017 the RRO rate will be capped at 6.8 cents a kWh."<sup>141</sup> With respect to the cap on energy rates, the Commission observes that if energy charges exceed this amount, the excess amount is not paid by individual customers. Thus, some portion of the base energy charge, CRC, or any other component of the rate is essentially capped, reducing customers' exposure to rate volatility.

### **CRC methodology to be used for the 2018-2020 EPSP**

183. For all of the above reasons, DERS has failed to satisfy the Commission that the Beblow method undercompensates DERS for risk, materially increases rate volatility for customers and must be replaced. Accordingly, and in the absence of any other acceptable alternative, the Commission directs DERS in the compliance filing to update its 2018-2020 EPSP to reflect the previously approved Beblow methodology for calculating the CRC, and to calculate the RCA on a quarterly basis.

## **6 Reasonable return**

184. For the reasonable return component of its 2018-2020 EPSP, DERS requested that the Commission include the after-tax reasonable return approved in its 2017-2018 default rate tariff (DRT) and regulated rate tariff (RRT) proceeding.<sup>142</sup> DERS requested an after-tax reasonable return of \$6.43/MWh, which was concurrently requested in its 2017-2018 DRT and RRT proceeding.<sup>143</sup> DERS indicated that it will use the actual income tax rates when calculating the before tax amount of the reasonable return to be included in the monthly energy charge.<sup>144</sup>

185. During the course of this proceeding, Decision 22004-D01-2018 was issued with respect to DERS' 2017-2018 DRT and RRT proceeding. In Decision 22004-D01-2018, no change was approved for DERS' after-tax reasonable return set previously in Decision 2941-D01-2015. Consequently, in its argument, DERS proposed that the after-tax return of \$2.83/MWh approved in Decision 2941-D01-2015 continue to be used in its 2018-2020 EPSP.<sup>145</sup> As a result of the Commission's findings in Decision 22004-D01-2018, the UCA submitted that DERS should only be permitted to recover an after-tax return of \$2.83/MWh.<sup>146</sup>

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<sup>141</sup> Exhibit 22635-X0001, PDF page 36.

<sup>142</sup> Proceeding 22004.

<sup>143</sup> Exhibit 22635-X0005, PDF pages 3 and 5.

<sup>144</sup> Exhibit 22635-X0005, PDF page 13.

<sup>145</sup> Exhibit 22635-X0164, paragraph 8.

<sup>146</sup> Exhibit 22635-X0166, paragraph 151.

## Commission findings

186. The Commission finds that the amount of \$2.83/MWh after-tax reasonable return should continue for DERS' 2018-2020 EPSP consistent with the Commission's findings in Decision 2941-D01-2015 and Decision 22004-D01-2018. Therefore, the Commission approves DERS' request to include an after-tax reasonable return of \$2.83/MWh. The Commission also approves DERS' request to use the actual income tax rates when calculating the before tax amount of the reasonable return to be included in the monthly energy charge. The Commission directs DERS, as part of the compliance filing, to incorporate the necessary wording changes required in its 2018-2020 EPSP to incorporate these reasonable return approvals.

## 7 Attestation letters

### 7.1 Monthly attestation letter

187. In Decision 21295-D01-2017, the Commission approved an attestation letter to be signed by an officer of DERS regarding the monthly procurement of energy under the EPSP. The letter requires confirmation from the officer that the officer has reviewed the RRO rates as well as affirmation that the rates have been calculated in accordance with the EPSP. In addition, the officer is required to confirm that the calculations are based on the regulated rate, the prices represent forward prices during the procurement period, and 100 per cent of the portfolio is supplied through procurement approved by the relevant Commission decision.<sup>147</sup>

188. When asked in an IR if it intended to file an attestation letter as part of its monthly energy rate filings during the term of the 2018-2020 EPSP, DERS replied that if deemed necessary by the Commission, DERS would be supportive of filing the attestation letter that was approved in Decision 21295-D01-2017. DERS added that it plans to have the signatory of the monthly attestation letter be either the commercial director, the vice-president, or the manager of government and regulatory affairs.<sup>148</sup>

## Commission findings

189. The continued filing of a monthly attestation letter is beneficial because it disseminates information about the monthly procurement under the EPSP to the Market Surveillance Administrator, interveners, the Commission and the public. The attestation letter provides information about the procurement sources for the month, including self-supply. It also provides assurance that the signatory has reviewed the monthly rates and requires the officer's affirmation that the RRO rates have been calculated in accordance with the 2018-2020 EPSP. This disclosure adds transparency to the monthly rate setting process undertaken by DERS.

