



# Memorandum

November 30, 2009

**TO: Willie Grieve, Chair, Alberta Utilities Commission**

**FROM: Darcy Mazurkewich, Manager Audit and Compliance**

## **REGULATORY AUDIT OF ATCO ELECTRIC LTD.**

1. Please find attached the audit report resulting from the recently completed Regulatory Audit of ATCO Electric Ltd. as well as management's response to the audit report.
2. The Audit Group determined that ATCO Electric Ltd. has demonstrated in all material respects for the year ended December 31, 2008 for both its Operating, Maintenance and General expenditures activities, and its Capital Management activities: that it had effective controls, policies and processes in place; that it complied with the applicable regulatory requirements for these areas; and that the relevant information provided in its 2008 Rule 005 filing with the Commission was presented fairly.
3. As noted in the report, ATCO Electric Ltd. management and staff provided us with their full cooperation throughout the audit.

A handwritten signature in blue ink, appearing to read 'D. Mazurkewich', is positioned above the typed name.

Darcy Mazurkewich  
Manager, Audit and Compliance  
Rates Division

**CC:** Sett Policicchio, President, ATCO Electric Ltd.  
Bob Heggie, Chief Executive, Alberta Utilities Commission  
Mike Hagan, Executive Director, Rates Division, Alberta Utilities Commission



November 6, 2009

Audit and Compliance Group – Utilities Branch  
Alberta Utilities Commission  
425 – 1 Street SW  
Calgary, AB T2P 3L8

Dear Mr. Mazurkewich:

**RE: ATCO Electric Regulatory Audit Report**

ATCO Electric would like to thank you for the opportunity to discuss your audit findings and observations during the closing meeting of the regulatory audit and for this opportunity to comment on the draft regulatory audit report. It is our understanding that this letter will be attached to the final version of the audit report.

ATCO Electric has reviewed the draft regulatory audit report and agrees with the information contained in the report. ATCO Electric is very pleased with the findings and overall conclusion of the audit. ATCO Electric believes that this is a direct result of our ongoing commitment to fully comply with all regulatory decisions and directives in a timely manner and to ensure effective systems of financial and operational controls are in place throughout the organization.

ATCO Electric would like to thank you for the recognition given to our management and staff and for accommodating our internal schedules and deadlines. ATCO Electric would also like to commend the audit team for its professionalism and conduct throughout the audit assignment.

Yours truly,

A handwritten signature in black ink, appearing to read 'S. F. (Sett) Policicchio'. The signature is written in a cursive style.

S. F. (Sett) Policicchio  
President



# AUC

Alberta Utilities Commission

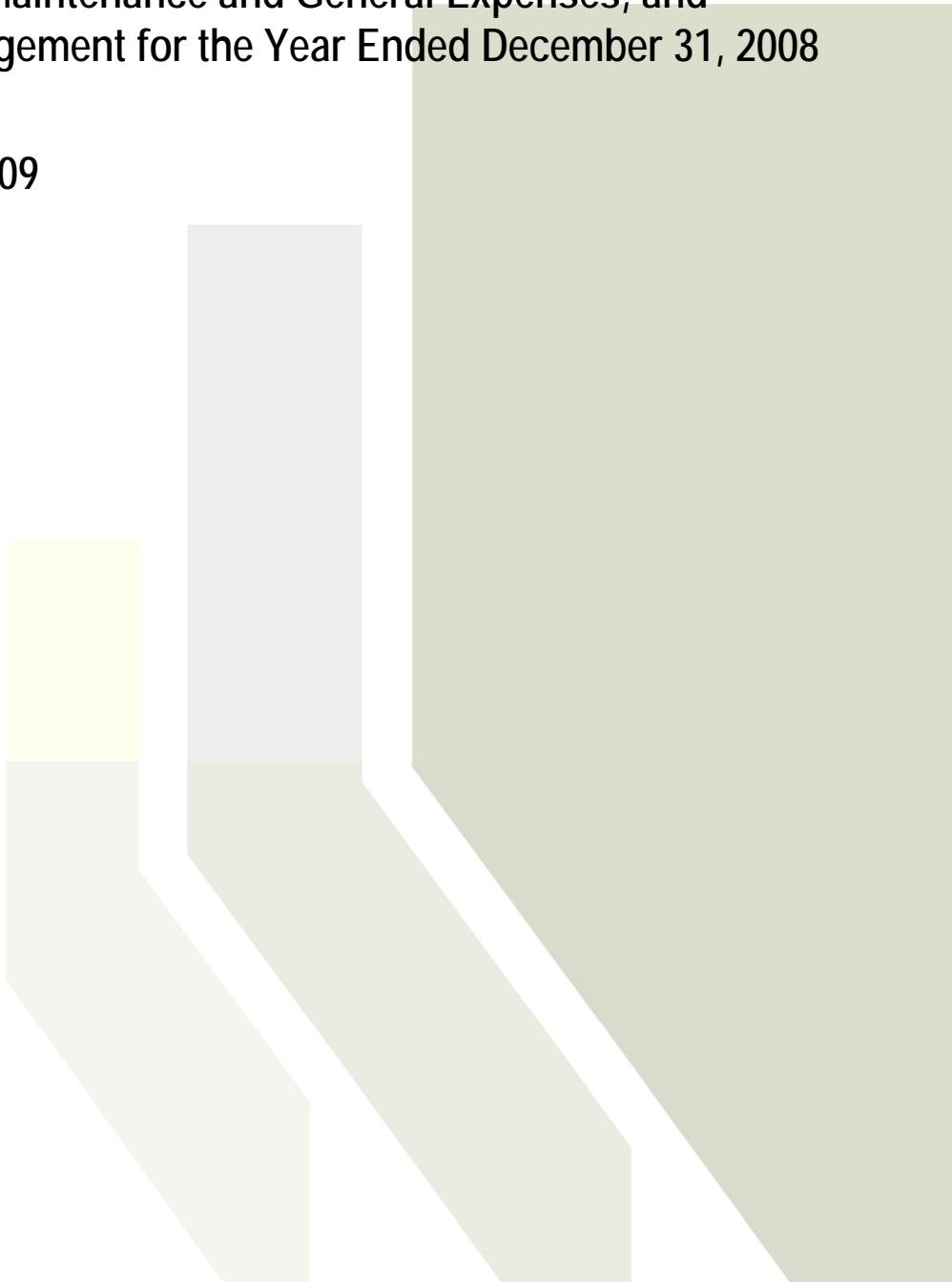
ATCO Electric Ltd.

