**Diane Roy**
Director, Regulatory Affairs - Gas
**FortisBC Energy Inc.**

16705 Fraser Highway
Surrey, B.C. V4N 0E8
Tel: (604) 576-7349
Cell: (604) 908-2790
Fax: (604) 576-7074
Email: diane.roy@fortisbc.com
www.fortisbc.com

Regulatory Affairs Correspondence
Email: gas.regulatory.affairs@fortisbc.com

July 23, 2012

Commercial Energy Consumers Association of British Columbia
c/o Owen Bird Law Corporation
P.O. Box 49130
Three Bentall Centre
2900 – 595 Burrard Street
Vancouver, BC
V7X 1J5

Attention: Mr. Christopher P. Weafer

Dear Mr. Weafer:

**Re: FortisBC Energy Utilities (comprised of FortisBC Energy Inc. ("FEI"), FortisBC Energy Inc. Fort Nelson Service Area ("FEFN" or "Fort Nelson"), FortisBC Energy (Vancouver Island) Inc. ("FEVI"), and FortisBC Energy (Whistler) Inc. ("FEW") Common Rates, Amalgamation and Rate Design Application (the Application)**

**Response to the Commercial Energy Consumers Association of British Columbia ("CEC") Information Request ("IR") No. 2**

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In accordance with Commission Order No. G-83-12 setting out the Regulatory Timetable for the review of the Application, the FEU respectfully submit the attached response to CEC IR No. 2.

If there are any questions regarding the attached, please contact Paul Craig at 604-592-7459.

Yours very truly,

**on behalf of the FORTISBC ENERGY UTILITIES**

***Original signed:***

Diane Roy

Attachment

cc (e-mail only): Commission Secretary
Registered Parties

**1. Exhibit B-7, CEC 1.2.4**

**Response:**

The FEU agree that both regional zone rates and postage stamp rates have a basis of fairness for rate setting.

The primary reason the FEU are proposing postage stamp rates is because they provide the most equitable rates for FEU's customers. As discussed in Section 6.2 of the Application, postage stamp rates are the most widely accepted and equitable rate setting model. Postage stamp rates are the most appropriate for an amalgamated FEU and provide benefits for all customers.

The beneficial effects for FEVI and FEW customers are an important benefit of postage stamp rates given the unique circumstances of the FEU.

1.1 Please confirm that the FEI customers will uniformly see rate increases as a consequence of the proposed amalgamation and postage stamp rate setting.

**Response:**

Confirmed. The FEU have applied the rate increase uniformly to all rate schedules (i.e. taking into consideration that the daily basic charge is not adjusted, the same percentage increase has been applied to the delivery rates for all rate schedules). Under the FEU's proposed phase-in, FEI customers will see a modest rate increase in 2014, with no further amalgamation-related increases in 2015 and 2016. In 2017, FEI customers will experience a second rate increase that will fully transition FEI customers to amalgamated rates. This strategy delays the impact of amalgamated rates and provides a smooth transition for all FEI customers.

1.2 Please confirm that in the rate design the FEU are proposing the design is expected to be revenue neutral in that the FEU are not undertaking this to increase its revenues.

**Response:**

The rate design proposed by the FEU is designed to be earnings neutral with a minor reduction to revenues as a result of the expected cost savings, net of the costs of amalgamation.

1.3 Please confirm that is some customers, FEVI and FEW above, are benefiting (paying lower rates) from the rate design proposals that others will be paying more and on a net basis will not be benefiting.

**Response:**

Not confirmed. While from a rate perspective FEVI and FEW customers will benefit, as explained in section 6 of the Application and expanded on in response to various information requests, all of the FEU's customers will derive some benefit from the amalgamation and postage stamp rates proposal. As discussed in section 6.2 of the Application, postage stamp rates will provide more stable rates for the smaller service areas of FEVI, FEW and FEFN. The susceptibility of these smaller rate bases to rate instability is discussed in section 4.4 of the Application. The rate stability benefit will also accrue to FEI. For instance, FEI customers will benefit from sharing the costs of its aging infrastructure costs over a relatively larger customer base. At the same time, the cost of the relatively new FEVI and FEW systems will decrease as they continue to depreciate. All customers of the FEI Amalco will benefit from the simplicity and ease of administration of the proposed rates as described in section 6.4 of the Application. FEFN, as well as FEVI and FEW, will benefit from the facilitation of service offerings and the expanded rate options offered by the FEI rate structure. In addition, the proposed amalgamation and postage stamp rates will result in regulatory, reporting and operational efficiencies, which will reduce the overall cost of service for FEI Amalco compared to the FEU as discussed in section 6.6 of the Application.

1.4 Please confirm that it is the FEU position that this balance of some benefiting (paying lower rates) and some paying higher rates is the consequence of the postage stamp rate setting across Amalco and that FEU believes this to be fair.

**Response:**

It is confirmed that the annual bill impacts, both increases and decreases, are a result of the amalgamation and postage stamp proposal and the FEU believe this to be fair and reasonable for all of the FEU's customers. As outlined in the Application, in particular, in section 6.1, the main principle behind amalgamation and common rates is fairness among all of FEU's customers, regardless of location. This means that under common rates, all customers within a rate class will pay the same rate, irrespective of where the customer resides.

The amalgamation proposal will result in some of the FEU's customers paying higher rates, while other customers pay lower rates. However, on the whole, common rates are more equitable. It is difficult to justify continuing rate disparity among groups of customers, when the majority of customers (Mainland, Inland & Columbia) already pay the same rates. The Mainland, Inland and Columbia regions account for approximately 90% of the FEU's customers, and with the exception of minor differences in midstream rates, these customers have paid common rates since 1993. The current differences in rates across the FEU are the result of the FEU's growth by acquisition, and do not reflect a careful consideration of the equities among all of the FEU's customers combined.

**2. Exhibit B-7, CEC 1.3.2**

**Response:**

The rate differences are an artifact of the FEU's growth by acquisition which has resulted in three separate companies, four distinct rate bases and six service areas. Any risk taken by the shareholder in making acquisitions is not a factor in the rate differences. Any acquisition was not predicated on a requirement or assumption of amalgamation and postage stamp rates.

2.1 Please confirm that when a shareholder acquires a separate company or service area that it is taking on the risks of that entity and provided that the entity is not amalgamated and included in a postage stamp rate the shareholder bears those risks separately with each entity and is unable to recover the cost of each separate entity from the other entities customers.

**Response:**

It is confirmed that the risk that the shareholder takes on may differ for each separate company or service area, and that the costs of a particular utility cannot be recovered from the customers of other utilities. The shareholder is entitled to a fair return, and is compensated through the allowed cost of capital for the relative risk of the utility that it owns.

To clarify, in response to CEC IR 1.3.2, the FEU were stating that the rates of the individual utilities themselves (other than the ROE/capital structure component) are not different because of differing risks for those utilities. The ROE/capital structure component is the part of the rate determination that is relevant to risk, and there has been extensive discussion in the Application and in response to IRs on what the impact of amalgamation and postage stamping is on the ROE/capital structure.

2.2 Please confirm that if one of the separately regulated entities, so acquired, fails with stranded costs not recoverable from its customers then the shareholder would have to bear the loss associated with the failure and the stranding of the costs.

**Response:**

Since costs can only be recovered from either customers or the shareholder, to the extent that costs are not recoverable from customers, the shareholder would bear the loss.