190. The monthly attestation letter should continue to be signed by an officer. The additional level of internal review by an officer ensures that a sufficient review of the RRO rates and calculations has been undertaken by DERS. The Commission reiterates that the significance of the attestation of these officers on a monthly basis confirms the verification of the monthly filings, and is in the interests of both customers and DERS. The Commission directs DERS, as part of its monthly energy rate filings during the term of its 2018-2020 EPSP, to include a monthly attestation letter in the form set out in paragraph 30 of Decision 21295-D01-2017.

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<sup>147</sup> Decision 21295-D01-2017, paragraph 30.

<sup>148</sup> Exhibit 22635-X0038, DERS-AUC-2017NOV09-001.

## 7.2 Trader attestation letter

191. In Decision 21295-D01-2017,<sup>149</sup> the Commission required DERS to file a trader attestation letter as part of its monthly energy rate filings. The trader attestation letter approved by the Commission requires that the trader verify that reasonable efforts were made to procure the daily target volumes at prices at or below the daily target price. The trader must also attest to compliance with the trader's obligations under Schedule G of the EPSP, Appendix G.1 of the EPSP, the Code of Conduct for the EPSP and the Procurement Conduct Agreement. In addition, the trader must provide confirmation that the trader has not engaged in any form of trading activity in the Alberta electricity market on behalf of any person or entity other than DERS.

192. Mr. Beblow submitted that DERS should continue to include a trader attestation letter as part of its monthly energy rate filings under the term of its 2018-2020 EPSP. A key aspect of this letter is the requirement for the dedicated trader to attest, on a monthly basis, that the trader has kept RRO-related information strictly confidential. This is particularly important given that DERS also has an unregulated trading arm. Mr. Below commented that the requirement for the dedicated trader to attest to not engaging in any trading activity on behalf of any person except DERS, is an important safeguard against inappropriate conflicts of interest.<sup>150</sup>

193. DERS stated the submission of a trader attestation letter on a monthly basis was not necessary. DERS indicated that its traders are required to operate under the EPSP Code of Conduct,<sup>151</sup> and sign the Procurement Conduct Agreement<sup>152</sup> that DERS attached as an appendix<sup>153</sup> to the 2018-2020 EPSP. DERS noted that prior to the 2016-2018 EPSP, it operated successfully and without issue under a code of conduct and was not required to provide a monthly trader attestation letter.<sup>154</sup> DERS submitted the confirmations provided each month by one of its officers, as part of the monthly attestation letter, require the traders to affirm their obligations and duties on a monthly basis, which includes the obligation of confidentiality relating to the RRO information.<sup>154</sup> DERS stated that if the Commission, nonetheless, determines that a trader attestation letter continues to be necessary, then the Commission should be aware that DERS had proposed modifications to the letter that reflect the framework of the specific obligations, in Schedule G and Appendix G.1.<sup>155</sup>

194. In an IR, the UCA questioned DERS about whether it still viewed the monthly filing of a trader attestation letter during the term of the 2018-2020 EPSP as unnecessary.<sup>156</sup> In response, DERS acknowledged that the trader attestation letter provides comfort to the Commission, and has been deemed necessary by the Commission.<sup>157</sup> DERS also confirmed that it has been submitting the trader attestation letter since February 2018. However, DERS had concerns with the use of the term "RRO-related information" as an undefined term. Further, the trader must attest that information was not "advertently or inadvertently disclosed."<sup>158</sup> DERS proposed that

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<sup>149</sup> Confidential Decision 21295-D01-,2017, Attachment 5.

<sup>150</sup> Exhibit 22635-X0090, PDF page 41.

<sup>151</sup> Schedule G of the 2018-2020 EPSP.

<sup>152</sup> Appendix G.1 to the 2018-2020 EPSP.

<sup>153</sup> Exhibit 22635-X0128, paragraph 32.

<sup>154</sup> Exhibit 22635-X0128, paragraphs 34-35.

<sup>155</sup> Exhibit 22635-X0128, paragraph 36.

<sup>156</sup> Exhibit 22635-X0141, DERS-UCA-2018JUL27-008.

<sup>157</sup> Exhibit 22635-X0150, DERS-UCA-2018JUL27-008.