Regulatory Audit of  
Operations, Maintenance and General Expenses, and  
Capital Management for the Year Ended December 31, 2008

November 2009

**Audit Group:**

- Nick Iannone
- Joel Thompson
- Silvia Danchuk
- Darcy Mazurkewich



**ALBERTA UTILITIES COMMISSION**

Regulatory Audit Report #2009-004: ATCO Electric Ltd.

Regulatory Audit of

Operations, Maintenance and General Expenses, and

Capital Management for the Year Ended December 31, 2008

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## Overview

1. The head office of ATCO Electric Ltd. (ATCO Electric) is located in Edmonton, Alberta. ATCO Electric has 38 field offices throughout its service territory in Alberta, and employs more than 1,400 people. ATCO Electric owns, operates and maintains over 69,000 kilometres (km) of transmission and distribution power lines. It operates an additional 12,000 km of distribution power lines on behalf of Rural Electrification Associations. ATCO Electric provides electricity distribution services to over 203,000 rural and urban customers in northern and east-central Alberta.

2. ATCO Electric also serves electricity customers in Canada's north through three subsidiaries: Yukon Electrical; Northland Utilities (NWT) Limited; and Northland Utilities (Yellowknife) Limited.

## Objective and Scope

3. The Audit Group of the Alberta Utilities Commission (AUC or the Commission) undertook this audit to provide the Commission an opinion<sup>1</sup> regarding two areas of ATCO Electric's business activities for the year ended December 31, 2008. These two areas were Operations, Maintenance and General Expense (OM&G), and Capital Management. The audit opinion expressed will relate to the effectiveness of the controls, policies and processes surrounding these areas, as well as compliance with applicable regulatory requirements for these two areas. In addition, the audit opinion will encompass information regarding these two areas that were contained in ATCO Electric's Annual Report of Operations and Financial Results<sup>2</sup> filing for the year ended December 31, 2008 which was submitted in accordance with [AUC Rule 005 – Annual Reporting Requirements of Operational and Financial Results](#) (AUC Rule 005).

4. The next two sections of this report explain in greater detail the nature of the work performed by the Audit Group to enable it to express an opinion on the areas outlined in the previous paragraph.

5. The Audit Group performed the fieldwork from August 31, 2009 to September 26, 2009 at ATCO Electric's head office located in Edmonton. Closing discussions were held with ATCO Electric's management on September 30, 2009.

## Operations, Maintenance and General Expenses

6. For the year ended December 31, 2008, ATCO Electric recorded OM&G expenses of \$188.5 million of which \$66.7 million pertained to the transmission services and \$121.8 million to the distribution services. The OM&G expenses include a variety of costs related to the delivery of electricity services to ATCO Electric's customers.

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<sup>1</sup> The Commission is not bound by the findings of the Audit Group with respect to any future hearings or proceedings in which an issue is raised or which was the subject of a prior audit.

<sup>2</sup> ATCO Electric Ltd., Alberta Utilities Commission Rule 005 - Report on Finances and Operations, Application No. 1605033.

