Corporate Planning & Financial Services Report to Regular Meeting of Council
2024 October 29

ISC: CONFIDENTIAL
C2024-1098

New Franchise Agreement for Natural Gas

PURPOSE

This report presents the new natural gas franchise agreement for ATCO Gas and an update on the franchise fee rates that were derived based on Council's direction on the revenue target on 2024 July 17.

PREVIOUS COUNCIL DIRECTION

Refer to Attachment 1.

RECOMMENDATIONS:

That Council:

1. Authorize a new franchise agreement for natural gas (Attachment 3) aligned to the Quantity Only methodology;
2. Give first reading to Bylaw 44M2024 (Attachment 4);
3. Withhold second and third readings of Bylaw 44M2024 until the Alberta Utilities Commission approves a new franchise agreement between The City of Calgary and ATCO Gas;
4. Direct that the Report and Attachments 1, 2, 3, 4, 5, and 7 be held confidential pursuant to Section 23 (local public body confidences) of the *Freedom of Information and Protection of Privacy Act*, to be released publicly when Council rises and reports; and
5. Direct that the Closed Meeting discussions and Attachment 6 remain confidential pursuant to Section 25 (Disclosure harmful to economic and other interests of a public body) of the *Freedom of Information and Protection of Privacy Act*, to be reviewed no later than 2026 December 31.

CHIEF ADMINISTRATIVE OFFICER/GENERAL MANAGER COMMENTS

The Chief Financial Officer and General Manager of Corporate Planning and Financial Services concurs with this report. Implementation of the Quantity Only methodology for Natural Gas meets Council's desire for predictability and reliability. Providing a transition period for ATCO to align their systems for implementation ensures ATCO can comply with the Franchise Fee agreement. Administration's recommendations are in the public's interest

HIGHLIGHTS

- To improve affordability, transparency, and certainty for Calgarians, we are implementing a new franchise fee model for electricity and natural gas to eliminate the current tie to fluctuating market rates and implement instead a transparent fixed rate directly tied to the amount of energy used.
- On 2024 July 30 Council approved a revised timeline of 2025 January 1 for implementation of a Quantity Only model for The City to collect franchise fees from electricity and natural gas.
- Administration worked with ENMAX and ATCO Gas to establish new franchise agreements and to establish new franchise fees for electricity and natural gas that:
    - Provide more stability and predictability for Calgarians.

- Support affordability concerns of Calgarians and businesses.
- Minimize shifts across user classes with the intent of not materially shifting the financial responsibility from one user class to another.
- Maintain and improve The City's financial sustainability ensuring The City continues to collect what we budget for.

- On 2024 September 27, ENMAX filed an application with the Alberta Utilities Commission following the Quantity Only Methodology and Franchise Agreement authorized by Council on 2024 September 17.
- To allow ATCO Gas time to update its billing system to accommodate the Quantity Only methodology for collecting franchise fees, the recommended new franchise agreement for natural gas in this report will utilize a transitional rate which aligns to the current Total Bill methodology but substitutes the variable "gas cost flowthrough rate" with a fixed rate of $3.15. The City recommended, and ATCO Gas agreed to, a period of up to 2026 December 31 for this transition rate. A Quantity Only methodology will be used for the remaining 18 years of the agreement, the rate for which will be determined in Q3 2026 and implemented 2027 January 01.
- Upon authorization and Council direction, we will support ATCO Gas in filing a new franchise agreement and franchise fee rate structure with the Alberta Utilities Commission by mid-November.

DISCUSSION

Administration has been collaborating with our partners at ENMAX and ATCO Gas to develop a new franchise agreement with new fee rates that align with the Quantity Only methodology. On 2024 September 17, Council approved authorized a new Franchise Agreement with ENMAX. The City supported ENMAX in filing an application with the new franchise agreement with the Alberta Utilities Commission on 2024 September 27. The evaluation process is expected to take approximately three months.

Negotiating a new agreement with ATCO Gas was more complex. One of the challenges concerned the time needed for the coordination, development, and implementation of the changes in ATCO Gas's billing system to accommodate the Quantity Only methodology. The City recommended, and ATCO Gas agreed to, a period of up to 2026 December 31 for a transition rate to allow adequate time to make the billing system changes. The result is a new franchise agreement for natural gas with ATCO Gas that incorporates a two-part rate structure.

The transition rate mirrors the current Total Bill methodology of charging 11.11% of the gas cost flowthrough rate (a fluctuating market rate) plus 11.11% of the delivery cost, except it substitutes the gas cost flowthrough rate with a fixed rate of $3.15 for 2025. This complies with the legislated requirement to not have franchise fees dependent on fluctuating market rates while giving customers stability and continuity of approach for this short-term franchise fee.

The recommended transition rate ensures that Council direction is met in that:

- The City meets its 2025 revenue target of $69.9M, contributing to the $19.7 million per year in 2025 and 2026 to fund the services Calgarians rely on and capital maintenance costs that have limited other sources of funding;
- Customer classes will not experience significant year-over-year changes to their bills;

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- The new franchise agreement can be approved and implemented by the legislated deadline of 2025 March 17.

Attachment 2 gives an overview of this analysis.

The franchise fee rate will shift to the Quantity Only methodology beginning 2027 January 01 and remain in place for the remaining 18 years of the 20-year agreement. The specific franchise fee rate for 2027 will be determined in the latter part of 2026 and will be based on 2027 consumption forecasts. Under the Quantity Only methodology, low-, mid-, and high-use customers, which comprise 99.99% of ATCO Gas customers in Calgary, are expected to see an overall decline in natural gas franchise fee paid relative to the existing Total Bill methodology. The Quantity Only rate can be adjusted on an annual basis with Council direction.