<sup>158</sup> Exhibit 22635-X0150, DERS-UCA-2018JUL27-008(c).

certain modifications be made to the currently approved trader attestation letter, for use during the term of the 2018-2020 EPSP.<sup>159</sup>

195. The modified trader attestation letter proposed by DERS and the trader attestation letter approved for use for the term of the 2016-2018 EPSP, are reproduced in the following table:

**Table 5. DERS' proposed trader attestation letter for the 2018-2020 EPSP,<sup>160</sup> and the Commission approved trader attestation letter for the term of the 2016-2018 EPSP**

2018-2020 EPSP	2016-2018 EPSP
<p>Please accept this letter as confirmation that I, _____, as an RRO Trader under DERS 2018-2020 Energy Price Setting Plan ("EPSP"), confirm that in procuring the RRO hedge volumes for the month of _____, 201_:</p> <p>a) I have applied my skill and expertise in executing transactions, and I made reasonable efforts to procure the Daily Target Volumes at prices at or below the respective Daily Target Price;</p> <p>b) I have complied with my obligations under Schedule "G" and Appendix "G.1" of DERS 2018-2020 EPSP, respectively, the Code of Conduct for the EPSP and the Procurement Conduct Agreement. I have exercised due care to maintain the strict confidentiality of the Daily Target Volumes and the Daily Target prices and all other materials and information related to Confidential Schedule "E" of DERS 2018-2020 EPSP. To the extent that I am aware of any advertent or inadvertent exchanges of information with unauthorized recipients, including, without limitation, individuals associated with DEML's [Direct Energy Marketing Limited's] unregulated trading business, I have disclosed such exchanges as required under Schedule "G" and Appendix "G.1".</p> <p>c) During the month, I did not engage in any form of trading activity in the Alberta electricity market on behalf of any person or entity except for DERS.</p> <p>Should you require additional information, please contact the undersigned at [insert contact information]</p>	<p>Please accept this letter as confirmation that I, _____, as the RRO Trader under the Direct Energy Regulated Services (DERS) 2016-2018 Energy Price Setting Plan (EPSP), confirm that in procuring the required regulated rate option (RRO) hedge volumes for the month of _____, 201_:</p> <p>a) I have applied my skill and expertise in executing transactions, and I made reasonable efforts to procure the Daily Target Volumes at prices at or below the respective Daily Target Price;</p> <p>b) I complied with my obligations under Schedule "G" and Appendix "G.1" of DERS 2016-2018 EPSP, respectively the Code of Conduct for the EPSP and the Procurement Conduct Agreement, and ensured that all RRO-related information was kept strictly confidential and was not disclosed, either advertently or inadvertently, to any unauthorized recipients, including, without limitation, individuals associated with DEML's unregulated trading business;</p> <p>c) During the month, I did not engage in any form of trading activity in the Alberta electricity market on behalf of any person or entity except for DERS.</p> <p>Should you require additional information, please contact the undersigned at [insert contact information]</p>

196. DERS stated that the term "RRO-related information" has not been defined, specifically, and may be broadly interpreted. In light of this potential broad interpretation, DERS submitted this term cannot be reasonably attested to, nor can it be of any value to the Commission. DERS further submitted that attesting to the protection of specific information in Confidential Schedule E of the EPSP provides better protection for regulated customers.<sup>161</sup>

197. With regard to the advertent or inadvertent disclosure of confidential information, DERS submitted:

<sup>159</sup> Exhibit 22635-X0128, paragraph 36 and Exhibit 22635-X0164, paragraph 50.

<sup>160</sup> Exhibit 22635-X0129.

<sup>161</sup> Exhibit 22635-X0150, DERS-UCA-2018JUL27-008.

Likewise, the current requirement that the RRO Trader must attest not to having shared information “inadvertently” is inappropriate. In the rare event that information is disclosed inadvertently or accidentally, the trader may not be aware of its disclosure. It is thereby difficult for a trader to attest to the fact that information was not disclosed inadvertently unless the inadvertent disclosure was in fact detected by the trader or the trader was made aware by another party. Further, there is an additional concern that the current wording of the prescribed trader attestation letter also implies that the RRO Trader must attest to the fact that RRO information was kept confidential and not disclosed, either advertently or inadvertently, by all employees of DERS. Again, the language can be interpreted in an overly broad manner and does not account for those circumstances where disclosure may have occurred by another employee, without the RRO Trader’s knowledge or awareness. If DERS becomes aware of any such disclosure, be it inadvertent or advertent, DERS will immediately take steps to correct and report the disclosure and take steps to prevent a reoccurrence.<sup>162</sup>

