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August 12, 2013

Via Email
Original via Mail

British Columbia Utilities Commission
Sixth Floor
900 Howe Street
Vancouver, B.C. V6Z 2N3

Attention: Ms. Erica M. Hamilton, Commission Secretary

Dear Ms. Hamilton:

Re: FortisBC Energy Utilities (FEU)[1]

Applications for Reconsideration and Variance of Commission Order G-26-13 Common Rates, Amalgamation, and Rate Design Decision (the Reconsideration Applications) - Phase Two

Response to the British Columbia Utilities Commission (BCUC or the Commission) Information Request (IR) No. 1

On June 26, 2013, the Commission issued Order G-100-13 establishing a Regulatory Timetable for Phase Two of the Reconsideration Applications. In accordance with Commission Letter L-46-13 setting out the Amended Regulatory Timetable, the FEU respectfully submit the attached response to BCUC IR No. 1.

If further information is required, please contact the undersigned.

Sincerely,

on behalf of the FORTISBC ENERGY UTILITIES

Original signed:

Diane Roy

Attachments

cc (e-mail only): Registered Parties

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[1] Consisting of FortisBC Energy Inc., FortisBC Energy (Vancouver Island) Inc. and FortisBC Energy (Whistler) Inc.

1.0 Reference: New Evidence of the FEU

Exhibit B-1, p. 3

Integration of FEU

The FEU states: "a comparison of these documents [the FEI to FEVI shared services agreements for 2004 and 2014] will show that, other than the additional provision of service from the Customer Service department which began in 2012, the schedules are substantially the same. This demonstrates that the overall level of integration of FEI and FEVI is unchanged from 2004 to the present. It also demonstrates that, at the time of the acquisition by Kinder Morgan, the FEU were already fully integrated, with the exception of adopting a common rate structure and common rates."

1.1 How does the FEU justify that the overall level of integration is unchanged from 2004 to the present if the schedules are "substantially the same" and there has been an addition of provision of service from the Customer Service department?

<u>Response:</u>

Since the schedules are "substantially the same", it shows that the same services are being provided from FEI to FEVI as were being provided in 2004, and that therefore the level of integration is substantially unchanged. The addition of provision of shared services from the Customer Service department is a result of the insourcing of the Customer Service function, which began in 2012. Prior to that, these services were provided by a third party, and the costs were allocated from the third party to FEI, FEVI and FEW. The insourcing of the services results in them being added to shared services agreements, but does not change the level of integration. These services were already being provided on an integrated basis prior to the insourcing of the Customer Service function.

1.2 Does FEU agree that the Commission expects utilities to operate efficiently? If no, please explain why not.

<u>Response:</u>

Yes.

1.3 Please explain what meaningful impact, if any, the level of integration between the FEU companies would have had on: (i) the Commission's Bonbright evaluation of the FEU common rates request (please identify the specific Bonbright principle affected and discuss whether the impact would be significant); and (ii) the FEU request to amalgamate if common rates were approved.

Response:

Please refer to the response to BCUC IR 1.11.14 for a discussion of the impact on the Commission's Bonbright analysis.

The level of integration is important to the request for amalgamation in several respects. For instance, because of the level of integration of the FEU, the cost savings usually associated with amalgamation alone have already been achieved. As another example, the level of integration means that amalgamation will result in few operational changes and will more accurately reflect the integrated nature of the service that is currently provided to all of FEU's customers.

1.4 Please explain what meaningful impact, if any, considering postage stamp rates within the context of an amalgamated entity would have had on the Commission's Bonbright evaluation of the FEU common rates request. Please identify each specific Bonbright principle affected and discuss whether the impact would be significant.

Response:

Please refer to the responses to BCUC IR 1.11.1 and 1.11.10.

1.5 Please provide details of how much of the purchase price in the Kinder Morgan acquisition was allocated or related to the predecessor of FEVI. Also, provide details of how that FEVI predecessor purchase price compared to the net book value of that entity. Clarify if the acquisition had accounted for the FEVI predecessor's losses in its consideration and determination of the agreed upon purchase price.

Response:

The FEU do not know the allocation that was done by Kinder Morgan's management in its assessment of the value of Terasen Inc., specifically related to FEVI, or the allocation of the purchase price to that effect.

1.6 Please discuss if FEU has considered selling FEVI.

Response:

No, the shareholder of FEVI has not considered selling FEVI. Further, the question of a sale of FEVI is not relevant to this proceeding, which is about whether it is in the public interest to amalgamate the FEU and implement postage stamp rates.

2.0 Reference: New Evidence of the FEU

Exhibit B-1, pp. 3-4; FEU 2012 Amalgamation Proceeding,

Exhibit B-15, BCUC 2.51.4, Exhibit B-9, BCUC 1.81.7.1

Energy Choices and Efficiency

The FEU states on pp. 3-4: "the FEU submit that the Commission should have considered all of the public interest factors in favour of amalgamation and postage stamp rates. As discussed in paragraphs 56 to 58 of the Reconsideration Application, one of those public interest considerations is how postage stamp rates affect consumers' choice between natural gas and electricity within the service areas of FEVI and FEW."

FEU states in Exhibit B-15, BCUC 2.51.4 of the FEU 2012 Amalgamation Proceeding:

> "The FEU expect that the impact of the postage stamp rate proposal on overall natural gas usage in the province will be neutral or close to neutral. Any usage increase in FEVI and FEW resulting from lower natural gas rates (whether from fuel switching or increased usage by existing customers) may be more or less counterbalanced by the usage decreases in FEI and FEFN due to the rate increases in those areas.
>
> Moreover, as indicated in Sections 4.1 and 6.8 of the Application, while amalgamation and common rates will improve natural gas prices in FEVI and FEW, the price of energy is only one of many determinants that inform customers' energy choices. Other factors include initial capital cost investment, perceptions about the green attributes of the fuel and space concerns with respect to appliance installations. Therefore, taking all these factors into account, the FEU do not expect any material fuel switching to take place from electricity to natural gas for space heating and hot water as a result of amalgamation and common rates."

FEU states in Exhibit B-9, BCUC 1.81.7.1 of the Original Application:

> "... it is difficult to determine the impact of postage stamp pricing in gas sales within the FEU as a whole. ... Even with the lower gas costs, potential new customers will continue to have the installation capital cost hurdle to overcome in making their energy choice, and potentially negative perceptions of natural gas as a fossil fuel. Therefore, significant new customer additions as a result of lower rates in FEVI and FEW may be limited."

2.1 Please describe all the public interest factors that FEU submit the Commission should have considered, but did not. In your response, please note if these factors were explored in the evidence during the original proceeding.

Response:

The FEU listed the public interest factors on pages 19 to 24 of the FEU's Reconsideration Application. These are:

1. Public policy
2. Regulatory practice
3. Energy choices
4. Cost savings and regulatory efficiencies
5. Government energy policy

These public interest factors were explored during the original proceeding. The FEU described the public interest benefits of amalgamation and postage stamp rates in section 6 of the Common Rates, Amalgamation and Rate Design Application (Exhibit B-3, pages 105 to 130), including the benefit of facilitating consistent access to service offerings, the benefit of regulatory, reporting and operational efficiencies and how common rates fit with government GHG policy. These and other public interest areas were explored in information requests, including public policy (see section 3.1 of the FEU's Final Argument for references to the evidentiary record), regulatory practice (see section 3.2 of the FEU's Final Argument), and energy choices (e.g., Exhibit B-9, BCUC IR 1.81 series; Exhibit B-12, BCRUCA IR 2.1.1).

While these factors were explored in evidence during the original proceeding, the Commission's framework for analyzing the approvals sought, which focused on the application of the Bonbright principles and gave paramountcy to the Commission's interpretation of the fairness principle, precluded the consideration of these public interest factors, which the FEU submit was in error.

The FEU also note that the new public policy evidence outlined in the Ministry's letter attached as Appendix "A" to the FEU's Reconsideration Application, including the policy rationales equality of investment and job creation opportunities, regulatory efficiency and customer rate impacts, should also now be considered by the Commission.

2.1.1 Given the FEU's evidence in the original proceeding that FEU did not expect any overall increase in fuel usage or fuel switching as a result of a move to postage stamp rates, please explain what meaningful impact, if any, the public interest factors noted above would have had on: (i) the Bonbright evaluation of the FEU common rates request (please identify the specific Bonbright principle affected); and (ii) the FEU request to amalgamate if common rates were approved.

Response:

The IR does not accurately describe the FEU's evidence. The FEU's evidence was that the FEU did not expect any material fuel switching from electricity to natural gas. The FEU have always expected that there could be increased fuel switching from heating oil and propane to natural gas. See the response to AVICC IR 1.8.2. However, for the various reasons discussed by the FEU, the FEU concluded that the impact of the postage stamp rate proposal on overall natural gas usage in the province will be neutral or close to neutral.

In the FEU's submission, the fact that the Commission adopted an approach which excluded public interest factors from consideration was a legal error. The Commission should have considered all the reasons in favour of amalgamation and the adoption of common rates as identified by the FEU, including public interest factors. The import of the public interest factors does not depend on there being a material overall increase in natural gas usage. Refer to the response to BCUC IR 1.11.1.

2.2 Does FEU believe that, as a result of the carbon tax, British Columbia provincial policy and legislation support consideration of economic efficiency alone in the choice between natural gas and electricity?

