Evergreen Gas Co-op Ltd.

Franchise Agreement with the Town of Drayton Valley

May 2, 2019
Alberta Utilities Commission
Decision 24257-D01-2019
Evergreen Gas Co-op Ltd.
Franchise Agreement with the Town of Drayton Valley
Proceeding 24257

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1 Introduction

1. On January 21, 2019, Evergreen Gas Co-op Ltd. (the Co-op) applied to the Alberta Utilities Commission for approval of a natural gas franchise agreement with the Town of Drayton Valley (the Town) pursuant to Section 45 of the Municipal Government Act. The application was filed based on the requirements of Rule 029,\(^1\) and included:

(a) a copy of the franchise agreement as well as a blackline of the agreement indicating the revisions made to the standard natural gas franchise agreement template approved in Decision 20069-D01-2015;\(^2\)

(b) Bylaw No. 2018/05/F, which was given first reading on May 16, 2018;

(c) a copy of the notice of the proposed agreement; and

(d) the natural gas franchise application form.

2. Notice of the proposed franchise agreement was advertised on December 11, 2018, in the Drayton Valley Western Review. No objections or concerns related to the proposed franchise agreement were received.\(^3\) On February 7, 2019, ATCO Gas North registered as an observer in this proceeding.

3. The process established by the Commission for this proceeding included information requests (IRs) from the Commission to each of the Town and the Co-op, and responses from these parties. The Commission considers the record for this proceeding to have closed on March 18, 2019, when the Town submitted supplementary evidence in support of its IR responses.

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

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\(^1\) Rule 029: Applications for Municipal Franchise Agreements and Associated Franchise Fee Rate Riders.


\(^3\) Exhibit 24257-X0003.
2 Proposed franchise agreement

5. In the proposed franchise agreement, the Town grants the Co-op the exclusive right to construct, operate and maintain the natural gas distribution system within an identified area of the municipality (described below) and to provide natural gas distribution service in that area to any customer that agrees to execute a contract with the Co-op for the service and to pay the associated costs.

6. The proposed franchise agreement has a term of 10 years effective the date the franchise agreement has received the Commission’s approval and the Town’s Bylaw No. 2018/05/F has received third reading. The proposed franchise agreement includes changes to the standard natural gas franchise agreement template approved in Decision 20069-D01-2015; among them, changes reflecting that:

   (a) The Co-op is a natural gas cooperative, as opposed to a private gas utility.

   (b) The proposed franchise agreement arises from an annexation by the Town of certain lands previously in Brazeau County\(^4\) (the Annexation Area\(^5\)). As a result, the Town will receive natural gas from both the Co-op and ATCO Gas and Pipelines Ltd. (ATCO Gas) upon approval of the franchise agreement. Historically, the Co-op has provided gas services to customers within Brazeau County and will continue to do so in the Annexation Area\(^6\). ATCO Gas will continue to provide natural gas in what was defined as the Municipal Area prior to the annexation, pursuant to the existing natural gas franchise agreement between ATCO Gas and the Town\(^7\).

   (c) There will be no franchise fee during the initial term of the agreement. In subsequent renewals of the agreement, the Town intends to require a franchise fee, which would apply only to new customers of the Co-op\(^8\).

3 Jurisdiction and nature of the Commission’s review

7. The Commission’s authority to approve franchise agreements derives from Section 45 of the Municipal Government Act, which in its relevant parts, states:

   Granting rights to provide utility service

   **45(1)** A council may, by agreement, grant a right, exclusive or otherwise, to a person to provide a utility service in all or part of the municipality, for not more than 20 years.

   **(2)** The agreement may grant a right, exclusive or otherwise, to use the municipality’s property, including property under the direction, control and management of the municipality, for the construction, operation and extension of a public utility in the municipality for not more than 20 years.

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\(^4\) The annexation was approved in Annexation Order MGB 016/12, issued by the Municipal Government Board on March 21, 2012 (Exhibit 24257-X0019).

\(^5\) Exhibit 24257-X0025.

\(^6\) Exhibit 24257-X0016, Drayton-AUC-2019FEB04-001, PDF pages 3-4.

\(^7\) Exhibit 24257-X0017.

\(^8\) Exhibit 24257-X0001, Letter re Application, PDF page 2.
(3) Before the agreement is made, amended or renewed, the agreement, amendment or renewal must
   
   (a) be advertised, and
   
   (b) be approved by the Alberta Utilities Commission.

8. While the Municipal Government Act requires Commission approval of a franchise agreement, it does not specify the basis for granting it. Some guidance may, however, be drawn from Section 49(2) the Gas Utilities Act, which states:

   49(1) No privilege or franchise granted to any owner of a gas utility by any municipality within Alberta is valid until approved by the Commission.