198. Further, the proposed trader attestation letter specifically references the obligations that are detailed in the Code of Conduct and the Procurement Conduct Agreement in the EPSP, and these requirements reflect the surrounding framework better and support the protection of specific, confidential information in Confidential Schedule E of the EPSP.<sup>163</sup>

199. The UCA did not object to DERS’ suggestion to replace the term “RRO-related information” with specific reference to the confidential information related to, or encapsulated in, Confidential Schedule E. However, it did not support the additional revisions recommended by DERS. The UCA disagreed with DERS that including a reference to inadvertent disclosures as part of the trader attestation letter is inappropriate.<sup>164</sup> The UCA submitted that the Commission should direct DERS to file an RRO trader attestation letter on a monthly basis in the form approved in Decision 21295-D01-2017, subject to revising the reference to “RRO-related information,” as contemplated by DERS.<sup>165</sup>

200. The UCA stated if the Commission agrees that revisions to the trader attestation letter are necessary, then the Commission should direct DERS to adopt similar language to that recently approved for ENMAX Energy Corporation (EEC) in Decision 23223-D01-2018.<sup>166</sup> The UCA specifically recommended the following wording consistent with Decision 23223-D01-2018:

I complied fully with my obligations under Schedule “G” and Appendix “G.1” of DERS’ EPSP and I ensured that all materials and information related to Confidential Schedule “E” of DERS’ EPSP, in my possession, were kept strictly confidential and used only for the purposes of the EPSP.<sup>167</sup>

201. The UCA argued that this alternative wording avoids the concern of over-breadth raised by DERS and ensures consistency between the wording of the trader attestation letters of DERS and EEC.<sup>168</sup>

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<sup>162</sup> Exhibit 22635-X0150, DERS-UCA-2018JUL27-008.

<sup>163</sup> Exhibit 22635-X0128, paragraph 36.

<sup>164</sup> Exhibit 22635-X0166, paragraphs 187-188.

<sup>165</sup> Exhibit 22635-1066, paragraph 193.

<sup>166</sup> Decision 23223-D01-2018: ENMAX Energy Corporation, 2016-2018 Energy Price Setting Plan Second Compliance Filing, Proceeding 23223, June 15, 2018.

<sup>167</sup> Exhibit 22635-X0166, paragraph 189.

<sup>168</sup> Exhibit 22635-X0166, paragraph 190.

202. DERS submitted that the alternative wording proposed by the UCA does not allow for the possibility of a breach of confidential information by the RRO traders. DERS indicated that while the RRO traders strive to ensure information is kept confidential, if a breach did occur, and was duly reported, the RRO trader would not be able to sign the UCA's proposed trader attestation letter, despite the RRO trader being compliant with both the Code of Conduct for the EPSP and the Procurement Conduct Agreement. DERS submitted that the purpose of the second paragraph of the trader attestation letter is to serve as a reminder to the traders of their ongoing obligations under the Code of Conduct for the EPSP and the Procurement Conduct Agreement.<sup>169</sup>

### Commission findings

203. The Commission continues to be of the view that a trader attestation letter provides accountability and transparency of DERS' RRO trader in the EPSP procurement process. It also provides a protective measure to mitigate the potential for conflicts of interest and provides a safeguard with respect to activities of the dedicated trader. For these reasons, the Commission will continue to require DERS to file a trader attestation letter every month during the term of the 2018-2020 EPSP.

204. Concerning the content of the trader attestation letter, the proposed clauses (a) and (c) are the same as those currently approved for the DERS 2016-2018 EPSP and no issue has been taken with their content. The Commission approves the proposed content of clauses (a) and (c) of the trader attestation letter, as filed.

205. Regarding clause (b) of the trader attestation letter for the 2018-2020 EPSP, in the first sentence, the Commission agrees with the UCA's suggestion that the word "fully" should be included after the word "complied." This would ensure greater consistency with the language approved in Decision 23223-D01-2018.

206. The Commission finds the proposed use of the words "due care" in the second sentence of clause (b) of the 2018-2020 EPSP to be problematic. This language is subjective and does not adequately reflect the positive obligation on the trader in a given month to ensure that all confidential information related to Confidential Schedule E was kept strictly confidential and was not disclosed.