2.3 Please confirm that higher rates, particularly those which place the service increasingly at risk of losing customers to competitive services, will increase the risk that the entity could fail with stranded costs.

**Response:**

The FEU agree that, if everything else is held constant, then significantly higher rates that are either uncompetitive or marginally competitive such that loss of customers may occur can lead to increased risk. However, the assumption of "everything else held constant" is unrealistic. For example, as natural gas rates increase, customers may switch to electricity. Over time, additional electric infrastructure may need to be built, resulting in higher electricity rates, that could affect the relative price competitiveness of the services.

At this time, the FEU do not foresee a significant risk of stranded costs for their utilities.

2.4 Please confirm that separate service entities with higher cost, particularly those with higher costs than competitor services, will have higher rates so long as the utility is recovering its costs of service including a return on its investments.

**Response:**

The FEU confirm that, since costs are recovered in rates, higher costs mean higher rates. Regarding the relationship to competitor services, rates are only one factor in the determination of competitiveness.

2.5 Please confirm that the risks of failing with stranded costs are not linear with respect to the level of rates relative to the prices for competing services, so that, all else being equal, the closer the rates of a separate entity get to the point of non-competitiveness with competitor prices the greater the incremental risk of failing.

**Response:**

Competitive risk depends on a number of factors, of which price is only one. For a discussion of whether or not risks with respect to the level of rates relative to the prices for competing services are linear, refer to the response to CEC IR 2.12.1.

**3. Exhibit B-7, CEC 1.4.2**

> For example, FEI customers pay relatively lower rates due to the centralized load centers in the Lower Mainland, which creates benefits of scale for all customers no matter where they live in FEI's service territory.

3.1 Please confirm that the Lower Mainland 'centralized load centre' has characteristics of being densely populated with a large population, served by an older systems with lower historical embedded costs, closer to the mainline transmission system and stable in terms of total use with relatively low growth.

**Response:**

The FEU interpret the characterization of "closer to the mainline transmission system" to be relative to the two other existing regions in FEI's service territory. As such, this statement is not confirmed.

The FEU however, do confirm that the Lower Mainland is densely populated with a large population, served by older systems with lower historical embedded costs and is stable in terms of total use with relatively low growth.

3.2 Please confirm that the above characteristics help to provide the Lower Mainland 'benefits of scale' as well as benefits of 'maturity' both of which contribute to lower rates and, all else being equal, a lower risk relative to competition than FEW and FEVI which do not have these characteristics.

**Response:**

It is confirmed that the above characteristics help provide the Lower Mainland with benefits of scale, contributing to lower rates, and all else equal, a lower level of competitive risk.

However, to clarify, the FEU have not categorized FEW or FEVI as immature utilities as discussed in the responses to BCUC IRs 1.86.1 and 1.86.2. As well, the FEU do not understand what is meant by the suggestion that the above characteristics help to provide the Lower Mainland with the benefits of maturity and cannot confirm the implication regarding the benefits of maturity.

3.3 Please confirm that amalgamation and the postage stamp rates for FEW and FEVI will substantially lower the rates for customers in these entities and will significantly improve the competitiveness of the service in their areas relative to competing fuel services, all else being equal.

**Response:**

While amalgamation and the implementation of postage stamp rates will lower the rates for customers in FEVI and FEW and improve the competitiveness of the service in their areas in respect of the price of natural gas relative to competing fuel services, the price differential between natural gas and competing fuel services is only one of many factors that influence competitiveness. As indicated in Sections 4.1 and 6.8 of the Application, customer energy choices and usage are informed by many factors such as capital cost investments, type of housing built, government policy and perceptions of the green attributes of energy sources, in addition to operational costs (i.e. the price of the energy source).

3.4 Please confirm that the impact of adding the FEW and FEVI customers and rate bases to the FEI customers and rate bases under postage stamp rates will make relatively much less substantial and less significant increases in rates for the Lower Mainland customers and make a much less significant change in the competitiveness of the services relative to competing fuels, all else being equal.

**Response:**

The impact of adding the FEW and FEVI customers and rate bases to the FEI customers and rate bases under postage stamp rates will make relatively less substantial and less significant increases in rates for the Lower Mainland customers and will make a less significant change in the competitiveness with respect to price of natural gas compared to competing energy forms, all else equal. However, the price differential between natural gas and competing fuel services is only one of many factors that influence competitiveness as discussed in CEC IR 2.3.3.

**4. Exhibit B-7, CEC 1.4.3**

> There are minor differences between the gas supply portfolios, as well as the gas cost allocation and recovery methodologies, in place for the various FEU entities / service areas; however, the main driver of the variance in the cost of gas is the amount and cost of fixed price swaps in place for FEVI versus FEI pursuant to previously approved Price Risk Management Plans.
>
> Based on differences in the price risk management strategies and plans implemented for the various FEU entities / service areas, a higher percentage of the commodity volumes for 2013 have been hedged within the FEVI portfolio while the FEI commodity portfolio contains relatively less hedging in 2013. Further, FEI hedging was implemented when market prices were lower.

4.1 Please confirm that the FEVI reasoning for asking for the longer term hedges was because the company had unique competitive challenges and by this the FEVI meant that its prices relative to competing fuel choices were approaching being non-competitive increasing problems acquiring new customers and retaining existing customers.

**Response:**

The request for longer term hedges that FEVI sought in its 2009-2014 Price Risk Management Plan was approved by the Commission per Letter No. L-36-09, dated June 8, 2009, and Letter No. L-45-09, dated June 11, 2009. As part of the approvals, the Commission recognized that FEVI was unique in that the royalty revenue arrangement between FEVI and the Province of British Columbia provided a natural hedge on approximately half of FEVI's annual core load requirements, and that this royalty revenue arrangement was scheduled to expire at the end of 2011. The primary reason for requesting the longer term hedges was to mitigate a future increase from the loss of royalty revenue that would have been exacerbated in a higher gas cost environment.

4.2 Please confirm that FEI did not seek such long term hedges because the company did not have the same unique competitive challenges that FEVI had.

**Response:**

Confirmed.

4.3 Please confirm that, all else being equal, had FEVI been amalgamated in 2009 and under a postage stamp rate there would not have been the same unique competitive challenges for customers on Vancouver Island and that the hedging decisions to manage perceived price risk for the amalgamated entity would most likely have been the same as the FEI decisions.

**Response:**

Confirmed.

**5. Exhibit B-7, CEC 1.5.1 & Exhibit B-3, Page 220**

If amalgamation and postage stamp rates are not approved, then the FEU will be considering individual rate design applications for each utility, which will consider the merits of rebalancing the rates for FEI, FEFN, FEVI and FEW. One of the outcomes of the proposed postage stamp rates is that the rates fall within an appropriate range of reasonableness, and therefore, no rate rebalancing is required.

**Table 9-10: Amalgamated Entity Rate Class Revenue to Cost Ratio**

| Rate Schedule | Revenue to Cost Ratio |
|---|---|
| Rate 1 – Residential | 93.4% |
| Rate 2 – Small Commercial (<2000 GJ/yr) | 104.6% |
| Rate 6 – Natural Gas Vehicle | 112.7% |
| Rate 3 & 23 Combined | 107.9% |
| Rate 5 & 25 Combined | 110.4% |

5.1 When applying postage stamp rates across regions do the FEU believe that there is an appropriate range of reasonableness and therefore no further equality of rates would be necessary if the regional rates are within a range of reasonableness or do the FEU believe that postage stamp rates across regions should not have a range of reasonableness and that the appropriate concept is equality of rates across regions.