Response:

The FEU believe that the carbon tax, representing a price on carbon emissions, should have the effect of placing natural gas on an equivalent footing with electricity with respect to greenhouse gas considerations. As such, comparison of the two energy sources from the standpoint of economic efficiency should become a primary consideration. However, as the FEU have consistently maintained, the efficient use of natural gas (and alternative energy solutions, where feasible), rather than electricity, to serve thermal energy needs in BC is both economically efficient and beneficial from an environmental and GHG emissions standpoint. This has been characterized as the "right fuel for the right use". From an economic efficiency perspective, using natural gas to serve thermal energy needs will provide throughput benefits on the natural gas system while at the same time reduce the need for electric utilities to acquire high cost marginal electricity supply and avoid costly electricity system upgrades that would be required to serve peak winter demand, when thermal energy demand is highest. From an environmental and GHG emissions perspective using natural gas for thermal energy needs can free more electricity supply resources to displace higher emitting energy demands such as for electric vehicles in the passenger vehicle markets, where electricity will displace gasoline or diesel fuel.

2.2.1 If yes, please provide evidence that BC is expected to meet the emission reduction targets as stated in the *Clean Energy Act*.

Response:

The FEU do not agree with the apparent premise of the question that unless BC is meeting its reduction targets, then natural gas and electricity should not be evaluated on similar basis. In theory, once the carbon tax is applied to natural gas it should be considered a clean fuel similar to electricity.

Considering other fuels, the issue is complex. For example, natural gas usage can reduce GHG emissions when it is displacing home heating fuels such as heating oil and propane, the use of gasoline or diesel in vehicles, or the use of electricity generated by burning diesel fuel or coal. Natural gas can also reduce emissions by displacing higher emitting fuels in industrial applications. As the FEU have discussed in the response to BCUC IR 1.2.2, the policy should be to use the right fuel for the right use.

The FEU have been making a contribution to reducing greenhouse gas emissions among their own customers and within BC through a number of initiatives. These include expanded energy efficiency and conservation programs, natural gas for transportation to reduce GHG emissions in the medium and heavy duty sectors, a renewable natural gas (biomethane) initiative to expand the availability of a carbon neutral fuel, and thermal energy solutions (undertaken by an affiliate company FAES).

2.3 Please confirm that natural gas and electricity are different energy sources with different characteristics.

Response:

Confirmed.

Despite such differences, natural gas and electricity are interconnected in a number of ways. They are alternative and competing energy sources in various energy end-uses, primarily in the space and water heating markets. Natural gas is also a fuel source for electricity generation in BC and in other jurisdictions. Electricity is also an energy source employed in important ways in natural gas delivery such as powering compressors and powering equipment to produce liquefied natural gas, to name a few.

2.4 Please confirm that: i) in BC, more than one utility provides electricity; and ii) all electric utilities in BC do not apply postage stamp rates consistent with BC Hydro's rates.

Response:

i) Confirmed that there are a number of electric utilities in the province. BC Hydro and FortisBC are the two largest electric utilities in BC, serving the vast majority of electric customers in the province. In addition there are a small number of municipally-owned electric utilities that are not subject to regulation by the BCUC and some small investor-owned electric utilities.

ii) Confirmed that all electric utilities do not apply the *same* postage stamp rates as BC Hydro; however, to the best of the FEU's knowledge, all electric utilities in BC do apply postage stamp rates within their own service territories. Postage stamp rates cannot occur between separate utilities; however, the municipally-owned and small investor-owned electric utilities, comprising in total only about 3 to 4 percent of electricity customers in BC, generally consider the rates of the neighbouring large utility (BC Hydro or FortisBC) in establishing their own rates and in some cases do adopt the same rates as the large neighbouring electric utility. Please also see the response to BCUC IR 1.11.12 regarding the use of postage stamp rates in BC.

3.0 Reference: New Evidence of the FEU

Exhibit B-1, p. 5

Moody's Report - FEU Interactions

FEU states: "Moody's has re-affirmed the challenges faced by FEVI. The denial of the Application has been noted as credit negative to FEVI, and may contribute to a future downgrade, which will increase borrowing costs to FEVI customers, all else equal."

3.1 Please describe interactions the FEU had with Moody's personnel prior to Moody's issuing its report on June 26, 2013. For example, please list meetings and dates, information sent to Moody's by the FEU and dates it was sent, and all other interactions or information Moody's based this report on.

<u>Response:</u>

The FEU have had the following interactions with Moody's with respect to the ratings of FEVI, FEI, FBC and FHI:

- February 27, 2013 – the FEU sent Moody's the amalgamation and common rates decision following its release on February 25, 2013.
- May 13, 2013 – the FEU sent Moody's the Stage 1 GCOC decision following its release on May 10, 2013.
- May 18, 2013 – Moody's requested and the FEU sent FEVI's December 31, 2012 Year End Financial Statements.
- June 11, 2013 – The FEU had a conference call with Moody's to provide a brief discussion to Moody's of the BCUC decisions regarding amalgamation and common rates and generic cost of capital. At that time, the FEU were advised Moody's would go to their credit committee later in the month of June.
- June 21 – Moody's provided the FEU with a draft press release of the credit negative watch to all Moody's rated FEU entities. FEU were not aware of the negative outlook until the draft press release was provided to the FEU. Moody's sought limited input on the press release according to the following instructions, included in the email:

"Attached is the draft press release for your review, to give you the opportunity to draw attention to any factual errors and/or inadvertent disclosure of confidential information. However, please note that under our policies, MIS retains ultimate editorial control over the form and content of all its publications. MIS will not accept other changes from an issuer that would alter the meaning or tone of our opinions or credit rating announcements.

> ***Please note that this draft report is strictly confidential and you may not disclose it to any other person except: (i) to your legal counsel acting in their capacity as such; (ii) to your other authorized agents acting in their capacity as such; and (iii) as required by law or regulation.***
>
> ***We would appreciate if you could revert with your comments within an hour."***

The FEU provided comments back to Moody's on the press release, as requested by Moody's, to draw attention to any factual errors and/or inadvertent disclosure of confidential information. Later that same day, the FEU had a conference call with Moody's to discuss the reasons for the negative outlook.

- June 24 – Moody's asked about FEVI's liquidity (FEVI credit facility was due to mature 2013) and 2012 dividend. FEVI was in the process of extending its credit facility and the lower dividend in 2012 was due to the timing of equity funding for the Mt Hayes facility.
- June 24 – Moody's provided the FEU with the draft credit reports and sought comments on any factual errors and/or inadvertent disclosure of confidential information, as per the following instructions:

> ***"Attached is the draft research for your review, to give you the opportunity to draw attention to any factual errors and/or inadvertent disclosure of confidential information. However, please note that under our policies, MIS retains ultimate editorial control over the form and content of all its publications. MIS will not accept other changes from an issuer that would alter the meaning or tone of our opinions or credit rating announcements.***
>
> ***Please note that this draft research is strictly confidential and you may not disclose it to any other person except: (i) to your legal counsel acting in their capacity as such; (ii) to your other authorized agents acting in their capacity as such; and (iii) as required by law or regulation."***

- June 25 - The FEU provided comments back to Moody's on FEVI's credit report, as requested by Moody's, to draw attention to any factual errors and/or inadvertent disclosure of confidential information.
- June 26 – The FEU had a follow up call with Moody's to discuss the negative outlook in the credit report. The discussion was focused on the basis of the negative outlook which was concerned about the impact of the Stage 1 GCOC decision and potential negative impact of the Stage 2 GCOC decision, and the negative implications of the denial of the amalgamation and postage stamp rates application.

3.1.1 Please specify whether the FEU provided Moody's with information about solutions to FEVI's challenges other than common rates.

Response:

It is not clear what other solutions are being referenced in the question. In the absence of common rates, the FEU do not envision any solutions that would not require a significant rate increase for FEVI at some point.

Moody's was briefed on the FEU's application to amalgamate the gas utilities and adopt postage stamp rates across the service territories. As this was the proposed solution, and the solution that was applied for as being the sustainable, long term solution to rate challenges at FEVI, no other proposal was discussed.

3.1.2 To the best of the FEU's knowledge, what information did Moody's have at the time of the June 26, 2013 report, about solutions to FEVI's challenges other than common rates?

Response:

Again, it is not clear what other solutions are being referenced in the question. In the absence of common rates, the FEU do not envision any solutions that would not require a significant rate increase for FEVI at some point.

To the best of FEU's knowledge, Moody's would have had access to the full evidentiary record in support of the application for common rates and amalgamation and would have been aware that common rates as proposed are the sustainable, long term solution to FEVI's challenges. Moody's is also aware of the reconsideration proceeding. Please also refer to the response to BCUC IR 1.3.1.1.

3.2 Does FEU have any evidence that Moody's or other agencies will or are considering a downgrade to FEVI's credit rating? If so, please provide. If not, is the FEU's statement: "may contribute to a future downgrade" speculation at this point?

Response:

Yes, there is clear evidence that FEVI is at risk for a downgrade by the very fact that FEVI is currently on negative outlook by Moody's. Having a negative outlook, as opposed to a stable outlook, is a first step to a change in rating. It is the method by which Moody's will signal to the market that it has sufficient concern that a ratings downgrade is likely, but not yet confirmed. Following a negative outlook, Moody's will more closely monitor the situation prior to making a determination to change the rating. Therefore, the FEU are not speculating when they state that the decision by the BCUC may contribute to a downgrade, as the denial of the application was noted as a credit negative for FEVI.

3.3 Please clarify what other things are that they are keeping equal, and if those other things changed, what the effect would be.

Response:

The quoted passage is making reference to two related issues: the potential downgrade of FEVI's rating, and the effect that a downgrade would lead to an increase in borrowing costs that could put further pressure on FEVI rates. The FEU used the phrase "all else equal" because it is possible that other factors, such as changes to market interest rates or credit spreads from general market conditions, could offset the increase in borrowing costs due to a downgrade. By using the phrase 'all else equal' the FEU is pointing out that the downgrade arising from the denial of common rates would have a negative impact in and of itself.

4.0 Reference: New Evidence of the FEU

Exhibit B-1, p. 5; FEU 2012 Amalgamation Proceeding,

Exhibit B-9, BCUC 1.92.1

Moody's Report - Rate Shock

FEU quotes from Moody's Credit Opinion for FEVI of June 26, 2013: "FEVI's rates have historically been capped such that the cost of gas has been similar to the cost of alternative forms of energy. Now, with the expiration of royalty payments, the company will likely require significant rate increases to maintain its financial stability ... in the midst of what could be a rate shock environment for FEVI customers."

