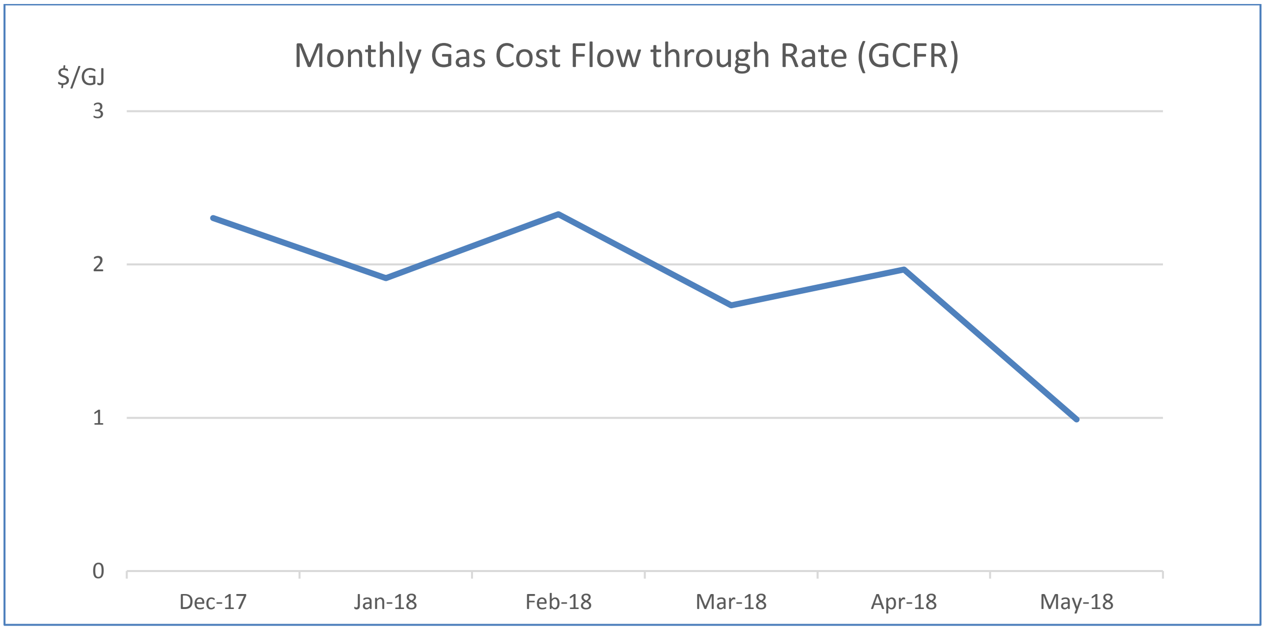
ENERGY PRICES AND MARKETS

Natural Gas

The May gas cost flow-through rate (GCFR) was $0.989/GJ.



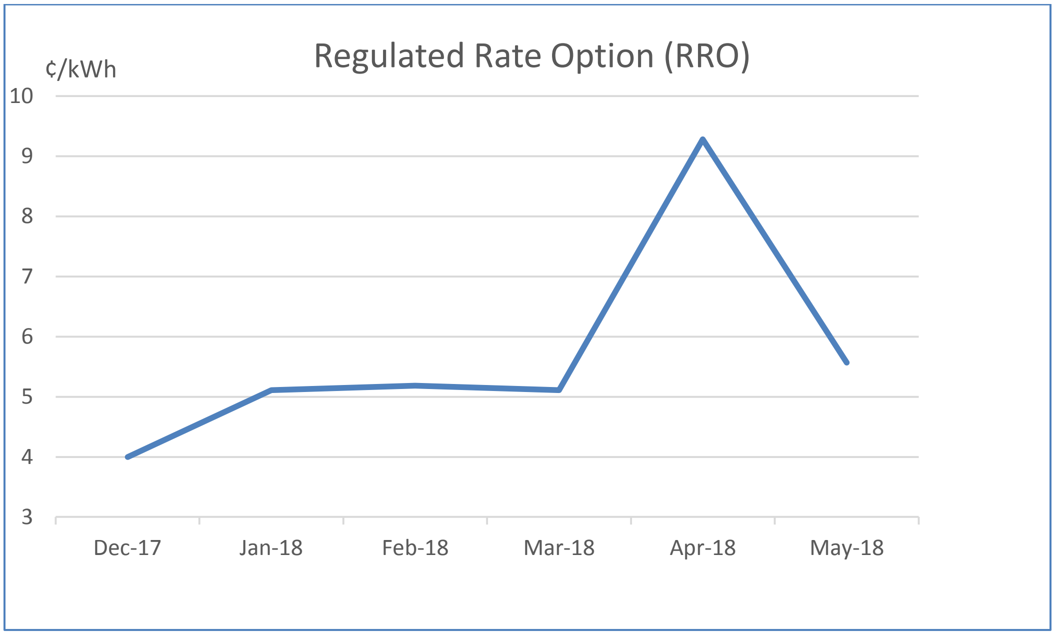
The GCFR price is made up of essentially four components;