**Response:**

The FEU interpret the question to read as follows:

*"When applying postage stamp rates across regions, do the FEU believe that there is an appropriate range of reasonableness and therefore no further rate re-balancing would be necessary if the rates are within a range of reasonableness or do the FEU believe that postage stamp rates across regions should not have a range of reasonableness and that the appropriate concept is equality of rates across regions"*

This response also addresses the response to CEC IR 2.5.2.

The FEU believe in equality of rates across regions and believe this is addressed by charging similar rates for similar services across all service areas. Under this rate proposal, all customers within a rate class are treated the same regardless of the region in which they live. To achieve this, the FEU believe there is an appropriate range of reasonableness in the evaluation of rate class revenue levels. As indicated in response to BCUC IR 1.74.1 and section 9.7.1 of the Application, a range of reasonableness is necessary to determine at which point rate re-balancing is necessary, as determined by whether the revenue-to-cost ratios fall within or outside of a prescribed range of reasonableness. Even if all of the rate classes fall within the range of reasonableness, it could be that further re-balancing may be necessary in light of rate class characteristics and rate design objectives. Moreover, as indicated in the response to BCUC IR 1.74.3, there are some circumstances where rate re-balancing may not be appropriate, such as when it is very close to the range of reasonableness, when it creates significant rate increases, when the COSA does not adequately measure the costs for a particular class, or when expected changes to costs in the near future would bring the class within the range of reasonableness.

Consistent with past precedents, the FEU believe the appropriate range of reasonableness for natural gas utilities is 90% to 110%.[1] As indicated in response to CEC IR 1.5.1, the outcome of the proposed postage stamp rates is that the rates fall within the current range of reasonableness, and therefore no rate rebalancing is required at this time.

5.2 Please discuss the FEU views on the range of reasonableness in regard to the revenue to cost ratios for rate classes.

**Response:**

Please refer to response CEC IR 2.5.1

5.3 Please discuss why equality of rates for rate classes across revenue to cost ratios should not be used as the standard of fairness.

**Response:**

The FEU interpret the question to ask:

[1] Refer to the response to BCUC IR 1.74.1 and Section 9.7.1 of the Application for the policy considerations that support the 90% to 110% Range of Reasonableness

'*Please discuss why 100% revenue to cost ratios (Unity) for each rate class should not be used as the standard of fairness*?'

Achieving unity implies a level of precision that does not exist with any COSA Study. As such, a range of reasonableness is necessary to determine the economic efficiency and fairness of rates. Please see the responses to BCUC IRs 1.74.1 and 1.74.2, Section 9.7.1 of the Application and the response to CEC IR 2.6.1 for further discussion.

5.4 Please provide historical revenue to cost ratios in graphical form for each of the rate schedules for each of FEI and FEVI over 10 years and for FEW since the introduction of natural gas service.

**<u>Response:</u>**

***FEI:***

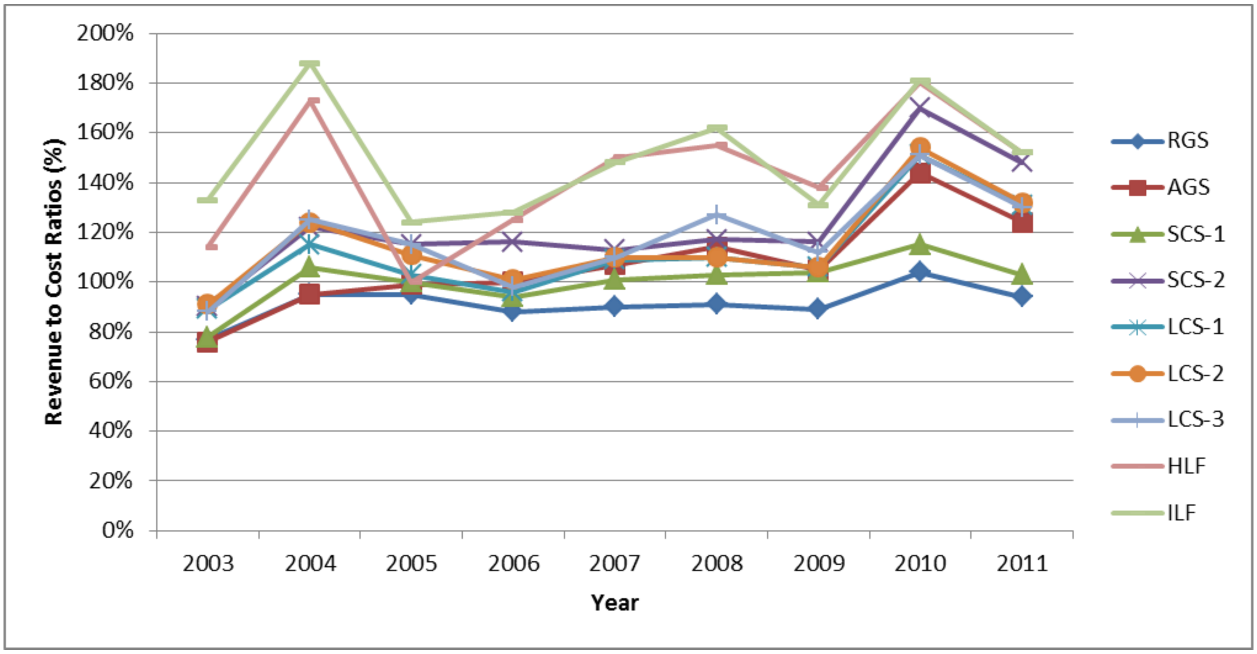
For FEI, a COSA and revenue to cost ratios were last prepared and presented in Tab 4 Page 9 of its 2001 Rate Design Application and are included in the table below:

| Rate Schedule | Revenue to Cost Ratio (2001) |
|---|---|
| Rate 1 - Residential | 96.5% |
| Rate 2 – Small Commercial (<2000 GJ/yr) | 101.5% |
| Rate 6 – Natural Gas Vehicle | 101.0% |
| Rate 3 – Large Commercial (>2000 GJ/yr) | 105.1% |
| Rate 5 – General Service | 102.1% |

***FEVI:***

For FEVI, historical revenue to cost ratios are included in the table and plotted in the chart below. From 2003 through 2009 FEVI rates were set relative to the competitive energy alternative under the Soft Cap Mechanism, and in 2010 to 2011 the rates were frozen. Since FEVI was not under a true cost of service rate setting mechanism in any of the years shown, the revenue to cost ratios should not be analyzed for rate setting/rebalancing purposes.

| Rate Schedule | FEVI Revenue to Cost Ratios by Year | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 |
| *RGS* | 77% | 95% | 95% | 88% | 90% | 91% | 89% | 104% | 94% |
| *AGS* | 76% | 95% | 99% | 100% | 107% | 114% | 105% | 144% | 124% |
| *SCS-1* | 78% | 106% | 100% | 94% | 101% | 103% | 104% | 115% | 103% |
| *SCS-2* | 90% | 122% | 115% | 116% | 113% | 117% | 116% | 170% | 148% |
| *LCS-1* | 89% | 115% | 103% | 96% | 109% | 110% | 106% | 151% | 131% |
| *LCS-2* | 91% | 124% | 111% | 101% | 110% | 110% | 106% | 154% | 132% |
| *LCS-3* | 88% | 125% | 115% | 98% | 110% | 127% | 112% | 151% | 130% |
| *HLF* | 114% | 173% | 100% | 125% | 150% | 155% | 138% | 180% | 152% |
| *ILF* | 133% | 188% | 124% | 128% | 148% | 162% | 131% | 181% | 152% |