FEU state in Exhibit B-9, BCUC 1.92.1 of the Original Application: "There are no customers in FEI, FEW and FEFN that are expected to experience significant rate increases under the status quo scenario."

4.1 Does FEU agree with Moody that, in the absence of postage stamp rates, FEVI customers could be subject to rate shock? Please explain.

Response:

Yes, the FEU agree with Moody's that, in the absence of postage stamp rates, FEVI customers could be subject to rate shock. Assuming rate shock is defined as an increase in burner tip rates of more than 10%, FEVI has the potential for rate shock once the RSDA is depleted. As the FEU described in response to BCUC IR 1.92.1 in the original proceeding:

> *If postage stamp rates are not approved and the RSDA is used to mitigate annual rate increases for FEVI, FEVI customers will experience rate increases in 2017, as well as 2018, once the RSDA is expected to be fully depleted and the impact of the loss of the royalty revenues is experienced. Specifically, FEVI estimates that sales customers will experience an approximate 11% burner tip increase in 2017 followed by a further approximate 13% burner tip increase in 2018.*

As shown in the response to BCUC IR 1.4.1.1, more current estimates of the increase to FEVI's customers are approximately 15% in 2020. This is still above the 10% guideline for burner tip rates.

4.1.1 Please provide updated evidence of forecast percentage rate increases for each of FEVI's major customer classes over the next 10 years in the absence of postage stamp rates.

Response:

The following table provides an approximate forecast of rate increases for all of FEVI's customers over the next 10 years. Note there are several high level assumptions included in this table around margin and gas cost increases, therefore, the forecast is subject to change. The assumptions included in the table below are as follows:

- Delivery Margin increases of 3% to reflect an updated projection of the potential future cost increases
- Commodity cost increases of 10% in 2014 reducing to 2% in 2023 as shown on Line 2 on the Table below to reflect updated projections of gas cost increases
- Income Tax Rate of 26% beginning 2014 to reflect recent changes made by the Provincial Government to the enacted tax rates
- Equity percentage of 40% and ROE of 10% (pending a decision in Phase 2 of the Generic Cost of Capital proceeding)
- Forecasted 2013 revenues and costs based on those approved through Order G-44-12 as part of the 2012/2013 Revenue Requirement Application.
- Opening 2012 RSDA updated to reflect the actual balance in the account and 2013 RSDA addition updated to reflect the 2013 approved RSDA addition included in Order G-44-12. This results in an ending 2013 RSDA balance that is approximately $12 million higher before-tax than was included previously.

These assumptions vary from the amounts shown in BCUC IR 1.4.1 as the original amounts included the following assumptions:

- Delivery Margin increases of 5%
- Commodity cost increases of 3%
- Income Tax Rate of 25% throughout
- Forecasted 2013 revenues and costs based on those presented in Exhibit B-52, Undertaking 24 of the 2012-2013 Revenue Requirement Application

Based on the new assumptions, FEVI would anticipate the RSDA providing stable rates for FEVI customers through 2019, until the depletion of the RSDA balance in early 2020. Once depleted, rates could be expected to rise approximately 15 percent that year and by 2 percent for the next several years thereafter.

Line	Assumptions	2013 Approved	2014 Forecast	2015 Forecast	2016 Forecast	2017 Forecast	2018 Forecast	2019 Forecast	2020 Forecast	2021 Forecast	2022 Forecast	2023 Forecast
1	Incremental Delivery Margin Increase		3%	3%	3%	3%	3%	3%	3%	3%	3%	3%
2	Incremental Commodity Cost Increase		10%	10%	5%	5%	5%	2%	2%	2%	2%	2%
3	Cumualtive Tax Rate Increase compared to 2013		1%	1%	1%	1%	1%	1%	1%	1%	1%	1%
4												
5												
6												
7		2013 Approved	2014 Forecast	2015 Forecast	2016 Forecast	2017 Forecast	2018 Forecast	2019 Forecast	2020 Forecast	2021 Forecast	2022 Forecast	2023 Forecast
8												
9	Annual Revenue Deficiency (Surplus)											
10	Delivery Margin	129,058	132,930	136,918	141,025	145,256	149,614	154,102	158,725	163,487	168,391	173,443
11	Cost of Gas	70,924	78,016	85,818	90,109	94,614	99,345	101,332	103,359	105,426	107,534	109,685
12	Income Tax Changes	-	582	582	582	582	582	582	582	582	582	582
13		199,982	211,529	223,318	231,716	240,453	249,541	256,016	262,666	269,495	276,508	283,711
14	Less: Forecast Revenue at Existing Rates	(195,727)	(202,819)	(210,621)	(214,912)	(219,417)	(224,148)	(226,135)	(228,162)	(230,229)	(232,337)	(234,488)
15	Forecast Annual Deficiency (Surplus)	4,255	8,709	12,697	16,805	21,035	25,393	29,881	34,504	39,266	44,171	49,223
16	RSDA	(4,255)	(8,709)	(12,697)	(16,805)	(21,035)	(25,393)	(29,881)	(465)	-	-	-
17	Net Annual Deficiency (Surplus)	-	-	-	-	-	-	-	34,039	39,266	44,171	49,223
18												
19	**Approximate Rate Increase (Decrease), %**	**0.0%**	**0.0%**	**0.0%**	**0.0%**	**0.0%**	**0.0%**	**0.0%**	**14.9%**	**17.1%**	**19.0%**	**21.0%**
20	**Effective Rate**	**15.725**	**15.725**	**15.725**	**15.725**	**15.725**	**15.725**	**15.725**	**18.071**	**18.407**	**18.715**	**19.026**
21												
22												
23	**RSDA Forecast**											
24	Opening RSDA Balance, net of tax	(77,773)	(76,867)	(72,533)	(65,081)	(54,328)	(40,087)	(22,162)	(348)	-	-	-
25	Annual (Surplus)/ Deficiency	4,255	8,709	12,697	16,805	21,035	25,393	29,881	465	-	-	-
26	Add: Interest on Balance	(3,047)	(2,853)	(2,626)	(2,273)	(1,790)	(1,170)	(404)	5	-	-	-
27	Less: Rate Rider drawdown		-	-	-	-	-	-	-	-	-	-
28	Less: Tax	(302)	(1,523)	(2,618)	(3,778)	(5,004)	(6,298)	(7,664)	(122)	-	-	-
29	Closing RSDA Balance, net of tax	(76,867)	(72,533)	(65,081)	(54,328)	(40,087)	(22,162)	(348)	-	-	-	-
30												
31	Tax Rate	25.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%
32	Closing RSDA Balance, before tax	(102,489)	(98,018)	(87,947)	(73,416)	(54,172)	(29,949)	(470)	-	-	-	-

4.1.2 Please provide sensitivity analysis for the rate increase estimates above arising from potential new projects (e.g. Woodfibre Site). For residential customers, please also provide average annual increases per customer in dollar terms (based on FEVI average residential consumption levels).

Response:

It is expected that potential new projects such as the project to serve the Woodfibre LNG Site will provide net benefits to FEVI's existing customers. However, as this project is still in the preliminary stage, a sensitivity analysis at this point would provide little value as FEVI is still working on its feasibility study to develop a capital cost estimate and finalize a firm contract daily demand to serve the Woodfibre LNG site. A sensitivity analysis, and the subsequent impacts on customer rates can be done after the project costs, contract demand and timelines have been established.

5.0 Reference: New Evidence of the FEU

Exhibit B-1, p. 5; FEU 2012 Amalgamation Proceeding, Exhibit B-15, BCUC 2.3.6;

BC Hydro 2008 RIB Application, Terasen Gas Final Submission, pp. 97-98

Moody's Report - FEVI Negative Impacts

FEU quotes from Moody's Credit Opinion for FEVI of June 26, 2013: "In an effort to combat the negative impact of royalty payments expiring, the [FEU] filed a joint application with the BCUC to amalgamate and harmonise rates." FEU state: "The denial of the Application has been noted as credit negative to FEVI, and may contribute to a future downgrade, which will increase borrowing costs to FEVI customers, all else equal."

FEU states in BCUC 2.3.6 of the Original Application: "Amalgamation results in marginally higher risks for FEI Amalco versus FEI and the FEU have filed evidence to establish that a 12 basis point risk premium is reasonable." FEU also states in their Final Submission on the Original Application (pp. 97-98):

> "[Ms. McShane] concludes that the 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. Overall, the slightly higher post-amalgamation price competitive risks of FEI Amalco indicate, directionally, a higher post-amalgamation cost of capital for FEI Amalco."

Terasen Gas (now FEI) state in their Final Submission on the BC Hydro Residential Inclining Block Application[1]:

> "While the policy behind establishing lifeline rates specifically intended to address low-income customers is commendable, the law of this province has long precluded the Commission from establishing a rate that is intended to create a cross-subsidy among customers."

Terasen Gas quotes *Prince George Gas v. Inland Natural Gas,* a 1956 decision of the British Columbia Court of Appeal in support of the above statement.

5.1 Given the evidence in the original proceeding that postage stamp rates would improve the competitive position of FEVI and FEW, but reduce the competitive

[1] http://www.bcuc.com/Documents/Arguments/2008/DOC_19330_07-24_TerasenUtilities_Argument.pdf

position of FEI; please explain to what extent, if any, the FEVI Moody's report is relevant to the reconsideration.

Response:

The Moody's report is evidence of the continuing challenges facing FEVI given the termination of the royalty payments and FEVI's vulnerability to externalities given its small size. The Moody's report is also evidence that the rejection of the FEU's Application to amalgamate the FEU and implement postage stamp rates will increase those challenges. These are factors that the FEU believe should be of concern to the Commission and should be considered in determining whether it is in the public interest to amalgamate the FEU and implement postage stamp rates.