1. Deferred Gas Account (DGA) carryover – the variance from the previous month.
   May 2018 – $0.096/GJ
2. Cost of Gas – the weighted average price of gas purchased.
   May 2018 – $0.835/GJ
3. Forecast charge – the approved amount for administration costs.
   Fixed at $0.023/GJ.
4. Return margin – this is essentially the profit for providing the GCFR product.
   Fixed at $0.035/GJ.

The natural gas forward strip shows prices remaining near $1 all summer.

Electricity

The regulated rate option (RRO) in May was $55.658/MWh (5.556¢ per kWh).



The RRO is not a flow-through product. RRO products are provided in accordance with an Energy Price Setting Plan (EPSP) which is approved by the AUC. The RRO price is made up essentially of the following bundle of costs;

1. Portfolio price – Essentially a mix of flat and peak priced power procured for the month.
   May 2018 - $51.54/MWh
2. Regulatory Costs – Costs incurred by interveners and the independent advisor in EPSP applications and filings
   May 2018 - $0.148/MWH
3. Various Risk Compensation – RRO providers get compensated for a number of administrative, settlement and market risks
   May 2018 - $0.629/MWh
4. Return Margin and Payment in Lieu of Tax Regulation (PILOT) – PILOT is paid on the Return Margin
   May 2018 - $3.34/MWh

Alberta saw higher prices for the first part of the month as a market response to two TransAlta coal plants being mothballed and a few temporary outages with Genesee and Shepard.

During the first half of May, prices reached triple digits over multiple hours, and for the first time since the Government of Alberta placed the 6.8 cents price ceiling on the RRO, we saw the RRO hit and surpass the cap. RRO customers were protected at the 6.8 cents per KWh with the difference paid by the provincial government.

Alberta Internal Load, averaged 9,925 MW ranging from 8,032 MW to 11,567 MW which is a 5% increase from load in April 2017 and a decrease of 7% from last month.

UTILITY REGULATION

Mothballing

On March 16, 2018, the Market Surveillance Administrator (MSA) filed a complaint about the Alberta Electric System Operators' independent system operator rules Section 306.7, Mothball Outage Reporting.

The Mothball Rule was implemented by the Alberta Electric System Operator (AESO) in 2016 and sets out how and when generators report temporary closures of generating facilities of more than five megawatts for periods up to two years. Sundance #3 (368 MW) and Sundance #5 (406 MW) were mothballed at the end of 2018 March.

In the MSA complaint filed under the Electric Utilities Act, the MSA said it believes the AESO's Mothball Rule does not support the fair, efficient and openly competitive operation of the electricity market, is not in the public interest, and may have an adverse effect on the structure and performance of the market. The concern is that a large generator, with multiple generation facilities, could mothball some generation facilities in an effort to create a supply shortage and thereby manipulate an increase in the market price.