1. 2003 Data - 2002 Centra Gas Rate Design Application, Proposed Rates Under Soft Cap Mechanism, Table 4.1
2. 2004 Data - TGVI 2003-2005 Settlement Agreement 2003 Annual Review Nov 2003, Table 2: Present Revenues to Cost
3. 2005 Data - TGVI 2003-2005 Settlement Agreement 2004 Annual Review, Nov 19 2004, Table 2: Present Revenues to Cost
4. 2006 Data - Terasen Gas (Vancouver Island) Inc., 2006 -2007 Revenue Requirement Extension NSP Nov-07 rev, Schedule 33C and D
5. 2007 Data - TGVI 2006-2007 Revenue Requirements Application, 2006 Negotiated Settlement Update, Schedule 33L
6. 2008 Data - TGVI 2007 Settlement Update 2008 Revenue Requirements, Table 2: Present Revenue to Cost (2008), Schedule 33K-08
7. 2009 Data - TGVI 2008 Settlement Update Revised Application, Table 2: Present Revenue to Cost (2009), Schedule 33K-09 & 33L-09
8. 2010 and 2011 Data - 2010 and 2011 revenue to cost ratios based on Proposed Rates from TGVI 2010-2011 Revenue Requirements and Rate Design Application (July 23 Amendment, Table K-8-2)

***FEW***

For FEW, the current Application is the first time a COSA and revenue to cost ratios have been prepared and filed with the Commission. Therefore, there is no historical information available on revenue to cost ratios of all rate classes since the introduction of natural gas service to FEW. However, all rate classes in the FEW have one rate schedule, which is based on the cost to serve all customers in FEW, which means that the revenue to cost ratio for that one rate is 100%.

**6. Exhibit B-7, CEC 1.5.2 & Exhibit B-1, Page 151**

The FEU have discussed the appropriate range of reasonableness in Section 9 of the Application in the context of the R:C ratios for the proposed postage stamp rates.

Ideally, the revenue to cost ratio should equal one for each rate class, indicating that the rates charged are in fact economically efficient and fair since the revenues recovered from each rate class would exactly equal the indicated cost to serve them. However, achieving unity implies a level of precision that does not exist with any COSA. As a cost of service study necessarily involves assumptions, estimates, simplifications, judgements and generalizations, a "range of reasonableness" is warranted when evaluating the appropriateness of the revenue to cost ratios.

6.1 Please confirm that the 'ideal' fairness principle is that when bundling costs the equality of rates across the grouping would be appropriate.

**Response:**

The FEU interpret this question to be regarding the fairness of the rates across an entity as measured by the revenue to cost ratios for each of the rate classes within the entity.

With respect to the Cost of Service Allocation studies ("COSA"), the 'ideal' outcome that is the most economically efficient and fair in principle occurs when the revenue to cost ratio equals one since the revenues recovered from each rate class would exactly equal the indicated cost to serve them. However, as indicated in response to BCUC IRs 1.74.1 and 1.74.2, and Section 9.7.1 of the Application, such precision is not possible due to the necessary assumptions, etc. involved in carrying out a COSA study. As such, a range of reasonableness is necessary to determine the economic efficiency and fairness of rates, as determined by whether the Revenue to Cost ratios fall within or outside of a prescribed range of reasonableness. Please refer to the response to CEC IR 2.5.1 for further discussion related to the Range of Reasonableness.

6.2 Please confirm that preparing the costs for individual regions or even the corporate entities providing services in those regions involves using assumptions, estimates, simplifications, judgments and generalizations.

**Response:**

Confirmed.

6.3 Please confirm that when the FEU prepare the cost accounting for FEVI, FEW and FEI that they use their best efforts to ensure that the costs allocated to those entities fairly represent the real costs.

**<u>Response:</u>**

In preparing the revenue requirements for FEVI, FEW and FEI, including any allocations required, the FEU believe that the results fairly represent the real costs for FEVI, FEW and FEI. Costs include those that are directly identified as well as allocated costs such as shared services which are based on approved costs and appropriate allocation methodologies.

6.4 Please confirm that when the FEU prepare a COSA study they use their best efforts to ensure that the allocation of costs and revenues to the rate classes fairly represents the real costs and revenues.

**<u>Response:</u>**

The FEU believe that when preparing a COSA study that the allocated costs fairly represent the real costs by customer class. However, because many of the costs are allocated on the basis of peak demand, which is not metered for every customer class, there is an inherent amount of uncertainty in the results (as with any COSA study). The FEU have prepared a COSA study, which is based on FEI's thoroughly reviewed COSA study and methodologies approved by the BCUC. Also, the COSA study has been reviewed by an expert third party who is satisfied with the allocation approaches used by the FEU.

**7. Exhibit B-7, CEC 1.6.1**

> The FEU, as prudent utility operators, look for ways to reduce costs and therefore rates to customers. The FEU are currently considering productivity improvements. Additionally,
>
> customers can take advantage of EEC programs that while not reducing rates, can have the effect of reducing consumption of individual customers and therefore the customer's bill.

7.1 Please confirm that the FEU are not taking any greater measures to mitigate FEI & FN customer bill impacts as a consequence of amalgamation and postage stamp rates than they would have taken without imposing the extra costs on the FEI customers.

**Response:**

The FEU's proposed postage stamp rates are consistent with rate design principles and fairly allocated costs in accordance with a cost of service study as described in section 9 of the Application. The FEU therefore do not agree with the characterization in the question that it is "imposing extra costs on the FEI customers".

In addition to the measures described in the response to CEC IR 1.6.1, the FEU have proposed the phasing in of the bill impacts to FEI and Fort Nelson customers. The FEU are not aware of other mitigation efforts that it could utilize in addition to a phase-in proposal and the measures referred to in response to CEC IR 1.6.1, including the FEU's efforts to increase throughput through programs such as Natural Gas for Transportation, its efforts to seek productivity improvements, and the expansion of its EEC programs to all customers. One particular benefit of the common rates and amalgamation proposal is the efficient facilitation of the extension of service offerings such as NGT to all of the FEU's service areas that will over time assist in increasing volume in the system that in turn may result in a favourable impact to rates, e.g., a rate decrease or no increase. There are also EEC programs in place today that are available to customers who wish to take advantage of them. These programs will continue to be available post-amalgamation and may be supported by new programs over time.

7.2 Please confirm that the FEU could take additional measures and or is not constrained from taking additional measures to mitigate FEI & FN customer bills and could ask the Commission to approve such mitigation efforts.

**Response:**

The FEU are not currently aware of other meaningful measures it could take at this time that could mitigate the impact to FEI and FEFN customer bills, other than variations on its proposal to phase-in bill impacts and its efforts to increase throughput through programs such as Natural Gas for Transportation, its efforts to seek productivity improvements, and the expansion of its EEC programs to all customers. One such variation on the proposed bill impact phase-ins is to phase-in the rate decreases to FEVI and FEW over a defined period. While the FEU would not be constrained from applying for Commission approval to phase-in bill impacts in this manner, the FEU believe that its 3-year and 15-year phase-in proposals for FEI and FEN customers, respectively, represent a reasonable balance of impacts to customer bills for all of the FEU.