5.2 What does FEU reasonably consider to be the 'negative impacts' arising from royalty payments referred to in Moody's credit opinion? Please include in your response if this could include negative impacts to the FEVI shareholder and rate increase to FEVI customers.

Response:

The FEU believe that the reference on page 3 of the Moody's report to the negative impacts of the royalty revenues expiring is a reference back to the immediately preceding discussion in the report about how Moody's expects "FEVI to have declining cash flow and financial metrics, from 2013 onwards, due to the phase-out of royalty revenues from the Province at the end of 2011." These negative impacts include rate increases to FEVI's customers. As discussed by Moody's, "Anticipating the termination date, FEVI has been able to grow the RSDA since 2009, allowing the company to amortize and smooth the impact of higher future costs by providing near-term rate stability." These negative impacts, which challenge the overall competitive position of FEVI, increase the risk to FEVI's debenture holders and shareholder on the capital investment in the utility.

5.3 Does FEU still consider that the 'law of this province' requires that the Commission can not establish a rate that is intended to create a cross-subsidy among customers? Please explain.

Response:

The FEU's proposed postage stamp rates do not create a cross-subsidy. The FEU's proposed postage stamp rates represent a different way to allocate costs amongst the customers of the amalgamated FEU compared to existing rates for the individual utilities, which is made possible by amalgamating the utilities. In particular, postage stamp rates remove rate difference due to the location of the customer. While this results in rate changes amongst existing regions, the resulting rates are cost-based with each class of customers recovering the cost to serve that class. As the FEU have emphasized, this is in fact the way FEI's costs are allocated now (with the exception of the costs to serve the small number of customers in Fort Nelson). The FEU's submission has been that it is beneficial in the public interest to amalgamate the utilities so that this way of allocating costs amongst the FEU (that is otherwise impossible) can be achieved and the benefits of the approach realized.

The way in which costs are allocated through postage stamp rates (i.e. without regard to the customer's location) has been determined to be just and reasonable and not unduly discriminatory by the Commission and other regulators across Canada, and is in fact the predominant approach for electric and gas utilities in North America. It is therefore well established that postage stamp rates, or setting rates without regard to location, is just, reasonable and not unduly discriminatory and within the jurisdiction of the Commission.

In summary, the principle referred to and supported by the Prince George Gas v. Inland Natural Gas case does not apply to the implementation of postage stamp rates, since postage stamp rates are cost-based rates, ensure that similarly situated customers in each class recover their cost to serve and do not create a cross-subsidy. There can be no doubt that the FEU's proposed postage stamp rates can be lawfully implemented by the Commission.

5.3.1 Does FEU consider that using postage stamp rates for the specific purpose of mitigating the impact of royalty payments conflicts with the above requirement? Please explain why/why not.

Response:

Please refer to the response to BCUC IR 1.5.3.

5.4 Please clarify what other things are that they are keeping equal, and if those other things changed, what the effect would be.

Response:

Please refer to the response to BCUC IR 1.3.3.

5.5 Does FEU agree that, in order to: (i) minimize unnecessary bill impacts; and (ii) ensure efficient use of utility and Commission resources, the Commission should require that a rate design application demonstrates an overall net benefit to ratepayers compared to the status quo (i.e. for FEU customers overall, not just for FEVI customers)? Please explain.

Response:

As the FEU have submitted, the proposed amalgamation and postage stamp rates provide a number of benefits and result in a net benefit to customers overall. However, it cannot be a general requirement that a rate design application demonstrate an overall net benefit to customers. The primary purpose of rate design is to apportion the recovery of the utilities revenue requirement amongst customers. The rate design process is necessary to set rates which are just and reasonable and not unduly discriminatory, and is not justified on the basis of net benefits to customers. A reasonable conclusion of a rate design application, for instance, may be that no changes to the rate are necessary. This would serve to confirm that the existing rates continue to be just and reasonable and not unduly discriminatory. To the extent that a rate design improves upon existing rate design, e.g. by resulting in more efficient rates, there can be a “net benefit” to customers. However, this cannot be a blanket requirement for rate designs.

5.5.1 If no, please explain how it would be an efficient use of utility and Commission resources to develop and review rate applications where there is no overall benefit to ratepayers?

Response:

Please refer to the response to BCUC IR 1.5.5.

5.5.2 Does FEU consider that large rate decreases for a small number of customers, with small rate increases for a large number of customers is a net benefit for ratepayers? If yes, please explain how this is consistent with FEI's previous position that the Commission can not establish a rate that is intended to create a cross-subsidy among customers.

Response:

As the FEU submitted in the original proceeding, the extension of common rates and amalgamation is clearly in the public interest, and of net benefit to the FEU's customers overall. While there is greater rate benefit to certain customers, this is not a cross-subsidization as suggested by the question, as the proposed postage stamp rates for the amalgamated entity are cost based.

Please refer to the responses to BCUC IR 1.5.3, 1.5.5 and 1.11.1.

6.0 Reference: New Evidence of the FEU

Exhibit B-1, p. 5

Moody's Report - FEVI Other Options

FEU quotes from Moody's Credit Opinion for FEVI of June 26, 2013: "FEVI's rates have historically been capped such that the cost of gas has been similar to the cost of alternative forms of energy. Now, with the expiration of royalty payments, the company will likely require significant rate increases to maintain its financial stability. This highlights the need for the small utility, with smaller scale and less ability to spread fixed costs across a larger customer base, to receive regulatory support in the midst of what could be a rate shock environment for FEVI customers."

The FEU state: "The FEU, however, see no evidence that a rate design that allocates costs or sets rates on a different basis as among existing customers can effectively address the challenges that have been well documented in the evidence before the Commission..."

6.1 Does Moody's comment that the provision of 'regulatory support' is required to maintain the financial stability of FEVI mean that Moody does not consider FEVI is an economic utility? If no, please explain what FEU considers that this comment means.

Response:

The FEU assume that the reference in the question to 'economic utility' is synonymous with 'going concern'. On that basis, the FEU do not agree with the premise of the question that Moody's "does not consider FEVI an economic utility." Moody's provides a rating on the debentures of FEVI and is assessing the credit risk of the debentures. Moody's is commenting on the financial stability in the context of its current A3 rating, and that absent regulatory support to alleviate the rate increases to customers and improve the competitive position of FEVI, FEVI may be at risk of a downgrade. In the context of Moody's past reference to the potential for amalgamation, Moody's comment on the provision of regulatory support appears to be referring to the adoption of amalgamation and common rates.

6.1.1 Please explain to what extent concerns regarding the financial stability of a utility are a concern for the ratepayer compared to a concern for the utility shareholder. Specifically, how would the FEVI shareholder be able to avoid a write-down of its assets if FEVI became uneconomic (other than through amalgamation/common rates)?

Response:

FEVI provides an important service to over 100,000 customers who rely on cost-effective, safe and reliable service. Therefore, FEVI and its customers are aligned in ensuring that the financial health of FEVI is maintained for the long-run. Customers benefit from lower cost of capital as well as from the stewardship of a shareholder seeking a reasonable return in order to maintain safe and reliable service.

The FEU have not suggested that FEVI is, or is about to become, uneconomic as defined as "not being able to continue as a going concern". Therefore the issue of a write down of assets is not relevant to this proceeding.

6.1.2 Does FEU agree that the FEVI shareholder has received compensation in the past (through its allowed return on equity) for the FEVI financial stability risk?

Response:

The FEU do not understand what is meant by 'financial stability risk'.

In the past, FEVI has received a risk premium in its ROE relative to FEI to compensate for the incremental risk to the benchmark FEI, associated with the long run risks faced by FEVI as a going concern utility. This premium has been justified for a number of reasons, including risk related to: FEVI's smaller size, more concentrated customer base, competitive pressures and operating risk. In general, the overall allowed ROE and capital structure for FEVI is intended to address the risk of return on and of capital faced by FEVI on a standalone basis.

The premise of the question seems to be that past cost of capital decisions had been based on an expectation that the Commission would not provide regulatory support if and when required. The FEU do not accept that premise; in fact, the opposite is true. The fundamental reason that allowed returns for utilities are lower than for unregulated peers is because the public utilities are afforded *regulatory protection* that unregulated market players do not benefit from. Experts filing cost of capital evidence in past proceedings tend to characterize BC as a relatively supportive regulatory environment. This assessment is also reflected in credit reports that have been cited in past Decisions. For instance, the 2006 ROE Decision cites DBRS's comment that: "The company benefits from a supportive regulatory regime," (p.34). In the 2009 Decision, the Commission cited Moody's assessment, which included for "Regulatory Support and Relationship" an assessment of "Very good, proactive support" (p.33), and quoted from

Moody's where it referred to "the relative supportiveness of TGI's regulatory environment" (p.34).

A practical example of the Commission providing support is its steps to assist PNG following the closure of its largest customers.

As such, for the Commission to adopt the position implicit in the question that it should no longer provide support to utilities, even where it is reasonable and in the public interest to maintain cost effective service to customers, would represent a profound change in the nature of the regulatory framework to date. The potential for this to occur is certainly not one that is reflected in the overall allowed return, and it is difficult to see how withdrawing regulatory support is in the best interests of anyone.

6.1.3 Does FEU consider it is good utility practice to compensate a utility for its financial stability risk through the allowed return on equity, and then provide additional 'regulatory support' in the event the risk materialises? If yes, please explain if this would result in the shareholder being compensated twice for the same risk.

<u>Response:</u>

Please refer to the response to BCUC IR 1.6.1.2. As noted, the FEU do not understand what is meant by 'financial stability risk.' The FEU consider it good utility practice to be granted an allowed ROE and capital structure that meets the fair return standard in compensating a utility relative to the risks faced by the specific utility on a standalone basis.