207. Regarding the information over which confidentiality is to be maintained, the Commission agrees with DERS and the UCA that the term "all RRO-related information" in clause (b) of the 2016-2018 EPSP is ambiguous and should be replaced with "all materials and information related to Confidential Schedule 'E' of DERS' EPSP." This change reflects the responsibilities of the trader better in affirming compliance with the trader's obligations and with the confidential treatment of information that is required under the EPSP.

208. The third sentence of clause (b) as proposed by DERS reads as follows:

To the extent that I am aware of any advertent or inadvertent exchanges of information with unauthorized recipients, including, without limitation, individuals associated with DEML's unregulated trading business, I have disclosed such exchanges as required under Schedule "G" and Appendix "G.1."<sup>170</sup>

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<sup>169</sup> Exhibit 22635-X0176, paragraph 160.

<sup>170</sup> Exhibit 22635-X0129.

209. DERS argued that the language in the third sentence of clause (b) is required because the trader may not be aware of inadvertent disclosures and that the trader must attest that confidential information was not disclosed “inadvertently” or “advertently.”

210. The Commission considers that the third sentence of clause (b) is overly narrow. The Commission considers that the alternative wording proposed by the UCA, included in paragraph 200 above, should be used to reflect the obligations of the trader in protecting confidential information related to the procurement of energy for the term of the 2018-2020 EPSP. The Commission finds that the alternative language proposed by the UCA will be sufficient to cover the attestation of the trader with regard to the confidential treatment of information within the knowledge of the trader or that the trader becomes aware of, and also addresses the concerns expressed by DERS.

211. The UCA’s alternative wording is also consistent with the wording recently approved for inclusion in the trader attestation letter, as finalized in Decision 23223-D01-2018 for EEC.

212. In making the above finding, the Commission acknowledges that DERS objected to the use of the language approved in Decision 23223-D01-2018, on the basis that if a breach did occur, and was duly reported, the RRO trader would likely not be able to sign the trader attestation letter despite the RRO trader being compliant with both the code of conduct for the EPSP and the procurement conduct agreement. If such a situation arises, DERS should advise the Commission at the time of its monthly filing that the trader could not sign the attestation letter and provide the reasons for why it is not able to execute the attestation letter, even though the trader was in compliance with Schedule G and Appendix G.1. If the reasons are confidential in nature, DERS should submit them under a separate confidential filing, and the Commission will, in turn, determine whether the filing warrants confidential treatment under Section 28 of Rule 001.

213. Based on its findings and considerations in this section, the Commission directs DERS, as part of its monthly energy rate filings during the term of the 2018-2020 EPSP, to submit a trader attestation letter in the following form:

Please accept this letter as confirmation that I, \_\_\_\_\_, as an RRO Trader under DERS 2018-2020 Energy Price Setting Plan (“EPSP”), confirm that in procuring the RRO hedge volumes for the month of \_\_\_\_\_, 201\_:

- (b) I have applied my skill and expertise in executing transactions, and I made reasonable efforts to procure the Daily Target Volumes at prices at or below the respective Daily Target Price;
- (c) I have complied fully with my obligations under Schedule “G” and Appendix “G.1” of DERS’ 2018-2020 EPSP, respectively, the Code of Conduct for the EPSP and the Procurement Conduct Agreement. I ensured that all materials and information related to Confidential Schedule “E” of DERS’ EPSP, in my possession, were kept strictly confidential and used only for the purposes of the EPSP;
- (d) During the month, I did not engage in any form of trading activity in the Alberta electricity market on behalf of any person or entity except for DERS.

Should you require additional information, please contact the undersigned at [insert contact information]

Yours truly,

[signatory]

## 8 Other issues

### 8.1 Proposed revisions to public portions of Schedule A - Definitions

214. The Commission compared the 2018-2020 EPSP<sup>171</sup> to the approved 2016-2018 EPSP<sup>172</sup> and identified changes in Schedule A – Definitions. The following three items were included in the definitions of the 2018-2020 EPSP:

**Letter of Credit** or **LOC** is a guarantee of payment issued by a bank on behalf of a client that is used as “payment of last resort” should the client fail to fulfill a contractual commitment with a third party;<sup>173</sup>

**Parental Corporate Guarantee** is a guarantee of payment from a parent company for a subsidiary when the subsidiary enters into a contract with a counterparty;<sup>174</sup>

**Wholesale Settlement Detail** or **WSD** is the historical consumption information that is provided by ATCO Electric at a site level.<sup>175</sup>