**8. Exhibit B-7, CEC 1.6.2 & BCUC 1.2.3**

- Under a 2% per year convergence proposal, typical FEI residential and commercial customers would reach the common rate by 2016[2] at the latest. The FEU are proposing to mitigate the rate increase to all FEI customers via a 3 year phase-in, with customers realizing the impact of common rates in 2017. Therefore, with an additional year before the common rate is achieved, the FEU believe that their proposal is more beneficial to FEI customers than a 2% per year convergence proposal.

8.1 Please confirm that the FEI proposed phase-in is not for the whole amalgamation and postage stamping of costs but refers only to one component of the impact.

**Response:**

Not confirmed. The FEU proposed phase-in is described in Section 8.4.1.2 of the Application and involves allocating a portion of the RSDA balance to mitigate the Mainland rate increases that occur upon amalgamation and the implementation of postage stamp rates. The proposal involves the use of a delivery rate rider to stream the allocation of the RSDA to Mainland customers, in effect providing an offsetting reduction to all impacts of amalgamation and the implementation of postage stamp rates. To clarify, the FEU have not segregated a single component of the impact to be offset by the allocation of the RSDA to Mainland customers.

- Finally, it is beneficial to customers in the FEVI and FEW service areas to move to common rates upon amalgamation. As FEVI and FEW customers will receive a rate decrease upon the implementation of common rates, there is no negative consequence to these customers in realizing the common rate immediately and therefore no need for a phase-in approach.

8.2 Please confirm that because the FEVI and FEW receive their benefits immediately the costs for which they are being relieved fall to the FEI customers.

**Response:**

As set out in the Application, the proposal by the FEU is for a common rate design that will see a sharing of the combined costs of the FEU and the recovery of those costs from the amalgamated entity's customer classes. As a result, customers in the current FEVI and FEW service areas will see lower rates compared to existing standalone rates upon implementation, while customers in the existing FEI and FEFN service areas will see higher rates in comparison to existing standalone rates. In order to mitigate the increase in rates for FEI and FEFN customers, the FEU are proposing to phase-in the amalgamated entity's rates over 3 and 15 years, respectively.

**9. Exhibit B-7, CEC 1.7.1**

> The main rationale for amalgamation and common rates is one of fairness amongst all of the FEU's customers. Under common rates, all customers within a rate class would pay the same rate, regardless of location within its service areas. This Application proposes to extend the common rates already realized by the majority of the FEU's customers across the Province, including those customers located in the FEW and FEVI service areas. Increasing customer base and retention of customers in FEVI and FEW service areas will be a benefit of introducing common rates via amalgamation as described in Section 6 of the Application.

9.1 Please confirm that the benefit of amalgamation and common rates for FEW and FEVI in increasing customer base and retention of customers will reduce the risks from competition in those areas.

**<u>Response:</u>**

The benefit of amalgamation and common rates for FEW and FEVI will improve the competitive position with respect to price of natural gas compared to competing energy forms, all else equal. However, as indicated in Sections 4.1 and 6.8 of the Application, other factors that influence customer energy choices and usage in addition to the price of the energy source, include government policy, upfront capital cost investment, type of housing built, government policy and perceptions of the green attributes of energy sources. As such, the risks of competition in terms of customer attraction and retention (i.e. energy use per customer and capture rates for new and existing customers) in those areas will still remain.

## 10. Exhibit B-7, CEC 1.8.1

> There are a number of factors that impact business risk associated with smaller utilities, and reliance on large customers is one factor.

10.1 Please describe the other factors that impact business risk with smaller utilities.

**Response:**

A small utility does not have the opportunities to diversify its risks to the same extent as a larger utility. Negative events are likely to have a greater impact on the earnings or viability of a small company. For example, assets are typically more concentrated in a limited geographic area, which limits operational flexibility. Small utilities also typically have fewer customers from which to recover their invested capital. Even for a small utility with the same customer base in terms of proportions of residential, commercial and industrial customers as a large utility, the loss of a single customer within a customer class could have a greater impact on a small utility. Further, a small utility has a limited service area, which means that it would not have the same ability to offset a secular decline in growth prospects with higher economic growth elsewhere as would a larger utility with a more economically diverse service area.

Smaller utilities have fewer financing options and less institutional interest in acquiring their debt securities. The issued debt of smaller utilities would be relatively illiquid, and, if issued to third-parties, would likely require stricter covenants than debt issued by large utilities.

Debt rating agencies often take size into account when rating companies and their debt issues. The impact of smaller size for rated utilities is frequently exhibited in lower debt ratings for these companies even in cases where their financial parameters are stronger than their larger peers.

Regulators have recognized small size as a factor in establishing capital structures and ROEs for utilities. The Alberta Utilities Commission (AUC) stated in its 2011 Generic Cost of Capital, Decision 2011-47 (December 8, 2011) page 43, "Due to its small size, AltaGas is more risky than ATCO Gas." As a result, the AUC set the deemed common equity ratio for AltaGas Utilities at 43% compared to ATCO Gas' 39%. The Régie de l'énergie (Régie) considers Gazifère Inc. to be of above average risk in particular due to its small size and competition with electricity in Québec. The Régie adopted an equity risk premium for Gazifère of 0.25% to 0.50% above that applicable to a benchmark distributor on a common equity ratio of 40%.[2]

[2] Régie de l'énergie, *Decision: Demande relative au renouvellement du mécanisme incitatif, à la fermeture réglementaire des livres pour la période du 1er janvier 2009 au 31 décembre 2009, à l'approbation du plan d'approvisionnement pour l'exercice 2011 et à la modification des tarifs de Gazifère Inc. à compter du 1er janvier 2011*, D-2010-147, November 26, 2010.

## 11. Exhibit B-7, CEC 1.15.1

This Application proposes to extend the common rates already realized by the majority of the FEU's customers across the province, including to those customers located in the FEW and FEVI service areas. Increasing customer base and retention of customers in FEVI and FEW service areas will be a likely benefit of introducing common rates; however this alone does not reduce the risk of post amalgamation FEI, as there are a number of risk factors, other than cost, that impact competitiveness of the FEU.

11.1 Please confirm that while increasing customer base and retention of customers in FEVI and FEW does not alone reduce risk of post amalgamation FEI this benefit of amalgamation does contribute to reducing the risk of post amalgamation FEI.

**Response:**

This cannot be confirmed. Please refer to the response to BCUC IR 1.70.1.

**12. Exhibit, B-7, CEC 1.16.1**

4. Harmonization of rates with amalgamation will improve the competitive pricing position of the former FEVI and FEW service areas versus electricity, but will modestly weaken the competitive position of the Mainland service area. The slightly higher post-

amalgamation price competitive risks of FEI Amalco indicate, directionally, a higher post-amalgamation cost of capital for FEI Amalco.

12.1 Please confirm that, all else being equal, the closer the price customers pay is to the price point at which customers cannot be attracted and existing customers leave the greater the incremental risk addition. Put another way the last increment of price increase before the threshold for competitive loss of customers and failure to attract customers represents a greater addition of risk than the same increment of price increase from a point of 100 units below the threshold.