   (2) Approval shall be given when, after hearing the parties interested or with the consent of the parties, the Commission determines that the privilege or franchise is necessary and proper for the public convenience and properly conserves the public interests.

9. Section 30 of the Gas Distribution Act likewise provides some guidance. Under that section, the Commission has the authority to hear an application from a consumer receiving gas service from a rural gas co-operative who has a grievance concerning terms of service, service charges, rates or tolls; and vary, adjust or disallow the whole or any part of such term, charge, rate or toll if satisfied that it does not conform to the utility rate structure, has been improperly imposed, or is discriminatory. These determinations are made with a view to the public interest.

10. Consistent with the foregoing, the Commission and its predecessor (Alberta Energy Utilities Board) have stated that the purpose of reviewing franchise agreements is to determine whether “the privilege or franchise is necessary and proper for the public convenience and properly conserves the public interests.”

11. The Commission and its predecessor have also consistently acknowledged that franchise agreements are typically the result of negotiations between a municipality and a utility or co-operative, and will likely reflect a number of compromises concerning the interests and positions of both parties. Such agreements are therefore accorded a high degree of deference. However, this deference must be tempered by the Commission’s obligation to ensure that franchise agreements are in the public interest.

12. The Commission’s review of a proposed franchise agreement is accordingly kept at a relatively high level, and is focused primarily on those provisions that may cause a serious concern with respect to the public interest. One of the Commission’s key concerns in any franchise agreement is with respect to the franchise fee.

13. The Commission finds that Clause 5(a)(ii) in the proposed franchise agreement relating to franchise fees is discriminatory and therefore not in the public interest. On that basis, the Commission declines to approve the franchise agreement as filed. The subject provisions of the

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proposed franchise agreement and the Commission’s reasons in support of its findings are detailed in the following section.

3.1 Municipal franchise fee

14. The proposed franchise agreement states that no franchise fee shall be payable during the initial 10-year term of the agreement. Thereafter, franchise fees are payable by new customers. Existing customers remain exempt from the requirement to pay such fees. The relevant provisions in the proposed franchise agreement are as follows:

5. FRANCHISE FEE

(a) Franchise Fee

The Co-op and the Municipality agree that:

i. no franchise fee shall be payable during the initial Term of 10 years;

ii. from and after the expiration of the initial Term of 10 years, the franchise fee calculated in accordance with the provisions of this Agreement shall be payable by any new Consumers commencing services with the Co-op from and after the expiration of the initial Term of 10 years, and for clarity shall include:

(A) any Consumer seeking connection and service to a new development within the Franchise Area not previously serviced by the Co-op; and

(B) any new Consumer seeking the continuation of service at an existing service location serviced by the Co-op within the Franchise Area, upon the transfer or sale of the lands containing the existing service location to the new Consumer.

Notwithstanding the foregoing, in the event of an assignment of this Agreement to a third party assignee as contemplated within paragraph 18 of the Agreement, in consideration of the exclusive grant of franchise, the ability to use Municipal rights-of-way, and the mutual covenants herein, the third party assignee agrees to pay to the Municipality a franchise fee in respect of all Consumers.

(b) Calculation of Franchise Fee

The parties agree that s.360(4) of the MGA [Municipal Government Act] does not apply to the calculation of the franchise fee in this Agreement. For each calendar year the franchise fee will be calculated as a percentage of the Co-op’s actual total revenue derived from the Natural Gas Distribution Service, including without limitation the Base Cost and Distribution Cost but excluding the cost of gas in that year within the Municipal Area.

For the first calendar year or portion thereof of the Term of this Agreement, where and if applicable the franchise fee percentage will be twenty-two (22.00) percent. The maximum annual franchise fee payable by any Consumer on any point of delivery within the Municipal Area will be Ten Thousand Dollars ($10,000.00).

By no later than September 1 of each year, the Co-op will: (i) advise the Municipality in writing of the total revenues that were derived from the Natural Gas Distribution Service within the Municipal Area for the prior calendar year, and (ii) with the Municipality’s assistance, provide in writing an estimate of total revenues to be derived from the Natural
Gas Distribution Service within the Municipal Area for the next calendar year. [emphasis added]¹²

15. The proposed franchise agreement does not include a definition for “new Consumers” beyond the description in Clause 5(a)(ii) above.

