

January 18, 2013

British Columbia Utilities Commission  
6<sup>th</sup> Floor, 900 Howe Street  
Vancouver, BC  
V6Z 2N3

Attention: Ms. Erica M. Hamilton, Commission Secretary

Dear Ms. Hamilton:

**Re: FortisBC Energy Inc. (“FEI”)**

**Biomethane Service Offering: Post Implementation Report and Application for Approval of the Continuation and Modification of the Biomethane Program on a Permanent Basis (the “Application”)**

**Application Changes Resulting from the AES Inquiry Report in Compliance with British Columbia Utilities Commission (the “Commission”) Order No. G-1-13**

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## **1. Introduction**

On December 19, 2012, FEI submitted an Application to the Commission which, among other things, sought a continuation of the Biomethane Program on a permanent basis, and constituted FEI’s Post Implementation Report (“PIR”) on the FEI Biomethane Pilot Program in compliance with Commission Order No. G-194-10.

On January 8, 2013, the Commission issued Order No. G-1-13 (the “Order”), establishing a Preliminary Regulatory Timetable for the review of the Application. Paragraph no. 5 of the Order directed FEI to make any adjustments to its proposals in the Application that may be required to take into account any relevant determinations made by the Commission in the AES Inquiry Report issued with Order No. G-201-12.

In compliance with paragraph no. 5 of the Order, below is a discussion of each of the relevant determinations made in the AES Inquiry Report. As discussed below, the determinations of the AES Inquiry Report are consistent with FEI’s Application. FEI does, however, address the form of regulation of third party upgraders and the CPCN threshold which were not canvassed in the Application.

## **2. Relevant Determinations of the AES Inquiry Report**

The relevant determinations of the AES Inquiry Report are discussed below, along with an explanation of how these determinations impact FEI's Application. Where required, FEI has provided additional information to address the determinations.

### **2.1 Biomethane Service**

#### **2.1.1 Need for Regulation and Business Structure**

The AES Inquiry Report found that the biomethane service is part of FEI's regulated service offering and within the natural gas class of service. It states (at p. 46):

**Biomethane Service can therefore best be viewed as another source of supply for the regulated utility. As such, it is part of FEU's regulated service offering.**

...

**Biomethane Service is appropriately considered a Separate Class of Customer within the natural gas class of service.**

These conclusions of the Commission Panel in the AES Inquiry are consistent with the approach taken by FEI in its 2010 Biomethane Application and its present Application. FEI's approach has been to contract for biomethane supply as part of FEU's regulated service offerings. The Commission has approved rate schedules, including Rates Schedules 1B, 2B and 3B, under which customers receive service. FEI is requesting the continuation of the rate schedules with some amendments, as described in section 3 of the Application.

#### **2.1.2 Cost Allocation**

The AES Inquiry Report states (at p. 47)

The Panel notes that detailed cost allocation decisions will require assessment of the specific facts in each situation and will be determined based on the evidence tendered at that time. The Panel recommends that such decisions should take into account the Principle and Guidelines on cost allocation set out in Section 2.4.

FEI has proposed a cost allocation approach in section 9 of the Application, which is consistent with the cost allocation approach approved for the two-year test period and consistent with FEI's general approach to cost allocation for service offerings within its traditional natural gas distribution class of service.

FEI's proposed cost allocation approach is consistent with the Principle and Guidelines set out in section 2.4 of the AES Inquiry Report. FEI's proposed cost allocation approach is consistent with the principle of cost causality as that principle has been applied to the customer choice program within FEI's traditional natural gas distribution class of service. As

with other services, costs related to making the service available to all customers are recovered from all customers. This is also appropriate as the benefits of lower GHG emissions from the use of biomethane and the realization of government policy flow to all customers. Further, if FEI does not develop biomethane supply projects, the projects will likely be developed as electrical supply projects, in which cases the costs will be borne by all BC Hydro customers, but with less benefits. (See sections 5.6 and 5.7 of the Application.) Consistent with the relevant guidelines in section 2.4 of the AES Inquiry Report, FEI's proposed cost allocation is transparent. A clear and concise description of the cost allocation approach is presented in section 9 of the Application.

## **2.2 Biomethane Upgrading Facilities and Extensions to Connect Facilities**

### **2.2.1 Need for and form of Regulation**

The AES Inquiry Report determined that biogas upgraders are regulated under the UCA, stating (at p. 47):

The Commission Panel is of the view that biogas upgraders are similar to provincial gas plants in function and are regulated under the UCA.