**Response:**

All else being equal, confirmed. However, as stated in response to BCUC IR 1.58.2, "it is important to recognize that competitiveness relates to broader considerations than operating costs. As discussed in the Application, customers' energy choices and usage are informed by capital cost investment, type of housing being built, government policy, and perceptions about the green attributes of the energy source". In many cases the choice of energy source is made by a developer or builder, not the ultimate customer who will be using the energy source. The developer or builder is more likely to choose the energy source whose installation cost is lowest, in order to maximize his or her returns, rather than the energy source whose operating costs would be lowest for the ultimate end user.

**13. Exhibit B-9, BCUC 1.70.1**

| Risk unique to FEVI (as compared with FEI) (Exhibit B-3, Appendix C-2, p. 14) | Is the risk eliminated as a result of amalgamation? Yes / No; please explain your response | Is the risk mitigated (reduced) as a result of amalgamation? Yes / No; please explain your response |
|---|---|---|
| As a maturing utility, higher price-related competitive risks against alternative energy sources, increasing with the loss of royalty revenues | No, the risk associated with the loss of royalty revenues is not eliminated, as the amalgamated utility will continue to face competitive risks (in terms of price, market share, and customer preference) against alternative energy sources and will have additional exposure to a maturing market. | Yes, the risk associated with the loss of royalty revenues is reduced in the Vancouver Island service area given that common rates will improve the price competitiveness in that area. However, the amalgamated utility would face marginally higher competitive risks (in terms of price, market share, and customer preference) against alternative energy sources due to the slight decrease in the Mainland service area's price advantage. |

13.1 Please confirm that while the risk is not eliminated the impact of the risk when contained in a high priced location relative to competitive fuels is much more likely to cause losses than when the risk is contained in a large pool location with lower prices relative to the competitive fuels.

**Response:**

The FEU agree that, from a strictly price competitiveness perspective, the risk of losing customers (or failure to gain new customers) is lower when the cost (and thus price) of the service is lower.

| Risk unique to FEVI (as compared with FEI) (Exhibit B-3, Appendix C-2, p. 14) | Is the risk eliminated as a result of amalgamation? Yes / No; please explain your response | Is the risk mitigated (reduced) as a result of amalgamation? Yes / No; please explain your response |
|---|---|---|
| A less diverse economic and customer base, with material reliance on two major industrial customers | No, the risk is not eliminated. Pre-amalgamation FEI has a large, diverse customer base, but with exposure to industrial margin. Amalgamation of FEVI transfers risk associated with exposure to the two major industrial customers in the Vancouver Island service area to FEI Amalco, resulting in marginally higher exposure for FEI Amalco compared to pre-amalgamation. | See column to the left. |

13.2 Please confirm that while the risk is not eliminated the impact of the risk contained in a small high priced location relative to the competition fuels is much more likely to lead to losses than if the risk is contained in a large pool lower priced location relative to the competition fuels.

**Response:**

Not confirmed. The size of the location in this context is irrelevant as regards the risk of losing the customers to competitive fuels. Please refer to the response to CEC IR 2.13.1 with regard to the impact of the relative price.

**14. Exhibit B-9, BCUC 1.24.2**

| Phase In Analysis Scenarios | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|---|---|---|---|---|---|---|
| **FEI** | | | | | | |
| FEI - No Phase In | 5.3% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| FEI - 3 Year Phase In | 3.6% | 4.1% | 4.7% | 5.3% | 0.0% | 0.0% |
| FEI - 5 Year Phase In | 3.4% | 3.8% | 4.1% | 4.5% | 4.9% | 5.3% |
| **FEVI** | | | | | | |
| FEVI - No Phase In | -25.5% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| FEVI - 3 Year Phase In | -9.6% | -14.9% | -20.2% | -25.5% | 0.0% | 0.0% |
| FEVI - 5 Year Phase In | -7.8% | -11.4% | -14.9% | -18.4% | -22.0% | -25.5% |
| **FEW** | | | | | | |
| FEW - No Phase In | -36.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| FEW - 3 Year Phase In | -5.2% | -15.4% | -25.7% | -36.0% | 0.0% | 0.0% |
| FEW - 5 Year Phase In | -1.8% | -8.6% | -15.4% | -22.3% | -29.1% | -36.0% |

*Exclusive of RSDA & MCRA Rider Impacts

14.1 Please explain why the 3 year phase-in does not start with an impact of 1/3 of the total change and why the 5 year phase-in does not start with an impact of 1/5 of the change.

**Response:**

The phase-in is calculated on a total deficiency or surplus basis and is then translated to a delivery rate rider for each region. As the delivery rate already reflects the common rate, this rider amount would be a credit on the bill for FEI customers (i.e. to reduce the bill) and a charge for FEVI and FEW customers (i.e. to increase the bill).

The three year phase-in approach passes on one fourth of the impact in the beginning year so that rates are phased-in over three years, achieving common rates at the start of the fourth year. Thus, in the case of the three year phase-in, the total amount added back in the first year for FEVI and FEW to determine the rider charge equates to ¾ of the total benefit. If the phase-in approach allocated one third in the beginning, it would result in the achievement of common rates at the start of the third year.

Similarly, the five year phase-in approach passes on one sixth of the impact in the beginning year so that rates are phased-in over a five year period, achieving common rates at the start of the sixth year.

The following example may provide additional clarity:

**Phase-In Example**

Vancouver Island

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| 1 | Residential Volume (TJ) | | 4,528 | | | | | | |
| 2 | Typical Use Rates (GJ per Year) | | 58.6 | | | | | | |
| 3 | Approx. Total FEVI Residential Benefit ($000s) | | 22,000 | | | | | | |
| 4 | Existing Annual Bill ($) | | 965 | | | | | | |
| 5 | RDA Annual Bill (No phase in) ($) | | **719** | | | | | | |
| 6 | | | | | | | | | |
| 7 | *Phase In Period (Years):* | *3* | | | | | | | |
| 8 | | | | **2013** | **2014** | **2015** | **2016** | | |
| 9 | Annual Phase In Amount | | | 16,500 | 11,000 | 5,500 | - | | |
| 10 | Residential Rate Rider Amounts | Line 9 / Line 1 | | 3.64 | 2.43 | 1.21 | - | | |
| 11 | Approximate Annual Bill Impact of Rider $ | Line 10 x Line 2 | | 214 | 142 | 71 | - | | |
| 12 | Approximate Annual Bill $ | Line 5 + Line 11 | | 933 | 862 | 791 | **719** | | |
| 13 | Approximate Annual Bill Decrease % | | | -3% | -11% | -18% | -25% | | |
| 14 | | | | | | | | | |
| 15 | *Phase In Period (Years):* | *5* | | | | | | | |
| 16 | | | | **2013** | **2014** | **2015** | **2016** | **2017** | **2018** |
| 17 | Annual Phase In Amount | | | 18,333 | 14,667 | 11,000 | 7,333 | 3,667 | - |
| 18 | Residential Rate Rider Amounts | Line 17 / Line 1 | | 4.05 | 3.24 | 2.43 | 1.62 | 0.81 | - |
| 19 | Approximate Annual Bill Impact of Rider $ | Line 18 x Line 2 | | 237 | 190 | 142 | 95 | 47 | - |
| 20 | Approximate Annual Bill $ | Line 5 + Line 19 | | 957 | 909 | 862 | 814 | 767 | **719** |
| 21 | Approximate Annual Bill Decrease % | | | -1% | -6% | -11% | -16% | -21% | -25% |

14.2 Please provide the assumption used with regard to the repayment of the government $25 million loan.

**Response:**

Consistent with the Application, this analysis assumes that the government loan is repaid according to the current schedule. Please refer to the response to BCUC IR 1.20.1 for a discussion of the repayment of the government loan.