The FEU are not clear on the premise put forth by the question that 'regulatory support' is additional compensation to the shareholder. If the question is suggesting that an approval on the common rates and amalgamation application is 'regulatory support' that is additional shareholder compensation, then the response is no, for the reasons described in the response to BCUC IR 1.6.1.2. The application to adopt common rates and amalgamate the utilities is based on a number of benefits that have been detailed in the proceeding. The application is not premised on addressing a shareholder risk.

6.2 Is "spread[ing] fixed costs across a larger customer base" the <u>only</u> solution for FEVI to maintain financial stability? If so, please provide reasons and evidence to support this for both the short and long run.

Response:

The specific concern raised by the question of 'maintaining financial stability' is Moody's perspective with respect to the credit ratings of FEVI. In the context of Moody's concerns, they may also be addressed through changes that may improve the credit metrics that underpin the credit rating, such as a much thicker equity component and higher allowed return on equity. Such changes would reduce the risk to debenture holders but this would likely be a shorter term solution as overall rates may increase further from the higher cost of capital. Such solutions, while potentially addressing concerns regarding the credit ratings of FEVI, would not address the long term competitive pressures of FEVI, which are best addressed through amalgamation and adoption of common rates.

From the Companies' perspective, the FEU are not proposing amalgamation and common rates for the specific intent of addressing Moody's concern regarding the financial stability of FEVI. As stated in Section 6 of the Amalgamation Application, the "main principle behind amalgamation and common rates is one of fairness amongst all of FEU's customers.", as well as addressing the rate pressures facing FEVI's and FEW's customers.

The proposed amalgamation may not be the only solution to 'maintain financial stability'. However, in the absence of common rates, the FEU do not envision any solutions that would not require a significant rate increase at some point.

6.2.1 If not, please list all other solutions for FEVI to maintain financial stability for both the short and long run.

Response:

Please refer to the response to BCUC IR 1.6.2.

6.3 How could the balance in the RSDA account achieve financial stability and/or prevent rate shock for FEVI?

Response:

As stated in the Amalgamation proceeding Exhibit B-9 response to BCUC IR 1.92.1 the Companies provided analyses on a number of ways that the RSDA could be used. However none of the alternatives evaluated could get away from the significant increase in rates required once the RSDA was depleted.

> *If postage stamp rates are not approved and the RSDA is used to mitigate annual rate increases for FEVI, FEVI customers will experience rate increases in 2017, as well as 2018, once the RSDA is expected to be fully depleted and the impact of the loss of the royalty revenues is experienced. Specifically, FEVI estimates that sales customers will experience an approximate 11% burner tip increase in 2017 followed by a further approximate 13% burner tip increase in 2018.*

In addition, allocation of the RSDA balance is a short-term solution, and will not lead to the long term fairness and rate stability addressed by the adoption of postage stamp rates.

Please also refer to the response to BCUC IR 1.4.1.

6.4 Given that the FEU knew the royalty revenues would expire at the end of 2011, when it purchased FEVI, why is spread[ing] fixed costs across a larger customer base the preferred option to maintain financial stability?

Response:

Please refer to the response to BCUC IR 1.6.2. The FEU are not proposing to amalgamate and adopt common rates to address Moody's view of financial stability. Amalgamation and common rates proposal as noted in the original application is based on principle of fairness to all FEU customers, and addressing the rate pressures faced by FEVI and FEW.

6.4.1 What could the FEU have done in the years leading up to the expiration of the royalty revenue to promote financial stability in FEVI?

Response:

The FEU discussed its actions to manage the expiration of the royalty revenues of FEVI in the Amalgamation proceeding in its response to BCUC IR 1.20.2:

> *The FEU were aware of the business risk profile of FEVI when it was acquired and have managed the business risk over time as the utility has been maturing. This is demonstrated by items such as the elimination of the RDDA; the ongoing cost savings achieved as a result of a move to a common management structure; and the negotiation*

and agreement of long term contracts with key customers, e.g., BC Hydro and VIGJV. In addition, the RSDA has been introduced.

The FEU disagree that there is a transfer of risk from the shareholder under the common rates proposal. The regulatory compact that has been in place remains the same post-amalgamation.

The FEU believe they have proactively taken steps to address the loss of royalty revenues and manage the business risk in FEVI in the years leading up to the expiration of royalty revenues. The amalgamation proposal is the long-run, sustainable solution which addresses and manages the rate pressures faced by FEVI.

7.0 Reference: New Evidence of the FEU

Exhibit B-1, pp. 5-6; FEU 2012 Amalgamation Proceeding,

Exhibit B-9, BCUC 1.93.8

Moody's Report - Solutions for FEVI and FEW

The FEU states: "In its Decision, the Commission suggested that rate design could be a solution to the challenges faced by FEVI and FEW. The FEU, however, see no evidence that a rate design that allocates costs or sets rates on a different basis as among existing customers can effectively address the challenges that have been well documented in the evidence before the Commission, and further identified by Moody's. Rate design is not able to either reduce costs or increase demand in any material way, both of which would be a requirement to resolve FEVI's challenges (or FEW's). In the absence of amalgamation and the adoption of common rates or other material change in FEVI's circumstances, the long-term issues faced by FEVI will continue for the foreseeable future. The same can be equally said for FEW."

FEU states in BCUC 1.93.8 of the Original Application: "If postage stamp rates are not approved, the FEU intend to submit at a later date(s), rate designs for some or all of the individual entities. The rate designs for the individual entities may, among other things, include adjustments to the bill components such as the basic charge."

7.1 Is it FEU's position that the only option to address FEVI competition challenges is to decrease the overall FEVI rate level? Please explain.

Response:

The preamble to the question includes part of the FEU's response to BCUC IR 1.93.8. The FEU are not clear why this response has been included, but would like to clarify that there was no intention to imply that a change to the basic charge would do anything to address the issues faced by FEVI and FEW customers. The response merely indicated that a future rate design may include a change to the basic charge as one component.

The FEU believe that the only long term solution to the competitive challenge is to improve the rate comparison with the primary competitive energy source for space and water heating, which is BC Hydro. Absent BC Hydro foregoing postage stamp rates and adopting a regional structure that would increase BC Hydro rates relative to FEVI's, or a material increase to BC Hydro rates for other reasons, the FEU believe amalgamation and common rates is the best option to address the competitive challenges faced by FEVI.

7.1.1 Please explain how a utility can be an economic utility and yet not able to address competition challenges through rate design and/or deferral mechanisms.

Response:

FEVI has a competitive challenge due to its rates relative to BC Hydro, and this challenge will be exacerbated in the near term with the loss of royalty revenues and amortization of the RSDA. While rate design and deferral mechanisms can potentially address competitive issues, these are not permanent or long term solutions as they do not address the underlying reasons for the competitive challenges. Using rate design and deferral mechanisms solely for the purpose of addressing competition is likely to lead to a rate design that is no longer tied to the underlying cost basis. Moving further away from the underlying cost of service of various rate components would not reflect economic efficiency and would not be an improvement over the proposed postage stamped rates.

7.2 Please explain why FEU considers that, in the absence of amalgamation, the adoption of common rates or other material change in FEVI's circumstances, the long-term issues faced by FEVI will continue for the foreseeable future?

Please discuss in your response how this aligns with FEU's position in the Original Application, that significant new customer additions as a result of lower rates in FEVI and FEW may be limited, and that the FEU do not expect FEVI/FEW customers to be materially affected by the price increases in the short run.

Response:

With no significant forecast increase in throughput on their systems, the existing higher rates on Vancouver Island and Whistler are expected to continue. FEVI and FEW will continue to have a difficult time attracting new customers and may in fact lose customers and/or face reduced consumption levels per customer. Without significant growth on the system, the rates will not decrease and the competitive position of FEVI and FEW will not improve. In the event of a loss of load, the rates would need to be raised even more.

There is no inconsistency in the above summary with the FEU's position explained in Exhibit B-9, BCUC IR 1.81.7.1 in the original proceeding that significant new customer additions from the adoption of common rates may be limited. The FEU have not stated that the reason that the adoption of common rates will be a long term solution to the problems faced by FEVI and FEW is because it will result in significant customer additions. The common rates will, however, allow the amalgamated entity to retain existing customers and their associated demand, and allow for any cost of service increases that result from significant sustainment projects or loss of customers to be spread across a larger customer base. While the FEU is not forecasting significant load growth for FEVI and FEW as a result of common rates, it is likely that without common rates there will be a decline in consumption.

7.3 What "other material change in FEVI's circumstances" could resolve FEVI's long-term issues?

Response:

There are only two methods to resolve the challenges faced by FEVI. The first is to reduce costs, and the second is to increase revenues by adding additional throughput to reduce the unit costs.

FEI has taken steps to decrease costs through initiatives such as the Utilities Strategy Project (USP). The USP was a major restructuring initiative that combined the management and operating structures of the entities, resulting in substantial cost savings. This integration initiative essentially allowed FEU to realize the majority of the savings available.

FEVI has also attempted to increase revenues by increasing throughput on the system. Two of the most recent initiatives associated with increasing throughput include the Woodfibre LNG Project, although very preliminary, and the addition of LNG transportation customers via the Greenhouse Gas Reduction Regulation (GGRR).

To provide some context to the materiality of change that would be required, FEVI's residential rates would need to decrease by 38% to equal those of a Lower Mainland residential customer. To achieve a 38% reduction in FEVI's cost of service would require a reduction of over $77 million in the annual cost of service or a corresponding increase in revenues with no associated costs.