The AES Inquiry Report discusses the form of regulation of biomethane upgrading facilities and extensions to connect such facilities as follows (at p. 47):

The Commission Panel finds that neither biomethane upgraders nor the pipe connecting them to the traditional distribution utility are extensions of the utility system as contemplated in subsections 45(1) and (2) of the UCA. These pipes are a connection to a new source of supply similar to connections to interprovincial pipelines.

Regarding upgraders, the Commission Panel will not make a blanket determination in this Proceeding and future Commission Panels will be required to assess the form of regulation to be imposed on biomethane upgraders, including the possibility of a subsection 88(3) exemption, taking into consideration factors such as the sophistication of the parties involved, the nature of the contract entered into with the utility, and whether there is a demonstrated track record in operating such facilities.

Regarding the pipe from the upgrader, these are capital additions for which there is no set test for economic feasibility. The Panel considers these additions should be reviewed on a case by case basis. The Panel reviewing the Biomethane Post Implementation Report relating to the existing Biomethane Pilot Project may wish to establish rules or parameters covering pipeline connections to upgraders.

In the context of this Application, the determination that biomethane upgraders are regulated under the UCA has implications for the biomethane upgraders of the four biomethane suppliers with which FEI has filed supply agreements in the Application. In determining the

form of regulation of these third-party suppliers, the principles and guidelines for determining the form of regulation set out in section 2.2 of the AES Inquiry Report should be considered. The AES Inquiry Report states that the principles to be applied are:

- Where regulation is required use the least amount of regulation needed to protect the ratepayer.
- The benefits of regulation should outweigh the costs.

The AES Inquiry also sets out guidelines (p. 18), including, “providing adequate customer protection in cost effective manner.” Based on these principles and guidelines, FEI submits that a light-handed form of regulation is appropriate, as discussed below.

The two practical implications in this proceeding are that the third-party upgrading facilities may require CPCN approval from the Commission and that the supply contracts also need to be approved as a rate of the supplier pursuant to sections 58 to 61 of the UCA, in addition to being approved as a supply agreement under section 71 of the UCA. Each of these is discussed below.

In each of the four supply agreements proposed in the Application, the biomethane suppliers will own the upgrader facilities. The capital costs of these upgrader facilities are below the \$5 million dollar CPCN threshold, which was maintained by the Commission in the AES Inquiry Report (p. 48) and stated to be applicable to all parties (AES Inquiry Report, p. 84). The capital costs of the upgrader facilities for the four supply projects are included in Confidential Appendix 1, as details of the supply projects are commercially sensitive. Alternatively, FEI submits that the Commission should exclude these third-party suppliers from the CPCN requirement pursuant to section 45(4) of the UCA. The reasons why an exemption would be appropriate are discussed further below. In the event the Commission wishes to have a CPCN filed for any of the facilities, FEI proposes that this should occur after the supply agreement is approved, as these projects will not otherwise proceed.

The implication of the AES Inquiry Report’s determination that upgrading facilities are regulated is that the supply agreements also need to be approved as a rate of the suppliers pursuant to sections 58 to 61 of the UCA. FEI is currently in discussions with the suppliers with respect to their need to seek approval of the supply agreement as a rate. FEI may obtain the consent of the suppliers to apply for the rate on their behalf or have the suppliers themselves file a request. FEI will advise the Commission of the results of its discussions with suppliers in due course. In either case, the review of the supply agreement as a rate should be done in this proceeding at the same time the Commission is considering whether to approve the supply agreements under section 7. The Commission could not approve the same contract under section 71 and yet disapprove it under sections 58 to 61. Further, the public interest considerations are the same, whether it is approved as a supply agreement or a rate.

In the future, it would be appropriate for third-party suppliers to be exempt from regulation under section 22 by order of the Minister or under section 88 of the UCA, with the advance approval of the Lieutenant Governor in Council. The rationale for an exemption for third-

party suppliers is that the purchaser of the biomethane will be FEI whose supply contract for the biomethane will be subject to review and acceptance by the Commission. The review of the supply agreement will determine the need for the facilities, so there should be no requirement for the Commission to consider the need separately in a CPCN application. In addition, the rate impact to customers is in the price of the supply, which is reviewed as part of the supply agreement. The quality and quantity of supply and conditions of providing service are also addressed in the terms of the supply agreement. In the FEI's view, the long-term supply agreements provide sufficient consumer protection. Further, the ongoing performance of the supplier is overseen as part of FEI's biomethane program. FEI therefore sees no need for ongoing regulation of third-party suppliers in addition to the review and acceptance of the supply agreement and oversight of the biomethane program generally.