### Commission findings

215. The Commission approves the inclusion of the definitions as set out above in Schedule A – Definitions, and as they are used throughout the EPSP and schedules. The Commission notes that the acronym “PCG,” for parental corporate guarantee, is also used in the EPSP, but is not included as part of the definition. For completeness, the Commission directs DERS, in the compliance filing, to include the acronym PCG as part of the definition of Parental Corporate Guarantee; i.e., the bold portion of the definition should read, “**Parental Corporate Guarantee or PCG.**”

216. Further, DERS filed three different versions of the EPSP and attached schedules on the record of the proceeding. The above definitions were not included in the original EPSP and schedules filed at Exhibit 22635-X0002 or the updated application EPSP and schedules at Exhibit 22635-X0016, but the definitions were later included in Exhibit 22635-X0045, in response to an IR. In response to the Commission’s findings and directions in this section, and elsewhere in the decision, the Commission directs DERS to file its revised EPSP and schedules in its compliance filing to this decision.

### 8.2 Other proposed revisions to confidential information in Confidential Schedule E

217. Paragraphs 217 to 222 are redacted.

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<sup>171</sup> As included in Exhibit 22635-X0045.

<sup>172</sup> The 2016-2018 approved EPSP is included as Appendix 5 to Decision 21295-D01-2017.

<sup>173</sup> Exhibit 22635-X0045, page 7.

<sup>174</sup> Exhibit 22635-X0045, page 8.

<sup>175</sup> Exhibit 22635-X0045, page 10.

**Table 6.** Redacted.

**Table 7.** Redacted.

**Table 8.** Redacted.

## **9 Compliance filing**

223. The Commission directs DERS to submit a compliance filing, to reflect certain changes that are required to the 2018-2020 EPSP, on or before January 31, 2019. As part of the compliance filing, the Commission directs DERS to submit a redacted version of its 2018-2020 EPSP, and a complete version of its monthly rate workbook that incorporate the revisions directed as part of the public version of this decision. The Commission also directs DERS to submit, on the confidential record, a complete unredacted version of its 2018-2020 EPSP that incorporates the directed revisions as part of this entire decision.

## **10 Confidentiality**

224. In its September 25, 2017 ruling<sup>176</sup> on DERS' confidentiality request for the current proceeding, Proceeding 22635, the Commission instructed parties who wished to receive copies of the confidential information in this proceeding to submit a confidentiality undertaking in the form included as Form RP5 in Rule 001. Under Section 7(c) of Form RP5, individuals who have a current confidentiality undertaking are required to file a statutory declaration indicating destruction of the confidential documents 30 days after a decision is issued by the Commission or the expiration of any review or appeal period.

225. As noted in the Commission's findings and directions in this decision, a compliance filing for DERS' 2018-2020 EPSP is required. The Commission considers that the compliance filing is required to address the remaining issues related to the 2018-2020 EPSP. Therefore, the Commission is exercising its discretion under Section 8(2) of the *Alberta Utilities Commission Act* to extend its September 25, 2017 confidentiality ruling to the upcoming compliance proceeding to allow individuals who have signed undertakings to retain the confidential documents filed with the Commission on a confidential basis in the current proceeding. Consistent with the current version of Rule 001 released after the confidentiality ruling in this proceeding was issued, the Commission will also allow parties who have filed an undertaking in the current proceeding to retain this decision until the completion of the compliance filing proceeding. This decision, along with any confidential materials retained subject to the September 25, 2017 confidentiality ruling, will now be required to be destroyed within 30 days of the expiry of any review or appeal period after a decision is issued by the Commission on the compliance filing or, if applicable, within 30 days of any disposition of a review application or 30 days of a final decision disposing of an appeal.

226. In summary, any individual to the current proceeding who received copies of the confidential information and who will be participating in the compliance filing to this decision, is, therefore, permitted to retain those materials for use in the compliance filing proceeding, which will be established to test DERS' 2018-2020 EPSP compliance with the Commission's directions. The Commission also confirms that individuals who signed a confidentiality

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<sup>176</sup> Exhibit 22635-X0019.

undertaking with respect to documents subject to the September 25, 2017 confidentiality ruling, do not need to sign a new undertaking for the purposes of retaining those documents or this decision, until a new decision is issued in the compliance filing proceeding. However, those individuals are required to file statutory declarations on the new proceeding that will be established to test DERS' 2018-2020 EPSP compliance filing, in accordance with the statutory declaration included in Rule 001, the September 25, 2017 ruling and the extension of confidential treatment, as set out in this decision.