7.3.1 Is the development of the Woodfibre LNG plant or BC Ferries Conversion to LNG a material change of this nature?

Response:

The BC Ferries Conversion to LNG would not be material enough to resolve FEVI's challenges. As mentioned in the response to BCUC IR 1.4.1.2, FEVI is still in its early stages of feasibility analysis to develop capital cost estimates and to finalize firm contract demand to serve the Woodfibre LNG Plant. In the absence of developing financial and sales estimates related to this project, the FEU are unable to confirm whether the project to serve Woodfibre LNG Plant can be considered as a material change in FEVI's circumstances at this time. As discussed in the response to BCUC IR 1.7.3, a project would need to be significant to result in a reduction to the cost of service by the estimated $77 million required to achieve rate parity with FEI.

7.3.2 Does the proposed Woodfibre LNG plant indicate that economic investment in FEVI is not disadvantaged despite the lack of common rates?

Response:

No. The proposed projects such as Woodfibre LNG plant are site specific projects. There are not many sites in the Lower Mainland, including Vancouver Island, suitable for projects like Woodfibre LNG.

FEU believes that the Woodfibre LNG Project proponent is disadvantaged in the absence of amalgamation of the utilities. This is because amalgamation could potentially lower the transportation toll for Woodfibre LNG Project as the costs associated with this project will then be allocated to a larger customer base. Also, the net financial benefits in that case will flow to all FEU customers potentially reducing customer rates.

7.4 Is it FEU's position that financial forecasts presented in the original application now require material amendments and adjustments to take into account the fundamental change in facts and circumstances, which include significant increased sales revenues associated with FEVI's new customers/projects? Please explain.

Response:

FEVI's new project to serve Woodfibre LNG is in the preliminary phase as FEVI is in its early stages of feasibility analysis to develop a high level capital cost estimate for the project and to finalize the firm daily contract demand for the potential customer. The potential customer itself needs to complete its studies and make a decision to proceed with its small scale LNG export project at the Woodfibre site by end of Q4 2015.

After the Commission's decision on the FEU's application to amend Rate Schedule 16 into a permanent tariff, BC Ferries informed FEU that it would not pursue LNG as a viable alternative for their ferry fleet. However, just recently BC Ferries announced that it will order three new ferry vessels that will be dual fuel (capable of running on diesel and LNG) to replace vessels set to retire in 2016.[2] Despite BC Ferries' announcement to add LNG capable vessels to their fleet, this project is still in the preliminary stages and capital and load forecasts have yet to be developed.

Neither of these projects would provide benefits to FEVI customers prior to the proposed amalgamation date of January 1, 2015 and would therefore not change the rate impacts of amalgamation. Therefore the financial forecasts presented in the original application do not require material amendments and adjustments. In the context of an amalgamated entity, the projects would provide benefits to existing customers of FEI, FEVI and FEW.

In terms of customers for natural gas for transportation (NGT) applications, FEVI will be constructing a compressed natural gas (CNG) fueling station for Coldstar Freight Systems Inc. at FEVI's operations facility located in Langford. Coldstar has committed to consuming 15,000 GJs per year for a term of 5 years. Although this CNG fueling station will be constructed under the Greenhouse Gas Reduction Regulation and costs will be recovered from the customer, the benefit of higher throughput and delivery margin benefits will be flowed through back to all FEVI customers. FEVI does not consider this a material adjustment to the financial schedules and has therefore not updated them to reflect this project.

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2 http://www.theglobeandmail.com/news/british-columbia/new-bc-ferries-ships-will-be-fuelled-by-liquefied-natural-gas/article13383262/

8.0 Reference: New Evidence of the FEU

Exhibit B-1, p. 6

Updated Rate Impacts for FEI - Exclusion of FEFN

The FEU state: "As the Fort Nelson region has been excluded from the Reconsideration Application."

8.1 Please explain why the FEU are proposing to exclude Fort Nelson for the Reconsideration Application?

Response:

The FEU continue to believe that it would be appropriate to implement postage stamp rates across the FEU, including the Fort Nelson service territory. However, as explained on page 3 of the FEU's Reconsideration Application, the basis for the reconsideration relies in part on the section 53 amalgamation request which is not applicable to the Fort Nelson service area as it is already part of FEI. The FEU were also clear in the original proceeding that the FEU did not consider the exclusion of the Fort Nelson service area from the postage stamp rate proposal as a barrier to otherwise proceeding with amalgamation and postage stamp rates.

8.1.1 Does exclusion of Fort Nelson indicate that the FEU sees merit in regional rates? Please explain.

Response:

No. Please refer to the response to BCUC IR 1.8.1.

9.0 Reference: New Evidence of the FEU

Exhibit B-1, p. 7; FEU 2012 Amalgamation Proceeding, Exhibit B-15, BCUC 2.44.2

Updated Rate Impacts for FEI – Rate Impact

Table 1: Incremental Annual Bill Impacts for Lower Mainland Residential Customers

	2015	2016	2017	2018	Total
FEI Forecast 2014-2018 Rate Change under PBR	0.9%	1.1%	0.5%	1.5%	4.0%
Rate Change under RSDA Allocation Period	1.3%	1.3%	1.3%	1.3%	5.3%
Total Incremental Rate Change	2.2%	2.4%	1.9%	2.8%	9.4%

FEU states in BCUC 2.44.1 of the Original Proceeding: "customer preferences may not be very useful in evaluating benefits if they are simply a "yes" or "no" to postage stamp rates. Rate design choices inevitably lead to different impacts to different customer groups, and each customer group will tend to prefer options where they believe they are getting a benefit regardless of other factors. Taking customer preferences as determinative would lead to a situation where no rate design is acceptable or rate design is determined by the majority."

9.1 Please explain what meaningful impact, if any, the updated rate information would have had on: (i) the Commission's Bonbright evaluation of the FEU common rates request (please identify the specific Bonbright principle affected; and (ii) the FEU request to amalgamate if common rates were approved.

<u>Response:</u>

Since the rate impacts have changed since the record was closed in the original proceeding, the FEU have updated the analysis so that the Commission can base its determination in this proceeding on more recent information. In the FEU's submission, the updated rate impact analysis shows that the impact of postage stamp rates on FEI customers is reasonable. Further, given the low increases forecast over the PBR period, the impact of postage stamp rates over the four final years of PBR would be well timed. As noted by the Ministry, the low cost of gas at this time also makes this an opportune time to implement postage stamp rates.

Given that the paramount concern of the Commission in its Decision appears to have been the impact of postage stamp rates on FEI customers, the FEU submit that the reasonableness of the rate impact should have a meaningful impact on the Commission's Bonbright analysis and the Commission's consideration of whether amalgamation to implement postage stamp rates is in the public interest. Namely, given the benefits from amalgamation and postage stamp rates, the reasonableness of the impact should reinforce that amalgamation and postage stamp rates are just and reasonable and not unduly discriminatory.

9.1.1 Does FEU consider that: (i) the updated rate information would change customer preferences regarding the postage stamp proposal; and (ii) that customer preferences should be a material consideration in a Bonbright rate design evaluation.

Response:

The FEU have not provided any new evidence regarding customer preferences or any evidence suggesting that the updated rate information would change customer preferences.

At the request of the Commission, the FEU did carry out a substantial stakeholder engagement process regarding its proposal to amalgamate and implement postage stamp rates, the results of which have been described in section 10 of the FEU's original Application (Exhibit B-3 in the original proceeding). The Commission had previously stressed the importance of consulting with its customers regarding postage stamp rates in the BC Gas 1992 Revenue Requirement Decision (Exhibit A2-1, p. 20, in the original proceeding).

In its Decision on the amalgamation of the FEU, the Commission considered customer preferences under the Bonbright principle of Customer Understanding and Acceptance, concluding in part on page 26 that the opposition to the FEU's application indicated a reduced level of customer acceptance. The FEU have submitted in their Reconsideration Application (pp. 31-32) that this is an error of fact. The FEU submit that the extent of FEI customer support for postage stamp rates, despite the recognition that FEI rates would increase as a result, was a notable fact that should have been considered and given weight by the Commission and that the only reasonable conclusion on the evidence was that postage stamp rates would improve customer understanding and acceptance.

9.2 Please update evidence filed in the original proceeding on revenue to cost ratios that occur under the status quo versus common rates (Exhibit B-15, BCUC 2.59.9) for FEVI and FEW.

Response:

As explained in the original response, the revenue to cost ratios provided in BCUC IR 2.59.9 are not meaningful or appropriate as they compare revenues and costs developed under very different circumstances.

The revenue to cost ratios provided in the response to BCUC IR 2.59.9 reflect the 2013 test year and as such will not change as a result of the expected rate impacts for 2015 to 2018. Cost of service studies are completed in the context of proposed rate design and are not updated every year to reflect changes in the revenue requirement. Assuming that revenue requirements increase uniformly across all rate base and expense items, revenue to cost ratios would also correspondingly remain unchanged.

10.0 Reference: New Evidence of the FEU

Other

10.1 Please clarify if FEU believes a basic principle of the decision had not been raised in the original proceeding. If so, please explain how this principle is not consistent with the framework of Bonbright and the 1992 BC Gas decision?

<u>Response:</u>

The FEU assume that the question is referring to the ground for reconsideration advanced by the CEC that the Commission has effectively put forward a new principle which "appears to be a determination that cost causation makes postage stamp rates unfair when a difference in a regional cost or cross subsidization is significant but with no determination as to the relevant threshold" (Exhibit C1-2, p.2).

The FEU's view is that the Commission has not put forward a new principle, but has applied the principle of cost causation in a way that is inconsistent with the Commission's application of the Bonbright framework in its previous decisions. The Commission's previous decisions include its continued approval of postage stamp rates such as for BC Hydro and FEI, and its determinations on the Chetwynd Complaint (Letter No. L-24-04) and the Big White Rate Design (BCUC Order G-87-07) (see Tabs 1 and 3, respectively, of the FEU's Book of Authorities for its Final Argument in the original proceeding).