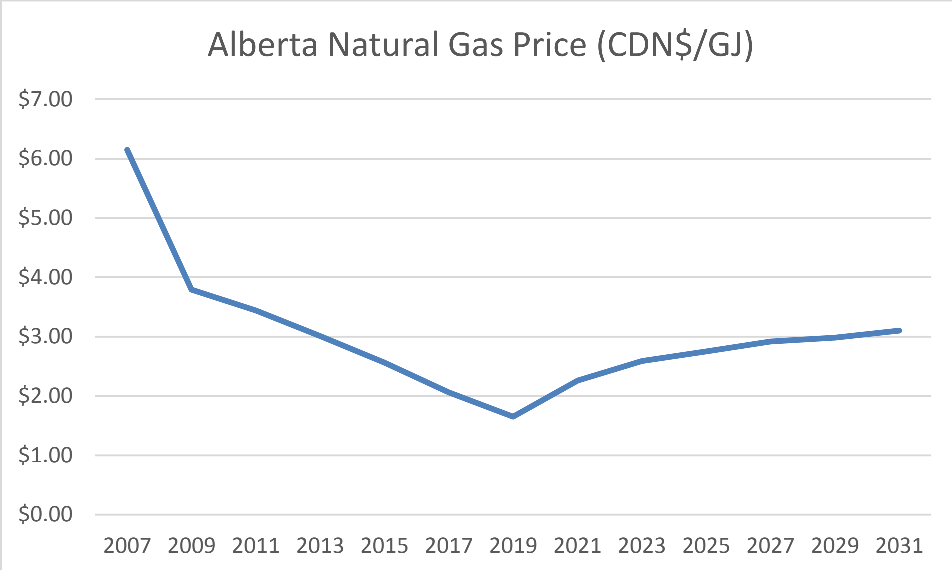
The MSA has asked the AUC to consider the Mothball Rule, and if it is found to contravene the Electric Utilities Act, to either require the rule to be removed, or to amend it to address adverse effects on the structure and performance of the market and to address the public interest.

Interesting not only because of the policy issues involved, but also because the AESO and the MSA are both provincial agencies. The only implications for The City would be the market distortion (high electricity prices) which could occur due to the strategic mothballing by large generators.

Natural Gas Price Woes

Pipeline constraints, seasonal maintenance issues and surging output in Western Canada are all contributing to a compounding problem of low prices for natural gas.

Canadian natural gas producers have been hammered by volatile markets since last summer, with prices in Alberta falling into negative territory at one point due to transportation bottlenecks. Gas pipelines are essentially full and while operators such as TransCanada have proposed expansions to increase shipping capacity out of the province, major additions are at least two years away. The lack of pipeline access and high levels of supply likely mean prices are going to stay low for the foreseeable future. The below forecast price data is from the EDC Associates – 2018 Second Quarter update.



Utility Asset Disposition and Bill 13

Utility asset disposition (UAD) broadly refers to situations where a regulated asset is sold, destroyed or no longer used to provide utility service. The Supreme Court stipulated in a case known as *Stores Block*: *ATCO Gas & Pipelines Ltd. v Alberta (Energy & Utilities Board)*, that the regulator could not direct that the upside on the sale of land be shared between shareholders and ratepayers.

Stores Block dealt with the power of Alberta's utility regulator (then the Alberta Energy and Utilities Board (AEUB), now the AUC) to direct the disposition of the proceeds received on the sale of utility assets that were no longer required by the utility to provide service. The case involved a non-depreciable asset, land, which ATCO originally acquired in 1922. When it was sold in 2001 there was a significant difference between the value at which the asset was carried on ATCO's books ($225,000) and the price ATCO received ($6.25 million). The majority of the Supreme Court of Canada ruled that neither the *Gas Utilities Act*, nor the more general provisions of the *Alberta Energy and Utilities Board Act*, gave the regulator any authority to deal with that upside. The asset was the property of ATCO and the fact that it had been a utility asset did not change that fundamental principle. The AEUB had no authority to direct that the upside be shared between shareholders and utility customers.

The AUC has adopted the logic of *Stores Block* for losses, suggesting that if gains associated with the disposition of utility assets accrue to the utility owner and not customers, then the losses that occur when an asset becomes stranded or is no longer required for utility purposes before it has been fully depreciated, should also accrue to the utility owner.

The utilities do not agree with the AUC interpretation of the UAD issue and have been lobbying the Alberta government to change the legislation. The changes wanted by the utilities would revise the current position that ratepayers are not required to keep the utility whole in the case of assets no longer required to provide utility service. The proposed changes to Bill 13 are not yet complete. On May 23 the Alberta government notified stakeholders that the legislation changes regarding UAD were being removed from Bill 13. The indication from the Alberta government was that it is unlikely that there will be more discussion on this issue prior to the next election.