14.3 Please confirm that the note exclusive of RSDA means that the balance therein was not used in running this analysis.

**Response:**

Confirmed, please refer to the response to CEC IR 2.14.7 for a discussion on the treatment of the RSDA.

14.4 Please provide a modeling and the appropriate assumptions that would go with it showing a 3 year phase-in progressing at 1/3 of 5.3% per year for FEI and the matching changes for FEVI & FEW progressing at the same rate. Please do the same for the 5 year phase in at 1/5 of the 5.3% per year for FEI and the matching changes for FEVI and FEW.

**Response:**

Please refer to the response to BCUC IR 2.57.2.2 where the FEU have expanded its Residential phase-in analysis from the analysis shown in the response to BCUC IR 1.24.2. The analysis now includes all rate schedules and this expansion results in a more uniform transition to common rates for all FEI customers, over both the three and five year periods. The FEU believe that this revised analysis accomplishes the same goal as the scenario requested in the question preamble.

14.5 Please provide a 7 year phase-in done on the same basis as the request above in 14.4.

**Response:**

Please refer to the responses to CEC IR 2.14.4 and BCUC IR 2.57.2.2.

The FEU have updated the analysis from the response to BCUC IR 2.57.2.2 to reflect a seven year phase-in as shown below:

| FEI- Seven Year Phase-In | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|---|---|---|---|---|---|---|---|---|
| Lower Mainland | | | | | | | | |
| Rate 1 - Residential | 0.9% | 1.5% | 2.1% | 2.8% | 3.4% | 4.0% | 4.7% | 5.3% |
| Rate 2 - Small Commercial | 0.1% | 0.6% | 1.1% | 1.7% | 2.2% | 2.8% | 3.3% | 3.8% |
| Rate 3 - Large Commercial | 0.8% | 1.3% | 1.7% | 2.2% | 2.7% | 3.2% | 3.6% | 4.1% |
| Rate 4 - Seasonal | 3.9% | 4.2% | 4.5% | 4.8% | 5.2% | 5.5% | 5.8% | 6.2% |
| Rate 5 - General Firm | 1.2% | 1.5% | 1.9% | 2.3% | 2.7% | 3.1% | 3.5% | 3.9% |
| Rate 6 - Natural Gas Vehicle | 0.8% | 1.5% | 2.1% | 2.7% | 3.3% | 4.0% | 4.6% | 5.2% |
| Rate 7 - General Interruptible Sales | 1.3% | 1.5% | 1.8% | 2.0% | 2.2% | 2.5% | 2.7% | 3.0% |
| Rate 22 - Large Volume Transportation (Non-bypass) | 4.8% | 6.2% | 7.6% | 8.9% | 10.3% | 11.7% | 13.1% | 14.5% |
| Rate 23 - Commercial Transportation | 0.2% | 1.4% | 2.6% | 3.8% | 5.0% | 6.3% | 7.5% | 8.7% |
| Rate 25 - General Firm Transportation (Non-bypass)[1] | -0.6% | 0.6% | 1.9% | 3.2% | 4.5% | 5.8% | 7.1% | 8.4% |
| Rate 27 - General Interruptible Transportation | 0.7% | 2.0% | 3.3% | 4.5% | 5.8% | 7.0% | 8.3% | 9.5% |
| Inland | | | | | | | | |
| Rate 1 - Residential | 1.2% | 1.8% | 2.4% | 3.0% | 3.6% | 4.2% | 4.8% | 5.5% |
| Rate 2 - Small Commercial | 0.4% | 1.0% | 1.5% | 2.0% | 2.5% | 3.1% | 3.6% | 4.1% |
| Rate 3 - Large Commercial | 1.1% | 1.6% | 2.1% | 2.6% | 3.0% | 3.5% | 4.0% | 4.5% |
| Rate 4 - Seasonal | 4.4% | 4.8% | 5.1% | 5.4% | 5.8% | 6.1% | 6.5% | 6.8% |
| Rate 5 - General Firm | 1.6% | 2.0% | 2.4% | 2.8% | 3.2% | 3.6% | 4.0% | 4.4% |
| Rate 6 - Natural Gas Vehicle | 1.0% | 1.7% | 2.3% | 2.9% | 3.6% | 4.2% | 4.9% | 5.5% |
| Rate 7 - General Interruptible Sales | 1.4% | 1.6% | 1.8% | 2.0% | 2.2% | 2.4% | 2.6% | 2.8% |
| Rate 23 - Commercial Transportation | 0.2% | 1.5% | 2.7% | 3.9% | 5.2% | 6.4% | 7.6% | 8.9% |
| Rate 25 - General Firm Transportation (Non-bypass)[1] | -0.6% | 0.8% | 2.3% | 3.7% | 5.1% | 6.5% | 7.9% | 9.3% |
| Rate 27 - General Interruptible Transportation | 0.7% | 2.0% | 3.2% | 4.4% | 5.7% | 6.9% | 8.1% | 9.4% |
| Columbia | | | | | | | | |
| Rate 1 - Residential | 0.8% | 1.4% | 2.0% | 2.6% | 3.2% | 3.9% | 4.5% | 5.1% |
| Rate 2 - Small Commercial | 0.0% | 0.5% | 1.1% | 1.6% | 2.1% | 2.7% | 3.2% | 3.8% |
| Rate 3 - Large Commercial | 0.7% | 1.1% | 1.6% | 2.1% | 2.6% | 3.1% | 3.5% | 4.0% |
| Rate 5 - General Firm | 1.0% | 1.4% | 1.7% | 2.1% | 2.5% | 2.9% | 3.3% | 3.7% |
| Rate 23 - Commercial Transportation | 0.2% | 1.4% | 2.6% | 3.9% | 5.1% | 6.3% | 7.5% | 8.7% |
| Rate 25 - General Firm Transportation (Non-bypass) | 0.2% | 1.5% | 2.8% | 4.0% | 5.3% | 6.6% | 7.8% | 9.1% |
| Rate 27 - General Interruptible Transportation | 0.4% | 1.1% | 1.7% | 2.4% | 3.1% | 3.7% | 4.4% | 5.1% |

*Exclusive of RSDA & MCRA Rider Impacts

[1] Minor decrease in year one due to rate rider set on a weighted average basis with RS 3

| FEVI- Seven Year Phase-In | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Rate 1 - Residential | 0.0% | -3.3% | -7.0% | -10.7% | -14.4% | -18.1% | -21.8% | -25.5% |
| Rate 2 - Small Commercial | | | | | | | | |
| Rate 2 - AGS[1] | 9.7% | 4.2% | -1.2% | -6.6% | -12.1% | -17.5% | -22.9% | -28.4% |
| Rate 2 - SCS1 | -4.3% | -8.2% | -12.0% | -15.8% | -19.7% | -23.5% | -27.3% | -31.2% |
| Rate 2 - SCS2 | -16.5% | -20.4% | -24.4% | -28.4% | -32.4% | -36.4% | -40.4% | -44.3% |
| Rate 2 - LCS1[1] | 0.3% | -4.7% | -9.7% | -14.7% | -19.7% | -24.6% | -29.6% | -34.6% |
| Rate 3 - Large Commercial | | | | | | | | |
| Rate 3 - AGS | -6.4% | -10.0% | -13.7% | -17.3% | -20.9% | -24.6% | -28.2% | -31.8% |
| Rate 3 - LCS2 | -6.5% | -10.1% | -13.6% | -17.2% | -20.7% | -24.3% | -27.8% | -31.4% |
| Rate 3 - LCS3 | -6.3% | -10.0% | -13.8% | -17.5% | -21.2% | -25.0% | -28.7% | -32.5% |
| Rate 3 - HLF[1] | 28.0% | 23.0% | 17.9% | 12.8% | 7.7% | 2.6% | -2.5% | -7.6% |
| Rate 3 - ILF[1] | 10.2% | 5.8% | 1.5% | -2.9% | -7.3% | -11.6% | -16.0% | -20.4% |