The new franchise agreement with ATCO Gas (Attachment 3) is based on the Alberta Utilities Commission template for natural gas franchise agreements, but modified to reflect the Quantity Only methodology and the transition period rate, as well as to accommodate the unique legislative landscape of The City which possesses several bylaws that are not generally in place in other Alberta municipalities, such as the Right of Way Bylaw and the Streets Bylaw.

After Council authorizes the new agreement and gives first reading to Bylaw 44M2024 (Attachment 4), Administration will continue working with ATCO Gas to support their new franchise agreement filing with the Alberta Utilities Commission with a targeted submission in mid-November. Attachment 5 illustrates our progress against the revised timeline approved by Council 2024 July 30 for this work.

Residential Customer Impacts

The *Calgary & Region Economic Outlook 2024-2029: Fall 2024* report projects an average natural gas cost of $3.11/GJ for 2025, which is very close to our chosen fixed rate of $3.15/GJ. This will result in marginal differences between the current model and the transition rate for projected 2025 franchise fees. However, since 2024 saw historic lows for the price of natural gas, for the average residential customer the franchise fee is projected to increase by $1.08 per month under the proposed transition rate for 2025, amounting to an overall increase of 1.5% in the total natural gas bill, which is estimated to be $83 per month. This is estimated to result in a year-over-year increase of ~$11M in total natural gas franchise fees collected by The City. This is in line with the 10-year average (without inflation adjustment) that consumers paid, in line with the approach Council used to direct franchise fee revenue targets for 2025.

Overall, the new transition rate:

- Minimizes the shifting the financial responsibility from one user class to another,
- Provides more stability and predictability than the current model,
- Allows for more predictability in collecting what we budget for through a stable revenue source to fund the services and infrastructure Calgarians rely on.

EXTERNAL ENGAGEMENT AND COMMUNICATION

☒ Public engagement was undertaken

☒ Public/interested parties were informed

☒ Dialogue with interested parties was undertaken

☐ Public communication or engagement was not required

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- Public notice for the new natural gas franchise fees will be advertised, which will provide an opportunity for the public and interested parties to submit questions and inquiries through email or by calling 311.
- Extensive engagement with ATCO Gas has taken place to establish new franchise fees and negotiate new franchise agreements.
- The Alberta Utilities Commission was consulted to clarify the process and expectations for filing for approval new franchise fees and agreements.
- The Government of Alberta was consulted to clarify expectations regarding *The Utilities Affordability Statutes Amendment Act*, 2024.

IMPLICATIONS

Social

The City set out to revise its franchise fee methodology to address affordability for Calgarians. The new methodology is designed to remove the volatility of the current model for more stability and predictability and allows consideration for setting appropriate rates for Calgarians and businesses while not materially shifting the financial responsibility from one class to another.

Environmental

The new franchise agreement for natural gas has a transition period of two years before the Quantity Only methodology is implemented. Given the proposed fee structure, these first two years will closely mirror current state, so the environmental benefits will not immediately be realized.

Once we are past the first two years, the Quantity Only methodology will apply the fee to the energy component of the utility bill only, and this will act as a disincentive to consume energy. Additionally, the Quantity Only methodology will help increase energy equity and meet the goals for the energy equity pathway in the Climate Strategy.

Economic

Franchise fees are broadly based, inclusive of all developed properties in Calgary including those exempt from paying property taxes, thus diversifying The City's revenue base. Franchise fees support a balance between property taxes and other revenues, one of The City's fiscal objectives.

Service and Financial Implications

Change in rates or fees

The new Quantity Only methodology was designed to allow The City to collect what we budget for more accurately than at present and minimize our operating budget variances.

RISK

We will use the contingency time built into the timeline Council approved on 2024 July 30 to implement the new franchise agreement with ATCO Gas. However, our risk management strategies are being utilized to ensure we meet the legislated deadline of 2025 March 17. Administration has been keeping the Alberta Utilities Commission aware of what to expect for

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our application, and since The City's new franchise agreement with ENMAX has already been filed, the Alberta Utilities Commission will have familiarity with the Quantity Only approach, thus reducing the timeline risk.

The financial risk associated with this work is reduced compared to the initial assessment in 2024 July. If the new rate structure isn't in place by 2024 January 01, there will be a difference in franchise fee revenue collected in 2025 based on the projections for the new rate. However, the current agreement can remain in place until 2025 March 17, so The City will still collect franchise fee revenue and the overall financial risk vs our current model is unchanged.

As compared with the City's current agreement with ATCO Gas, the terms of the new franchise agreement will be more consistent with franchise agreements in place in other municipalities. The City will now have many of the same risks, benefits and protections under the new agreement as exist for other municipalities so while the risk profile has shifted the overall risk for The City remains the same.

The overall risk profile therefore remains acceptable. With a full set of risk management strategies in place, Administration is confident in making the recommendation of this report.

A full risk assessment is provided in Attachment 6.

ATTACHMENTS

1. Background and Previous Council Direction
2. New Franchise Fee Structure for Natural Gas
3. New Franchise Agreement: Natural Gas
4. Proposed Bylaw 44M2024
5. Timeline update
6. Risk Assessment
7. Presentation

Department Circulation

General Manager/Director	Department	Approve/Consult/Inform
Carla Male, Chief Financial Officer and General Manager	Corporate Planning & Financial Services	Approve
Chris Stewart, Director	Corporate Planning & Performance	Approve
Amit Patil, Director	Supply Management	Approve
David Mercer, Assistant Director	Law, Legislative Services & Security	Approve

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