There is precedent for this treatment. Independent Power Producers that sell only to BC Hydro are exempt from the operation of Part 3 of the UCA by order of the Minister despite being "public utilities." They are not exempt to the extent that they otherwise sell to the public for compensation. Attached as an Appendix 2 to this filing is Minister's Order No. M-22-0205, dated June 6, 2002, which exempts independent power producers selling to BC Hydro.

Regarding the interconnection facilities, in all cases FEI owns and operates the necessary interconnection facilities that are downstream of the receipt meter. Where a third-party owns the upgrading facility, the third-party is responsible for the pipe from the upgrader to the receipt meter. FEI would only own the pipe from the upgrader to the receipt meter when FEI also owns the upgrading facility. As a safety matter, FEI seeks to have the interconnection station, including the meter and odorizing equipment, close to the upgrading facility to minimize the distance of pipe through which unodorized gas is passing. This is the same arrangement that FEI has with the interconnection facilities from interprovincial pipelines and is appropriate (see section 9.2 of the Application). Similar to the costs for interconnections to interprovincial pipelines, FEI is proposing that the costs of interconnections to biomethane projects continue to be borne by all customers as discussed in section 9 of the Application. FEI has addressed the potential for a test of the economic feasibility of interconnection facilities in section 6.5.2 of the Application.

### **2.2.2 CPCN Threshold**

The AES Inquiry Report states (at p. 48):

The Panel recognizes that the Biomethane Post Implementation Report is due in December 2012 and considers that the appropriate CPCN threshold and regulatory review (i.e. supply agreements reviewed under s. 71 of the UCA) will be dealt with in that Review. The Commission Panel reaffirms the \$5 million CPCN threshold until that time.

FEI did not address the CPCN threshold in the Application. FEI submits that the appropriate CPCN threshold for the biomethane activities continues to be \$5 million. The capital costs of upgrading facilities will typically be between \$2 and \$3 million, while the capital cost of interconnection facilities will typically be below \$1 million. It is possible, however, that large

supply projects may exceed these amounts and trigger the CPCN threshold. FEI submits that it is appropriate that only large projects trigger the threshold for the following reasons:

- The Biomethane service as a whole has been extensively reviewed in the 2010 Biomethane Application proceeding and is being reviewed again in the current proceeding. The Biomethane Program is clearly in line with British Columbia's energy objectives. In this proceeding, the Commission will be considering again the features of the program, including the appropriate cost allocation methodology and supply criteria. There is no need to revisit these general issues in detail for each new investment in a facility or for each new supply contract going forward.
- FEI is required to submit the supply contracts for acceptance under section 71. The investment in the upgrading and interconnection facilities will not proceed if the supply contract is not accepted. The Commission can, upon the filing of a supply contract, decide to require a CPCN if the circumstances suggest that this kind of review is needed.
- The costs of the Biomethane Program are modest. Annual program costs are approximately \$400,000 per year and interconnection capital costs are estimated at approximately \$2.1 million for the three existing projects, with \$30 thousand in annual operating and maintenance costs (sections 5.4 and 5.5 of the Application). Upgrading facilities typically cost between \$2 and \$3 million, and FEI's Salmon Arm Landfill upgrader is projected at \$2.3669 million (see section 5.2.5 of the Application).
- Demand for the biomethane service and supply exists as demonstrated in the Application. The demand-supply balance can be reviewed with the filing of each new supply agreement.
- There is low stranding risk associated with the upgrading assets, as a result of contractual provisions and the fact that significant components of the assets can be redeployed in the unlikely event that this is required.
- The Commission receives a detailed annual snapshot of the overall costs and state of the Biomethane business when the Biomethane Energy Recovery Charge is recalculated for January 1 of each year. Updates are also provided with the quarterly gas cost reports. The reports to the Commission include a forecast of all the costs of upgrading raw biogas and upgraded biomethane computed into an average rate for the coming year.