16. In IR responses, the Co-op acknowledged that no customer of the Co-op within the franchise area will be required to pay any franchise fee during the initial 10-year term of the franchise agreement. However, following the expiration of the initial 10-year term, a different franchise fee will apply to new customers than will apply to existing customers (as defined). More specifically, “pursuant to Clause 5(a)(ii), following the expiration of the initial 10-year term, new customers of the Co-op within the franchise area will be required to pay a franchise fee, which may be set by the Town pursuant to Clause 5(d), but that is set at 22% as a default pursuant to Clause 5(b).”¹³

17. The Co-op explained the intent of and rationale for Clause 5(a) and provided the definition of “new consumers” as follows:

(a) The intent of Clause 5(a) is to impose a franchise fee after the expiration of the initial 10-year term on new consumers within the franchise area and to allow existing customers to continue to be exempt from paying a franchise fee under the Franchise Agreement.

(b) While Evergreen acknowledges that a different franchise fee will apply to new consumers than will apply to existing consumers, Evergreen submits that these differing franchise fee rates are justified in the circumstances. The difference in franchise fees after the initial 10-year term is justified because:

i. The negotiated decision agreed to by the Town and Evergreen (not to impose a franchise fee on existing customers at all or on new customers for the initial term of 10 years) was made in the context of the annexation of the franchise area from Brazeau County by the Town.

Annexations are typically approved on the basis that the annexation should not adversely affect individuals already living within the annexed area. Annexation orders typically include provisions whereby ratepayers within the annexed area will not bear additional financial burdens as a result of the annexation.

For example, the annexation order relating to the franchise area lands requires that lands within the annexed area will be taxed at the lower of the Town’s or Brazeau County. So, ratepayers within the annexed area are typically entitled to be taxed at a preferential rate in comparison to ratepayers outside the annexed area but within the annexing municipality.

The annexation order also contemplates that any new parcels of land that are created after annexation will not benefit from the same tax protections, and they will be taxed in the same fashion as any other property within the Town. Therefore, parcels of land that were created (voluntarily) after the annexation do not similarly benefit from the tax-advantaged status that applies to parcels...

¹² Exhibit 24257-X0002, Final Franchise Agreement.
¹³ Exhibit 24257-X0015, EVERGREEN-AUC-2019FEB05-003, PDF pages 6-7.
of land that are effectively pulled (involuntarily) into a municipality through an annexation.

The franchise fees proposed under the Franchise Agreement are similar to the provisions in the annexation order relating to tax relief for affected parcels in that existing customers within the franchise area do not experience a sudden increase in their utility rates through the imposition of a franchise fee, while new customers do not similarly benefit from an exclusion from the franchise fee.

ii. The Town and Evergreen conducted extensive negotiations regarding the franchise fee that would apply under the Franchise Agreement and jointly produced a Memorandum of Agreement that addressed that specific issue. The Memorandum of Agreement specifically stated that:

1. Evergreen would continue to provide natural gas utility services to the franchise area for a period of 50 years following the annexation;
2. No franchise fee would apply in respect to “Existing Customers”;
3. A franchise fee will apply to “New Customers”.

The Franchise Agreement is largely a reflection of the agreement reached between Evergreen and the Town through the Memorandum of Agreement.

iii. While the Franchise Agreement will result in separate franchise fees applying between existing and new and existing customers within the franchise area, it is also important to consider that any arrangement of franchise fees will inevitably result in different franchise fees between:
a) customers receiving services from the Co-op in the surrounding County and within the franchise area within the Town; or
b) new and existing customers within the Franchise Area; or c) customers within the Town receiving services from Evergreen and those receiving services from ATCO.

The terms “New Customers” and “Existing Customers” were defined in the Memorandum of Agreement as follows:

i. “New Customers” means a customer that receives services from Evergreen from a hook-up made after the effective date of the annexation; and

ii. “Existing Customers” means a customer who receives services from Evergreen from a hook-up that exists as of the date of the annexation.

As the differences in the franchise fees between new and existing customers is premised on the fact that existing customers were affected by the annexation whereas new customers are not, the definitions of those terms should be interpreted based on the pre-annexation versus post-annexation distinction.14

18. There is some inconsistency or ambiguity between the proposed franchise agreement and the IR responses in terms of the definition each provides for the terms new and existing customers (consumers). Nevertheless, the Co-op acknowledges and it is clear that the proposed

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14 Exhibit 24257-X0015, EVERGREEN-AUC-2019FEB05-001(b), PDF pages 1-3.
franchise agreement is intended to and will differentiate between these two customer groups after the initial 10-year term, relative to payment of the franchise fee.

19. The Commission has considered what constitutes discrimination in a utility context and has consistently stated that in assessing whether any service charge, rate or toll is discriminatory, the Commission must assess the presence or absence of any rationale or logic underlying the charges imposed. Effectively, the Commission must determine whether a reasonable distinction exists between customers to support their differential treatment.