227. Any party to the current proceeding who received copies of the confidential information but will not be participating in the proceeding to test DERS' 2018-2020 compliance filing to this decision, must fulfill his or her obligations included in the confidentiality undertaking filed on the record of the current proceeding, by completing the Rule 001 statutory declaration in Form RP5 and filing it on the record of Proceeding 22635.

228. Any individual who wishes to obtain confidential information in the compliance filing proceeding who has not previously executed and filed an undertaking with the Commission, pursuant to the Commission's September 25, 2017 confidentiality ruling, may file an undertaking in the compliance filing proceeding. The undertaking filed should reference the September 25, 2017 confidentiality ruling and this decision as the authorities that grant confidential treatment for relevant confidential information related to Proceeding 22635 and the subsequent information related to the Commission's September 25, 2017 ruling that will be filed in the compliance filing proceeding.

## 11 Order

229. It is hereby ordered that:

- (1) Direct Energy Regulated Services will submit a compliance filing to reflect the Commission's findings and directions, on or before January 31, 2019.

Dated on December 21, 2018.

### **Alberta Utilities Commission**

*(original signed by)*

Henry van Egteren  
Panel Chair

*(original signed by)*

Tracee Collins  
Commission Member

*(original signed by)*

Carolyn Hutniak  
Commission Member



## Appendix 1 – Proceeding participants

Name of organization (abbreviation) Company name of counsel or representative
Direct Energy Regulated Services (DERS) Lawson Lundell, Barristers & Solicitors
Consumers' Coalition of Alberta (CCA)
Office of the Utilities Consumer Advocate (UCA) Reynolds, Mirth, Richards & Farmer LLP

<p>Alberta Utilities Commission</p> <p>Commission panel</p> <p>H. van Egteren, Panel Chair</p> <p>T. Collins, Commission Member</p> <p>C. Hutniak, Commission Member</p> <p>Commission staff</p> <p>A. Sabo (Commission counsel)</p> <p>D. Reese (Commission counsel)</p> <p>C. Burt</p> <p>D. Mitchell</p> <p>G. MacIntyre</p>
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## Appendix 2 – Summary of Commission directions

This section is provided for the convenience of readers. In the event of any difference between the directions in this section and those in the main body of the decision, the wording in the main body of the decision shall prevail.

1. The Commission notes that the EPSP document does not contain an expiry date. The Commission directs DERS, as part of the compliance filing, to include wording indicating the expiry date of April 30, 2020, in the body of the EPSP document, preferably somewhere in the early pages of the EPSP, and in the definition section of the EPSP included in Schedule A to the EPSP. .... Paragraph 26
2. The Commission considers that DERS’ proposal to amend Section A (3) of Schedule C does not accord with the largely mechanical nature of the load forecasting methodology employed in the proposed EPSP and the approved 2016-2018 EPSP. The proposed amendment is based on DERS’ judgement that the average monthly net growth and attrition factors for rate classes E3 and E4 should be zero over the term of the EPSP, rather than based on the actual experience of the net growth or attrition over the previous two years. The Commission finds that DERS did not adequately support or explain why the load forecasting methodology for these two rate classes should be different from the methodology approved in the 2016-2018 EPSP, or why it should be different from the methodology employed for all the other rate classes. In the absence of further evidence on this issue and given the mechanical nature of the plan, the Commission denies the proposed revision to Section A (3) of Schedule C to the EPSP. The Commission directs DERS, in the compliance filing, to use the same wording for SFRC that was approved in the 2016-2018 EPSP. .... Paragraph 34
3. It would be beneficial to the Commission that the information described above be filed by DERS in any filing for acknowledgement. The information listed in the previous paragraph from EEA’s 2018-2021 EPSP will allow for disclosure of relevant information regarding changes in load forecasting, and will assist the Commission in reviewing the changes filed for acknowledgement. Therefore, the Commission directs DERS, in the compliance filing, to include the wording quoted above from Section C of Schedule C of EEA’s 2018-2021 EPSP, as part of Section D of Schedule C to DERS’ 2018-2020 EPSP, replacing EEA with DERS in the first sentence. .... Paragraph 37
4. The Commission finds that the amount of \$2.83/MWh after-tax reasonable return should continue for DERS’ 2018-2020 EPSP consistent with the Commission’s findings in Decision 2941-D01-2015 and Decision 22004-D01-2018. Therefore, the Commission approves DERS’ request to include an after-tax reasonable return of \$2.83/MWh. The Commission also approves DERS’ request to use the actual income tax rates when calculating the before tax amount of the reasonable return to be included in the monthly energy charge. The Commission directs DERS, as part of the compliance filing, to incorporate the necessary wording changes required in its 2018-2020 EPSP to incorporate these reasonable return approvals. .... Paragraph 183
5. The Commission finds that the amount of \$2.83/MWh after-tax reasonable return should continue for DERS’ 2018-2020 EPSP consistent with the Commission’s findings in Decision 2941-D01-2015 and Decision 22004-D01-2018. Therefore, the Commission approves DERS’ request to include an after-tax reasonable return of \$2.83/MWh.