The FEU assume that the reference to the "1992 BC Gas decision" in the question is a reference to the B.C. Gas Utilities Ltd., 1993 Phase B Rate Decision (Exhibit A2-2 in the original proceeding). The *de facto* effect of the 1993 BC Gas Decision was to postage stamp delivery rates for the Lower Mainland, Columbia and Inland service areas, despite cost differences amongst the regions. Accordingly, the FEU do not believe that the application of the cost causation principle by the Commission in its Decision is consistent with the 1993 BC Gas Decision.

10.2 Does FEU believe it possible that the: (i) application of the *Utilities Commission Act* (UCA); and (ii) regulatory principles of rate design, may result in rate policies that are not consistent with government policy?

<u>Response:</u>

The FEU believe it is possible. However, neither the *Utilities Commission Act* nor regulatory principles of rate design result in rate policies that are inconsistent with the government policy in favour of postage stamp rates.

10.3 If regulatory policies determined applying the UCA and generally accepted regulatory theory are inconsistent with government policy, what role (if any) does FEU believe that the Commission has in bridging the two policies?

Response:

The question is hypothetical because the FEU are not aware of any regulatory policies or generally accepted regulatory theories that are inconsistent with the government policy in favour of postage stamp rates. This Commission and regulators across Canada have approved postage stamp rates and postage stamp rates are in fact the most common rate design for gas and electric utilities in North America generally. On this basis, the FEU believes that regulatory policy and generally accepted regulatory theories support government policy in favour of postage stamp rates.

10.4 Please provide all available correspondence made between FEU and each party requesting support for the Reconsideration to the extent that the communication relates to this application.

Response:

The FEU respectfully decline to provide the requested correspondence for the following reasons.

First, the documents requested are irrelevant to the determination of the merits of the Reconsideration Application. In the Reconsideration Application, the FEU argued three main grounds to reconsider and vary Order G-26-13. The documents requested are not relevant to these grounds, as they have no bearing on the alleged errors or whether the Commission should reconsider and vary Order G-26-13. For example, no communication between the FEU and a supporting party could change whether the Commission made a legal or factual error in Order G-26-13.

Second, some of the documents are also subject to common interest privilege, as they are documents prepared for the purpose of litigation (i.e. this regulatory proceeding) and have been shared with a party with a common interest in the proceeding. The FEU and a number of other parties, including government, share a common interest in opposing the Commission's Decision denying amalgamation and common rates for the FEU. As a result, the FEU have cooperated to an extent with these other parties and each party has filed its position in the proceeding for the Commission's consideration.

Third, the FEU, before filing a regulatory application for a project or program, often discuss the project or program with key stakeholders. The FEU and the stakeholders should be free to communicate without the worry that their communications will become part of a regulatory proceeding. Their ability to freely discuss issues in confidence is a vital aspect of a fair and efficient regulatory process.

11.0 Reference: Application for Reconsideration and Variance of G-26-13, dated April 26, 2013

Errors in Law and Fact

Within FEU's Application for Reconsideration, FEU takes the position that 3 errors of law have been made.

11.1 For each of FEU's 3 proposed errors in law, please indicate if FEU is of the position that each of these errors is material, individually, to the Commission's decision applying the framework of Bonbright as included in the Decision. Please explain your response.

Response:

The significance of each of the three interrelated legal errors is explained in the FEU's Reconsideration Application. The FEU believe that these legal errors are material on an individual basis to the Commission's Decision. The impact of these legal errors is not limited to the application of the Bonbright framework in the Decision. However, the material impact of each legal error on the Bonbright framework as applied in the Decision is as follows. As the errors are interrelated, there is some overlap.

1. *Failure to Consider Postage Stamp Rates within the Context of an Amalgamated Entity*. As the FEU have submitted, the Commission was incorrect to analyze postage stamp rates within the context of three separate utilities. There were three effects of this error. The first effect of this error was that it led the Commission to avoid the consideration of whether amalgamation for the purpose of implementation of postage stamp rates was beneficial in the public interest. The Commission therefore failed to consider the various public interest and other factors in favour of amalgamation and postage stamp rates. This is discussed further below. The second effect was that the Commission focused on rate impacts as an inter-utility matter, whereas within an amalgamated entity the adoption of postage stamp rates is an intra-utility issue. The FEU submit that this contributed to the Commission's incorrect approach of using the existing rates as the measure by which the rates for the amalgamated entity should be judged, as discussed below, and contributed to the Commission's incorrect conclusion that postage stamp rates caused a cross subsidy. A third effect is that the Commission did not consider the extent to which amalgamation itself contributed to the rationale for adopting postage stamp rates. Amalgamation would reflect the high degree of physical and operational integration of the FEU. In the FEU's submission, postage stamp rates are more appropriate within an amalgamated entity. Within this context, the Commission should have considered the Bonbright principles as they related to postage stamp rates for an amalgamated utility that was fully integrated. The concept of regional rates for an amalgamated utility in that case would need to be considered in terms of both regulatory

precedent and Bonbright principles on a general basis first, followed by an examination of the most appropriate regions. Assuming the existing regions are appropriate simply on the basis of past ownership does not adequately reflect the principles of cost causation.

2. *Reliance on Fact that Existing Rates are Approved*. As the FEU have submitted, the way in which the Commission relied on the fact that existing rates were approved was in error. One result of the Commission's approach is that it did not acknowledge that the existing rates were a problem. This resulted in the Commission failing to fully consider the challenges facing FEVI and FEW and the benefits of postage stamp rates for resolving those challenges. A second result is that it precluded a full consideration of whether postage stamp rates could be just and reasonable and not unduly discriminatory for an amalgamated entity. The Commission incorrectly treated existing rates as the measure of cost-causation and movements away from approved rates as being movement away from cost causation. This is a fundamentally incorrect approach. Amalgamation opened up the possibility of allocating costs across the service areas of the FEU on a postage stamp basis. The rate changes resulting from the move to postage stamp rates reflect the removal of rate differences based on location and the reallocation of costs based on rate class. Movement away from the existing approved rates is not reason in itself to conclude that rates are not based on cost causation. The proposed rates themselves have to be considered on their own terms to consider whether they are based on cost causation. As the FEU have submitted, postage stamp rates have been repeatedly found to be consistent with Bonbright principles.

3. *Did not Consider Factors Relevant to the Public Interest*. As the FEU have submitted, the approach taken in the Decision foreclosed consideration of factors relevant to the public interest. In other words, the FEU submit that the Commission's Bonbright analysis was legally insufficient to dispose of the FEU's application. The Commission cannot confine itself to a list of rate design factors which has the effect of excluding from consideration key public interest factors that are relevant to a public interest determination regarding amalgamation. Further, because public interest factors do have an impact on several of the Bonbright principles, including the customer impact and the customer's own view on fairness, they should have been taken into account in that context. Had the Commission considered the public interest factors as set out on pages 19 to 24 of the FEU's Reconsideration Application, the FEU submit that the Commission should have concluded that the benefits of amalgamation and postage stamp rates outweigh any negative rate impacts to FEI customers and should be approved.

The FEU submit that the effect of these errors is that the Commission did not appropriately consider the FEU's proposal to amalgamate and implement postage stamp rates. If it had, the FEU submit that the conclusion would be that amalgamation and postage stamp rates are in the public interest and that postage stamp rates result in a fair and accepted approach to cost allocation that offers a number of important benefits, including the resolution of the long-term challenges facing FEVI and FEW.

11.2 Had the Commission Panel approved the amalgamation, but denied postage stamp rates, was it FEU's intent to proceed with the amalgamation despite indicating otherwise in the original application? If not, what other value or usage might this approval have for FEU?

Response:

No. Please refer to the response to BCUC IR 1.11.3.

11.3 Had the Commission Panel concluded that amalgamation should proceed but denied the usage of postage stamp rates, does FEU believe that the Commission Panel could have dismissed the entire application given that FEU requested amalgamation only if postage stamp rates were approved?

Response:

Yes.

11.4 Given that FEU made a request for amalgamation on the condition that postage stamp rates were approved, is it not possible to evaluate and decide on the precondition before proceeding to evaluate the rest of the application? If not, please explain how the outcome would vary if the postage stamp rates was not approved?

Response:

As stated in the FEU's original Application, the FEU sought amalgamation in order to implement postage stamp rates because amalgamation is a precondition to implementing postage stamp rates. The FEU have explained in Part V of its Reconsideration Application why it is not possible to evaluate postage stamp rates before evaluating amalgamation or at least assuming an amalgamated entity. If amalgamation was assumed for the purpose of the analysis of postage stamp rates, the Commission should have considered rate impacts as an intra-utility matter, should not have relied on the approval of existing rates in a manner which foreclosed full consideration of the appropriateness of postage stamp rates and should have considered the various public interest factors in favour of postage stamp rates, rather than limiting its analysis to Bonbright principles.

11.5 Does FEU believe that the review of the amalgamation application should have re-evaluated existing rates of FEU (including underlying cost data) considering that existing rates were a viable alternative to the proposed postage stamp rates? If so, why wasn't this information included as part of the original application for amalgamation?

Response:

No, the FEU do not see any need to reevaluate the existing rates of the FEU in the context of the postage stamp rate proposal. Please refer to the response to BCUC IR 1.11.6.

11.6 Were existing rates a possible alternative to postage stamp rates presented in the original application?

Response:

Yes, the existing rates for the existing separate utilities were an alternative to the proposal to amalgamate and implement postage stamp rates.

11.7 What, if any, significant facts and circumstances have changed since the last FEU revenue requirement proceeding that may have a material impact on existing rates of the current standalone entities? Clarify if it is it FEU's position that these facts and circumstances indicate that further regulatory process is needed to address the existing rates of the current standalone entities given postage stamp rates were not approved?