20. In Decision 2012-363,15 the Commission’s predecessor recognized that discrimination in utility regulation can arise in two circumstances:
   - First, when a utility fails to treat all users of a public utility equally where no reasonable distinction can be found between those favoured and those not favoured.
   - Second when a utility treats all its users equally where differences between users would justify different treatment.

21. The fundamental issue is whether the differential charges between customers are supported by sufficient rationale or logic and fact-based evidence justifying the distinction.16

22. As noted, the Co-op has confirmed that new and existing customers will be treated differently in terms of the requirement to pay a franchise fee after the expiration of the initial 10-year term of the proposed franchise agreement. In summary, the Co-op advanced three primary arguments for why, in its view, the differing franchise fee rates are justified.

23. The Co-op emphasized that Clause 5(a) was the result of extensive negotiations between the Town and the Co-op. The fact that Clause 5(a) was negotiated does not obviate the Commission’s responsibility to ensure that the terms of the proposed franchise agreement are in the public interest; nor does it, in itself, offer a reasonable rationale or basis for differential treatment between these two customer groups.

24. The Co-op argued that the differential treatment was warranted in the context of an annexation where the intention is to ensure that ratepayers within the annexed area do not incur additional financial burden and rate shock as a consequence of the annexation, and further suggested that, in this respect, Clause 5(a) is analogous to the provisions in the annexation order relating to tax relief.

25. While the expressed intention explains why no franchise fee is payable within the initial 10-year term of the proposed franchise agreement, it does not offer a reasonable rationale or fact-based justification for the differential treatment of these two customer groups after the expiry of its initial 10-year term. Further, the Co-op has failed to persuade the Commission that the point

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16 Decision 20744-D01-2016: New Sarepta Water and Sewer Complaint, Proceeding 20744, February 24, 2016, paragraphs 30, 32-33; Decision 2012-363, paragraphs 34-36; Public Utilities Board (PUB) Decision E94014: The Town of Bruderheim, Complaint by Mr. J.H. Lambert alleging discriminatory water and sewer billings by the Town of Bruderheim, March 28, 1994, page 16, where the PUB noted that the definition should be revised to fit the context of then Section 291 of the Municipal Government Act under which the complaint against the public utility was brought, so as to read: “… rates are discriminatory when they fail to treat all users of a public utility equally where no reasonable distinction can be found between those favoured and those not favoured.”
in time at which a customer takes service from a natural gas supplier, on its own, affords sufficient justification for the differential imposition of the franchise fee.

26. As its final argument, the Co-op asserted that while the franchise agreement will result in separate franchise fees applying between the Co-op’s existing and new customers within the franchise area, the Commission should consider that there will also be different franchise fees between Co-op customers receiving services in the surrounding county and within the franchise area and also between customers within the Town receiving services from the Co-op and those receiving services from ATCO.

27. None of these other arrangements is before the Commission in this proceeding, and if a complaint were to arise relating to any of these other arrangements, the Commission would consider it at that time and in the context of that proceeding. This proceeding seeks approval of the proposed franchise agreement and, accordingly, it is only the terms of that agreement with which the Commission is concerned.

28. For all of the above reasons, the Co-op has failed to satisfy the Commission that a reasonable distinction exists between new and existing customer groups supporting their differential treatment concerning the payment of franchise fees after the expiration of the initial 10-year term of the proposed franchise agreement. On that basis, the Commission finds that Clause 5(a)(ii) in the franchise agreement will allow for the imposition of discriminatory rates and is, therefore, not in the public interest. Consequently, the Commission cannot approve the franchise agreement as filed.

4 Order

29. It is hereby ordered that:

   (1) Evergreen Gas Co-op Ltd.’s application for approval of the proposed natural gas franchise agreement with the Town of Drayton Valley is denied.

Dated on May 2, 2019.

Alberta Utilities Commission

(Original signed by)

Carolyn Hutniak
Commission Member
### Appendix 1 – Proceeding participants

<table>
<thead>
<tr>
<th>Name of organization (abbreviation)</th>
<th>Company name of counsel or representative</th>
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<tbody>
<tr>
<td>Town of Drayton Valley (the Town)</td>
<td>Brownlee LLP</td>
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<tr>
<td>Evergreen Gas Co-op Ltd. (the Co-op)</td>
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Alberta Utilities Commission

Commission panel
- C. Hutniak, Commission Member

Commission staff
- E. Galan (Commission counsel)
- O. Saenz
- C. Burt