

Chief Financial Officer's Report to
Gas, Power and Telecommunications
2019 July 25

ISC: UNRESTRICTED
GPT2019-0920

Decision Report – ATCO Utilities IT Common Matters

EXECUTIVE SUMMARY

The Alberta Utilities Commission (AUC) held a proceeding to consider whether to approve the prices contained in the information technology (IT) master service agreements (MSAs) between ATCO Utilities and Wipro Solutions Canada Limited (Wipro) for inclusion in each of the regulated utilities' revenue requirements.

The City intervened in the proceeding with the objective to achieve just and reasonable natural gas utility rates. The City's contended that ATCO's requirement that IT services suppliers bidding on the MSA contract must also purchase ATCO I-Tek at an inflated price resulted in utility rates for consumers that were higher than they would have otherwise been.

The AUC determined that ATCO Utilities failed to demonstrate that the IT pricing in the MSAs would result in just and reasonable rates. The AUC decided that in the first year (2015) of the MSAs, IT expenditures that may be included in customer rates are to be reduced by 13 percent. For each of the remaining 9 years of the MSAs (2016 to 2024), an additional annual decrease of 4.61 percent will be imposed across all IT cost towers (a grouping of like expenditures) on a weighted average basis.

ADMINISTRATION RECOMMENDATION:

That the Gas, Power and Telecommunications Committee recommends that Council:

1. Receive this Report for information; and
2. Direct that Attachment 1 be held confidential pursuant to Section 23 (local public body confidences) of the *Freedom of Information and Protection of Privacy Act* and not be released.

PREVIOUS COUNCIL DIRECTION / POLICY

To report on the decisions of the AUC with respect to proceedings where The City has actively participated as an intervener.

BACKGROUND

Prior to 2014 December 31, ATCO Utilities obtained IT services from ATCO I-Tek, an unregulated affiliate company. The pricing of these services was evaluated in the ATCO Evergreen 2 proceeding where The City intervened and demonstrated to the AUC that the prices paid to ATCO I-Tek for IT and Customer Care and Billing services from the year 2010 onward were above market rates and led to higher than necessary utility rates for consumers. Refunds to ATCO Utilities' customers amounted to over \$50 million.

In 2014 August, ATCO sold ATCO I-Tek to Wipro for \$204 million and concurrently contracted with Wipro for 10-year MSAs for the provision of IT services. The AUC held the ATCO Utilities IT Common Matters proceeding to determine whether to approve the IT services costs under the MSAs for inclusion in ATCO Utilities' revenue requirements, which are recovered from utility customers through rates. ATCO Utilities bear the onus of demonstrating the prudence of their costs and that any changes to rates resulting from the inclusion of the MSA costs in their revenue requirements are just and reasonable.

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INVESTIGATION: ALTERNATIVES AND ANALYSIS

The IT sourcing strategy of ATCO was to rely on a multi stage competitive bid process whereby the supplier of IT services would simultaneously purchase ATCO I-Tek. ATCO's objectives were to purchase IT services at fair market value (FMV), minimize transition costs and maximize the value received on the disposition of ATCO I-Tek.

ATCO contends that the AUC should only evaluate whether the IT services were provided at FMV and thereby result in just and reasonable rates for customers. ATCO relied on a benchmark study by Gartner Consulting and a price assessment by KPMG to determine that the MSAs prices were at FMV. The AUC disagreed with ATCO stating that FMV is only one criterion to be considered in the determination of just and reasonable rates.

The City's expert witness, PA Consultants (PAC), found that ATCO's primary goal in the transaction was to maximize the sale price of ATCO I-Tek and that ATCO's sourcing strategy harmed customers. By limiting the competition to suppliers that were both able and interested in purchasing ATCO I-Tek the market options were constrained. Furthermore, evidence in the proceeding revealed that bidders altered their bids in a manner that demonstrates a direct relationship between increases in the proposed upfront payment for the ATCO I-Tek purchase and the proposed MSA pricing.

The Utilities Consumer Advocate (UCA) stated that ATCO's tied transactions should be evaluated based on whether the least cost option, associated with safe and reliable utility service, was chosen along with no harm to customers and tests for prudence.

The AUC found that ATCO failed to demonstrate that their IT sourcing strategy was prudent because they did not adequately consider all the available options or whether the price paid was the least cost option that met the needs of ATCO Utilities. The Commission also found that due to numerous failings and lack of transparency, neither the KPMG price assessment nor the Gartner benchmark established that the MSA pricing was at FMV.

The AUC decided that adjustments were necessary to the MSA pricing both in the first year of the agreement and over the subsequent years of the agreement. Referring to evidence from The City's expert witnesses, who the AUC found to be very credible, and informative aspects of the Gartner benchmark, the AUC directed a reduction of 13 percent to the first year of the MSAs. In year 2 to 10 of the MSAs, a glide path that reduces prices on a weighted average basis across cost towers of 4.61 percent each year will be imposed.

ATCO Gas and ATCO Electric Distribution are under Performance-Based Regulation (PBR) and the AUC has directed them to make this adjustment to the going-in rates for the second PBR term (2018-2022). They will file the compliance to this decision in their next annual PBR applications in the fourth quarter of this year. ATCO Pipelines and ATCO Electric Transmission remain under cost of service regulation and are ordered to file their compliance in their next general rate or general tariff applications.

The AUC granted ATCO extensive confidentiality on the commercial aspects of the Wipro transaction restricting the ability to report on the decision in dollar terms. To ensure that the ordered reductions are made as directed, The City will audit the compliance applications of ATCO Gas and ATCO Pipelines.

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Stakeholder Engagement, Research and Communication

The UCA was also an active intervener in this proceeding and there was collaboration between the UCA and The City.

Strategic Alignment

The City's participation in the ATCO Utilities IT Common Matters proceeding was in alignment with the mandate of the Gas, Power and Telecommunications Committee.

Social, Environmental, Economic (External)

The AUC decision on this proceeding will result in lower cost utility services for all customers of the ATCO Utilities.

Financial Capacity

Current and Future Operating Budget:

The decision on this proceeding will lower the cost of utility services for the City of Calgary. The amount of decrease will be known when ATCO files its compliance application. This proceeding began in 2015 June with the yearly expenditures charged to the annual GPT budget. Expenditures in 2019 are within budget.

Current and Future Capital Budget:

This decision will have no impact on the current or future capital budget.

Risk Assessment

There is a possibility that ATCO will seek relief at the Alberta Court of Appeal. Participation in an appeal would require additional expenditure by The City.

REASON(S) FOR RECOMMENDATION(S): This report provides information with respect to the AUC decision on the ATCO Utilities IT Common Matters proceeding in which The City participated as an intervener.

ATTACHMENT(S)

1. Attachment 1 - Additional Information on ATCO IT - CONFIDENTIAL