As a result of the low risk associated with these assets and their modest costs, the fact that the Biomethane Program is already subject to a detailed regulatory review and biomethane assets are subject to acceptance of supply contracts, the FEU submit that applying the standard CPCN threshold for the natural gas business of \$5 million is appropriate going forward.

### **2.2.3 Ownership of Upgraders and Business Structure**

The AES Inquiry Report states (at p. 49):

With respect to FEU ownership of upgrader facilities, the Commission Panel, in keeping with the Extension of Ownership principle, recommends that the utility not own the upgrading facilities where there are viable options. A viable option is put forward by the FEU where biomethane is supplied from third parties and is regulated through filing supply contracts under section 71 of the UCA. In the case where FEU own the upgrader, the upgrader should be owned and operated in a Regulated Affiliated Business and biogas supplied to FEI under a section 71 contract.

FEI continues to believe that it is important for it to have the flexibility to own upgrader facilities in certain situations as discussed in section 6.3 of the Application. FEI is, however, not proposing to own the upgrading facilities for the four supply agreements which it has proposed in the Application.

### **3. Conclusion**

As discussed above, the AES Inquiry Report confirmed that biomethane service is part of FEI's regulated service offering and part of the natural gas class of service. In light of the determinations in the AES Inquiry Report, FEI has provided further information in this filing addressing the CPCN threshold for biomethane activities and the form of regulation for third-party biomethane upgrading facilities.

If you have any questions or require further information related to this Application, please do not hesitate to contact the undersigned.

Yours very truly,

**FORTISBC ENERGY INC.**

***Original signed by: Ilva Bevacqua***

**For:** Diane Roy

Attachment

cc (email only): Registered Parties to the FEU 2012-2013 RRA, FEI 2010 Biomethane Application, Natural Gas Marketers

**Appendix 1**

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**FILED CONFIDENTIALLY**



## **Appendix 2**

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IN THE MATTER OF THE SALE, PURCHASE OR PRODUCTION OF A POWER SERVICE AND AN EXEMPTION FROM THE PROVISIONS OF PART 3 OF THE UTILITIES COMMISSION ACT, R.S.B.C. 1996, c. 473, AS AMENDED ("THE ACT")

WHEREAS, certain persons in the Province produce and sell to the British Columbia Hydro and Power Authority ("BC Hydro") or Powerex Corp. ("Powerex") a power service as defined in Section 22(1) of the Act;

AND WHEREAS, public utilities subject to the legislative authority of the Province are subject to regulation under Part 3 of the Act;

AND WHEREAS, persons who enter into energy supply contracts as defined in Section 68 of the Act must file copies of the contracts with the British Columbia Utilities Commission under Section 71 of the Act;

AND WHEREAS, pursuant to Section 22 of the Act, the Minister of Energy and Mines ("the Minister") is empowered to exempt, by order, persons selling, producing or purchasing a power service, and any equipment, facility, plant, project or system of such persons, from the provisions of Part 3 and Section 71 of the Act;

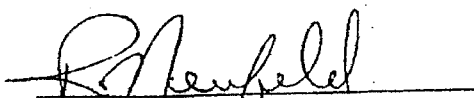
AND WHEREAS, the Minister considers that certain persons that produce and sell a power service to BC Hydro or Powerex should be exempt from the provisions of Part 3 except Section 22 of the Act, with respect to the production and sale to BC Hydro or Powerex of the power service;

AND WHEREAS, this exemption is made in addition to, and not in repeal of, exemptions ordered previously pursuant to Section 22 or its predecessors;

NOW THEREFORE, the Minister pursuant to Section 22 of the Act hereby exempts from the provisions of Part 3 except Section 22:

- (1) persons, their successors or assigns who produce and sell a power service to BC Hydro or Powerex, with respect to the production and sale to BC Hydro or Powerex of the power service;
- (2) subsection (1) above shall not apply to persons who at the time of their entering into an agreement to produce and sell the power service to BC Hydro or Powerex are otherwise a public utility; and
- (3) the equipment, facilities, plant, projects, or systems of the persons referred to in subsection (1) above which are used to produce and sell the power service to BC Hydro or Powerex, with respect to the production and sale to BC Hydro or Powerex of the power service.

Ordered this 6 day of June, 2002

  
Richard Neufeld  
Minister of Energy and Mines