*Exclusive of RSDA & MCRA Rider Impacts

[1] Increase due to rate rider set on a weighted average basis with all other FEVI customers within rate schedule

| FEW- Seven Year Phase-In | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Rate 1 - Residential | -0.1% | -5.2% | -10.3% | -15.4% | -20.6% | -25.7% | -30.8% | -36.0% |
| Rate 2 - Small Commercial | | | | | | | | |
| Rate 2 - Commercial[1] | 0.7% | -5.3% | -11.3% | -17.4% | -23.4% | -29.4% | -35.4% | -41.4% |
| Rate 2 - LCS1 | -2.9% | -9.0% | -15.1% | -21.2% | -27.3% | -33.4% | -39.5% | -45.7% |
| Rate 3 - Large Commercial | | | | | | | | |
| Rate 3 - LCS2 | -4.2% | -10.5% | -16.9% | -23.2% | -29.5% | -35.9% | -42.2% | -48.6% |
| Rate 3 - LCS3 | -5.9% | -12.3% | -18.6% | -25.0% | -31.3% | -37.7% | -44.0% | -50.3% |

*Exclusive of RSDA & MCRA Rider Impacts

[1] Increase due to rate rider set on a weighted average basis with all other FEW customers within rate schedule

14.6 Please confirm that some alternative to the FEU proposal in the nature of this form of phase-in would be a viable option for the FEU with common rates and the phase in being managed through a phase-in rate rider.

**Response:**

Confirmed. As described in the response to BCUC IR 2.57.2.2, if an alternate phase-in approach to that recommended in the Application was pursued, the FEU believe that the approach as outlined in the response to BCUC IR 1.24.2 and further expanded on in the response to BCUC IR 2.57.2.2 provides a reasonable phase-in of the impacts of amalgamation and postage stamp rates while still achieving full cost recovery in each year.

14.7 Please discuss options for managing the RSDA balance within the context of one of these 'straight line' phase-in options.

**Response:**

The FEU interpret "managing the RSDA balance" to mean the disposition of the RSDA balance.

In the context of the two approaches that the FEU outlined in the response to BCUC IR 2.57.2.2, it would still be appropriate to return the RSDA to FEI Mainland and Fort Nelson customers as discussed in the Application. That is, a portion of the RSDA could be allocated to Fort Nelson customers to finance the phase-in of common rates for the Fort Nelson region with the remaining balance in the RSDA allocated to Mainland customers over a three year or five year period via a rate rider, beginning in 2014. Alternatively, the RSDA could be held in an account, accruing interest, for future disposition to Mainland customers once the approved phase-in was complete.

## 15. Exhibit B-9, BCUC 1.58.6

> The credit rating agencies will upgrade or downgrade the post-amalgamated FEI if there is a material change to FEI's business and financial risks that warrant a ratings change within their methodology. At this time, the FEU do not foresee a material change in business risks affecting the post-amalgamation FEI that is caused by the proposed amalgamation and common rates that would lead to a change in ratings. A material reduction in equity thickness and/or approved ROE could cause a downgrade; likewise an increase could prompt an upgrade. Please refer to the response to BCUC IR 1.58.5.

15.1 Do the FEU believe that if FEVI was separately rated by the credit rating agencies and it was to then face on its own the loss of the royalty credits and loan repayment requirements that this would be a sufficient relative change to the risks of the business that they would consider a down grade because this would be a 'material change'?

**Response:**

FEVI has been separately rated by both DBRS and Moody's for the last number of years. Both DBRS and Moody's are aware of the loss of royalty revenues for FEVI and the FEU believe that this issue is considered in the current credit rating provided by each agency.

The future impact of the loss of royalty revenues is expected to have a negative impact on the competitive position of FEVI and increase the risk profile of FEVI.

The rating agencies will consider whether the change in business risk will materially impact FEVI's credit metrics in a sufficient way to warrant a downgrade. The FEU are not in a position to determine what action may be taken by the rating agencies but believe the deterioration of the competitive position over time is a primary consideration that could lead to a ratings change.

See Exhibit B-9-1, Attachments to BCUC IR No. 1, Attachments 71.1.1 and 72.1.1 for ratings agency reports since 2008.

**16. Exhibit B-9, BCUC 1.67.7**

> The term "similar" in the context of "similar competitive pressures" means that the sources of the competitive pressures are similar, e.g., competition from electricity and other sources of energy, and the impacts of energy policy on customer preferences and choices. It does not follow that the degree to which those competitive pressures impact each utility is the same. All three of the utilities experience competition from similar alternative energy sources; however, the competitive risks are higher for FEVI and FEW than for FEI.

16.1 Please explain why the risks for FEVI and FEW are higher than for FEI.

**<u>Response:</u>**

FEVI faces higher competitive risks than FEI due to higher price-related competitive risks against alternative energy sources, increasing with the loss of royalty revenues, as stated in Ms. McShane's Opinion (Appendix C-2), page 14. FEW faces higher competitive risks than FEI versus electricity due to higher delivery costs and higher competitive risk from alternative renewable energy sources resulting from the service area's commitment to reducing reliance on fossil fuels and commitment to renewable energy initiatives, as stated in Ms. McShane's Opinion (Appendix C-2) on page 15. Please also refer to the response to BCUC IR 1.70.1, which discusses which other risks are higher for FEVI and FEW than FEI and why.

16.2 Please confirm as implied above that the risk is based on the exposure to the competition and the degree of impact on the utility of the competitive pressure.

**<u>Response:</u>**

Confirmed, with respect to price competition pressures. As indicated in the response to CEC IR 2.16.1, there are other risks specific to FEVI and FEW that are higher than FEI's; please refer to the response to BCUC IR 1.70.1.

16.3 Please confirm that the degree of impact on the utility of the competitive pressure will depend in part on how close the utilities costs and prices are to the threshold past which the competition degrades the ability of the utility to attract and retain customers.

**Response:**

Yes, in part. However, see the caveats expressed in the response to CEC IR 2.12.1.

## 17. Exhibit B-9, BCUC 1.85.2.1

The postage stamping of rates does not transfer risks to the ratepayer. The allocation of risk between the shareholder and ratepayer remains the same whether there are postage stamp rates or not.

As discussed in response to BCUC IR 1.70.1 amalgamation and postage stamp rates will mitigate certain business risks that are unique to stand alone FEVI and FEW, however there are no risks transferred between ratepayers and shareholders. While there will be some customers facing higher rates while other customers face lower rates as a result of postage stamping, over time all customers will see more stability in rates as a result of postage stamping over a broader number of customers.

17.1 Does the greater stability in rates for customers provide a lower risk relative to competing fuels with less stable rates?

**Response:**

Yes, all other things equal (e.g., competitive prices and a supportive market environment for the service).