7. The following summarizes the major categories of OM&G expenses:

Transmission (\$ millions)	Description	Distribution (\$ millions)
25.3	Direct Operating & Maintenance	66.4
-	Customer Accounting	13.4
-	Account Services & Public Information	3.6
5.6	Isolated Generation Operation & Maintenance	1.1
3.5	Allocated Share of General O&M	3.6
2.5	Allocated Share of Common Operations	4.5
(0.1)	Non-utility Items	(0.3)
<u>36.8</u>	Total Operation & Maintenance Costs	<u>92.3</u>
11.9	Allocated Admin & General	17.2
17.0	Linear Taxes and Franchise Fees	13.3
1.0	Farms, Irrigation Trans Operating Costs	(1.0)
<u>29.9</u>		<u>29.5</u>
<u>66.7</u>	Total Operations, Maintenance & General Expenses	<u>121.8</u>

8. The OM&G expenses are incurred through the normal operations of the business, and are reported and controlled through a system of internal controls which include numbered transaction documents (e.g., Purchase Requisitions & Purchase Orders), expenditure authorization limits, and transaction approval procedures.

9. On a monthly basis, a budget to actual variance report is prepared for each operating group. This report compares actual expenses to those budgeted for the month, the year-to-date totals, and provides a comparison of the current annual estimate to the annual budget. Variance explanations provided by the individual operating groups are summarized into a Variance Analysis report and forwarded to all Vice Presidents for review and sign-off.

10. The following were the significant audit procedures undertaken:

- A review of relevant AUC Decisions to identify the related regulatory requirements.
- A review of the documented procedures and control matrices prepared to comply with the Canadian security reporting requirements commonly referred to as C-SOX. This included risk control measures such as the authorization matrix, the reporting processes for areas of Purchasing, Inventory Control, Payroll, Financial Reporting and Accounts Payable.
- A review of how ATCO Electric determines its overhead rates and applies the overhead charges.
- An analysis and reconciliation of ATCO Electric's accounts and financial statements against relevant schedules in its 2008 filing under AUC Rule 005.
- A review of the operating and capitalization policies of ATCO Electric.
- A selection and testing of a sample of OM&G transactions to verify that the items were:
  - complete, properly supported, authorized and accurate;
  - costs were for utility business and had not been previously disallowed;
  - recorded in the correct entity, appropriate Uniform System of Accounts prime account, and time period; and
  - in accordance with regulatory requirements.

- A review of a sample of ATCO Electric's 2008 operating programs to verify that they were not disallowed.

## Capital Management

11. ATCO Electric experienced significant growth in capital expenditures in the 2008 business cycle. It recorded capital expenditures in excess of \$525 million in 2008, a 69 percent increase over the previous year. This significant growth was due to the need for ATCO Electric to replace, upgrade and add new assets to keep pace with the growth in demand for services.

12. The capital expenditures examined were incurred in the following main categories:

- Industrial and residential customer growth
- Capital upgrades and replacements
- Planned capital maintenance
- Transmission & Distribution capacity increases and improvements
- Facilities construction and upgrades related to existing and new sub-stations
- Alberta Electric System Operator assigned projects

13. An example of a major project in 2008 was the construction of the Britnell to Wesley Creek 240-KV transmission line to add 226 kilometres of lines to the electrical system. The 2008 capital expenditures on this project totaled \$113 million and the project is forecasted to be completed in 2010 at a cost of approximately \$210 million.

14. The following were the significant audit procedures undertaken:

- A review of relevant AUC Decisions to identify the related regulatory requirements.
- A review of the capital budget process and controls to identify the key components, procedures, control points, issues, and risks associated with the capital project management process.
- An analysis and reconciliation of ATCO Electric's accounts and financial statements against the relevant capital schedules in its 2008 filing under AUC Rule 005.
- A selection and testing of a sample of capital projects started in the audit period, to verify that the selected items were properly approved.
- A selection and testing of a sample of completed capital projects to verify that the charges were recorded properly, that adequate closure procedures existed, and the procedures were executed in a timely manner.
- A test of project invoices to verify that they were complete, properly supported and accurate; were recorded in the correct time period; had been properly authorized; and were in accordance with both ATCO Electric's capital policies and the Commission's regulatory requirements.
- A review of completed projects sampled to verify that the charges were moved from construction accounts to the appropriate fixed assets accounts.
- A selection and testing of a sample of asset retirement transactions to check for proper depreciation and allocation treatment.
- A review of the methodology and rates used to calculate the amounts in the Allowance for Funds Used During Construction recorded to verify that the amount was calculated and applied correctly and complied with Commission requirements.
- The sampling and testing of project change orders, to check that explanations were provided and that they were authorized in accordance with ATCO Electric's policies.

**Conclusion**

15. Based on the objective, scope and significant procedures set out above, the Audit Group is of the opinion that ATCO Electric Ltd. has demonstrated in all material respects for the year ended December 31, 2008 for its OM&G and Capital Management activities: that it had effective controls, policies and processes in place; that it complied with the applicable regulatory requirements for these areas; and that the relevant information provided in its 2008 Rule 005 filing with the Commission was presented fairly.

16. The Audit Group thanks the ATCO Electric management and staff for the cooperation and assistance they provided during the course of the audit.