The Commission also approves DERS' request to use the actual income tax rates when calculating the before tax amount of the reasonable return to be included in the monthly energy charge. The Commission directs DERS, as part of the compliance filing, to incorporate the necessary wording changes required in its 2018-2020 EPSP to incorporate these reasonable return approvals. .... Paragraph 186

6. The monthly attestation letter should continue to be signed by an officer. The additional level of internal review by an officer ensures that a sufficient review of the RRO rates and calculations has been undertaken by DERS. The Commission reiterates that the significance of the attestation of these officers on a monthly basis confirms the verification of the monthly filings, and is in the interests of both customers and DERS. The Commission directs DERS, as part of its monthly energy rate filings during the term of its 2018-2020 EPSP, to include a monthly attestation letter in the form set out in paragraph 30 of Decision 21295-D01-2017. .... Paragraph 190
7. Based on its findings and considerations in this section, the Commission directs DERS, as part of its monthly energy rate filings during the term of the 2018-2020 EPSP, to submit a trader attestation letter in the following form:

Please accept this letter as confirmation that I, \_\_\_\_\_, as an RRO Trader under DERS 2018-2020 Energy Price Setting Plan ("EPSP"), confirm that in procuring the RRO hedge volumes for the month of \_\_\_\_\_, 201\_:

- (a) I have applied my skill and expertise in executing transactions, and I made reasonable efforts to procure the Daily Target Volumes at prices at or below the respective Daily Target Price;
- (b) I have complied fully with my obligations under Schedule "G" and Appendix "G.1" of DERS' 2018-2020 EPSP, respectively, the Code of Conduct for the EPSP and the Procurement Conduct Agreement. I ensured that all materials and information related to Confidential Schedule "E" of DERS' EPSP, in my possession, were kept strictly confidential and used only for the purposes of the EPSP;
- (c) During the month, I did not engage in any form of trading activity in the Alberta electricity market on behalf of any person or entity except for DERS.

Should you require additional information, please contact the undersigned at [insert contact information]

Yours truly,

[signatory] ..... Paragraph 213

8. The Commission approves the inclusion of the definitions as set out above in Schedule A – Definitions, and as they are used throughout the EPSP and schedules. The Commission notes that the acronym "PCG," for parental corporate guarantee, is also used in the EPSP, but is not included as part of the definition. For completeness, the Commission directs DERS, in the compliance filing, to include the acronym PCG as part of the definition of Parental Corporate Guarantee; i.e., the bold portion of the definition should read, **"Parental Corporate Guarantee or PCG."** ..... Paragraph 215
9. Further, DERS filed three different versions of the EPSP and attached schedules on the record of the proceeding. The above definitions were not included in the original EPSP and schedules filed at Exhibit 22635-X0002 or the updated application EPSP and schedules at Exhibit 22635-X0016, but the definitions were later included in Exhibit 22635-X0045, in response to an IR. In response to the Commission's findings and directions in this section, and elsewhere in the decision, the Commission directs DERS to

file its revised EPSP and schedules in its compliance filing to this decision. ....  
..... Paragraph 216

10. The Commission directs DERS to submit a compliance filing, to reflect certain changes that are required to the 2018-2020 EPSP, on or before January 31, 2019. As part of the compliance filing, the Commission directs DERS to submit a redacted version of its 2018-2020 EPSP, and a complete version of its monthly rate workbook that incorporate the revisions directed as part of the public version of this decision. The Commission also directs DERS to submit, on the confidential record, a complete unredacted version of its 2018-2020 EPSP that incorporates the directed revisions as part of this entire decision. ...  
..... Paragraph 223