Response:

Please refer to the response to BCUC IR 1.11.5 and 1.11.6. Respectfully, the FEU do not understand the intent of this question and do not believe it is relevant to this proceeding. A reevaluation of existing rates would not have any impact on the issues before the Commission in this proceeding. The proposal is based on taking the approved revenue requirements and adjusting for the impact of amalgamation to determine the postage stamp rates, and therefore, there is no need to examine existing rates. In the context of a denial of this reconsideration, the rates and revenue requirements for the existing separate utilities will be addressed in their respective revenue requirements applications.

11.8 By making the amalgamation application, which included a request for postage stamp rates, does FEU believe that previously approved rates are somehow rendered non-viable for regulatory purposes? If so, please explain how this aligns with the current regulatory process of maintaining previously approved rates until a new Commission determination either approves interim or new rates.

Response:

No. The postage stamp rates reflect the appropriate and reasonable rates for the amalgamated utility. The existing rates reflect the rates for three separate utilities. Therefore, both sets of rates are viable, reflecting their specific situation.

11.9 Given that the amalgamation application is not approved, is it not reasonable for FEU to continue to apply previously approved rates?

Response:

Yes.

11.10 Had postage stamp rates been considered in a context of amalgamation, please elaborate on how the FEU believes the regulatory evaluation for postage stamp rates (using the framework in the decision) would have changed.

Response:

If the Commission had considered postage stamp rates in the context of amalgamation, the FEU submit that the Commission would not have used the framework that it applied in the Decision. Please also refer to the responses to BCUC IR 1.11.1 and 1.11.4.

11.11 Had postage stamp rates been considered in a context of amalgamation, please explain if any cost or cross-subsidization amounts used in the regulatory evaluation for postage stamp rates would have changed.

Response:

The FEU understand that the Commission's regulatory evaluation was to compare existing rates to the proposed postage stamp rates. If postage stamp rates had been considered in the context of an amalgamated entity, this comparison would not change. However, the FEU do not agree that a move away from existing rates means that the proposed postage stamp rates are not cost-based or result in cross-subsidization. Postage stamp rates do not allocate costs based on location, but still allocate costs to each rate class in accordance with the principle of cost causation.

11.12 Please confirm that in BC we do have utilities, other than FEU, that do apply regional rates.

Response:

To the Companies' knowledge, other than FEI which has a regional rate for the approximately 2,500 customers in Fort Nelson, Pacific Northern Gas (including Pacific Northern Gas (N.E.) Ltd. and Pacific Northern Gas Ltd.) is the only utility that applies regional rates. Attachment 11.12, which is an excerpt from the 2012 BCUC Annual Report, shows on page 21 that in 2011 Pacific Northern Gas served 39,575 customers or approximately 4% of the total of 998,764 gas customers in the province.

To the FEU's knowledge, all other gas utilities and all electric utilities in BC have postage stamp rates within their respective service territories.

In its letter, the FEU also asserts that the Commission made a number of errors in fact.

11.13 Does FEU believe that any of the proposed errors in fact are material on a standalone basis? Please explain.

Response:

Yes. As stated in paragraph 75 of the Reconsideration Application, the FEU submit that the errors of fact, both individually and collectively, were material to the Commission's analysis. The FEU have explained each error of fact in its Reconsideration Application.

11.14 For each proposed error in fact that FEU believes to be material to the overall Decision, identify which regulatory frame-work consideration (from the Bonbright model applied in the Decision), would be impacted by the proposed error in fact, and then include an evaluation of how FEU believes this proposed error in fact would modify the evaluation.

Response:

The FEU have discussed each error of fact in its Reconsideration Application. In addition to the errors of fact identified in Part IX of its Reconsideration Application, the FEU also consider here the error of fact related to cost savings and regulatory efficiencies identified and discussed on pages 21 to 23 of the FEU's Reconsideration Application.

While the impact of the errors is not confined solely to the Bonbright analysis, the impact of each of the errors of fact on the Bonbright model applied in the Decision is as follows:

1. *Cost Savings are Material and Flow from Postage Stamp Rates*. While the FEU have been conservative in their estimate of potential cost savings and are unable to put an exact dollar amount on all savings, the savings are in the millions of dollars annually. In the FEU's view, this is a material amount that customers would be interested in saving. The Commission understated the potential cost savings ("modest at best") and incorrectly attributed the cost savings to amalgamation despite clear evidence to the contrary. The FEU also submit that it was an error to disregard savings attributable to amalgamation alone in any case. (See paragraphs 59 to 63 of the FEU's Reconsideration Application.) The Bonbright principles that this error impacts are as follows:

    a. *Practical and Cost Effective to Implement*. The Commission appears to have concluded at page 27 that postage stamp rates had no benefits weighing in favour of them when compared to existing rates. The cost savings flowing from postage stamp rates, however, should have been an overriding factor that showed that postage stamp rates are more practical and cost effective to implement than regional rates. In addition to the fact that it simply costs millions of dollars less to implement and maintain postage stamp rates, postage stamp rates are more simple than the current array of regional rate structures. In the FEU's submission, there is no evidence on which the Commission could reasonably conclude that the existing rates are either more practical or more cost effective to implement than postage stamp rates.

b. *Customer Understanding and Acceptance.* The fact that postage stamp rates are more practical and cost-effective to implement would contribute to customer understanding and acceptance.

c. *Rate Stability*. The costs savings and efficiencies flowing from postage stamp rates would have helped manage customer rate impacts.

2. *The FEU are already operationally integrated.* As the FEU have submitted, the Decision was premised on the assumption that there is a much lower degree of integration among the FEU than currently exists. There is in fact a very high degree of integration amongst the FEU, as the original evidence showed and the FEU's new evidence now more fully demonstrates. The Bonbright principles that this error impacts are as follows:

a. *Fairness* and *Avoidance of Undue Discrimination*. The high degree of integration of the FEU should have contributed to the Commission's consideration of the fairness principle and been a factor weighing in favour of postage stamp rates. Because of the high level of integration of the utilities both in terms of infrastructure and operations, it is difficult to definitively assign costs to the respective utilities. The Shared Services Agreement allocates those shared costs in a similar manner as common costs are allocated among customer classes within a cost of service study. Because of the integration, certain facilities and costs are incurred by all customers on the system, regardless of which utility they are served by. There is an inherent amount of uncertainty associated with the allocation of costs under the Shared Services Agreement, just as there is between customer classes within a cost of service study. To ignore this shared use and uncertainty by treating the costs assigned to each utility as an exact amount to be balanced with revenues does not accurately reflect the true nature and apportionment of the costs. As indicated in EES Consulting's evidence, postage stamp rates would simplify the sharing of costs and removes the potential for contention in allocating those costs.[3] The high degree of integration also means that all customers, wherever they are located, are receiving the same service from the same system from (in effect) the same utility and therefore should pay the same rate on a class-by-class basis. The FEU submit that the

[3] Exhibit B-3-1, Appendix D-1, EES Consulting, "Natural Gas Cost of Service Review," pp. 6-7.

level of integration is a significant factor in favour of concluding that postage stamp rates are fair and avoid undue discrimination.

b. *Customer Understanding and Acceptance*. This error explicitly came into play in the Commission's consideration of Customer Understanding and Acceptance, as the Commission found that customer understanding may be lost due to postage stamp rates because of "the significance of regional differences". The FEU submit that the high degree of integration that actually exists should have been considered as a factor that weighed *against* maintaining regional differences and supported the conclusion that customer understanding and acceptance would have improved due to postage stamp rates.

c. *Practical and Cost Effective to Implement*. The high degree of integration should have led to the conclusion that postage stamp rates were more practical and cost-effective to implement than existing rates. As noted above, because of the existing level of integration, the existing rates require allocation of many costs. Postage stamp rates would remove the need for such allocations and are simpler by any measure.

3. *Customer Support for Amalgamation and Postage Stamp Rates.* The FEU have discussed the extent of customer support for amalgamation and postage stamp rates at pages 31 to 32 of the Reconsideration Application. As submitted by the FEU, the extent of FEI customers' support for the Application, despite recognition that FEI rates would increase as a result, was a notable fact that should have been considered and given weight. The Bonbright principles impacted by this error are discussed below.

a. *Customer Understanding and Acceptance*. This error explicitly came into play in the Commission's consideration of Customer Understanding and Acceptance, as the Commission based its conclusion on the erroneous conclusion that FEI customers generally oppose postage stamp rates. The FEU submit that the level of support in fact should have led to the opposite conclusion, that postage stamp rates would have increased customer understanding and acceptance.

b. *Fairness* and *Avoidance of Undue Discrimination*. The FEU are also concerned that the Commission's apparent belief that customers were opposed to postage stamp rates inappropriately coloured the Commission's conclusions on the principles of fairness and avoidance of undue discrimination. The extent of customer support for postage stamp is evidence that customers in fact believe that postage stamp rates is a fair approach despite regional differences. The level of support from customers, despite rate impacts, is a therefore a factor that should have been weighed in favour of concluding that postage stamp rates are fair.

4. *Customer Understanding and Acceptance.* Based on the two errors above and the evidence on the record, the FEU submit that it was an error of fact to conclude that customer understanding and acceptance would decrease as a result of postage stamp rates. The fact that postage stamp rates improved customers' understanding and acceptance should have weighed in favour of approving postage stamp rates.

5. *Regional Rates are not More Beneficial.* The FEU have identified several instances in the Decision where the Commission incorrectly relied on apparent benefits of regional rates over postage stamp rates. The FEU submit that by overstating the apparent benefits of regional rates, the Commission discounted the challenges faced by FEVI and FEW and failed to take into account key benefits of postage stamp rates that the Commission was legally required to consider. In particular, the Commission incorrectly concluded that regional rates were more effective at resolving the challenges of FEVI, when one of the key benefits of postage stamp rates was in fact a long term resolution to these challenges. While the overall impact of these errors is therefore not confined to the Commission's Bonbright analysis, the FEU describe the impact of these errors on the Bonbright principles below.

   a. *Fairness* and *Avoidance of Undue Discrimination.* In the context of its discussion of the principle of fairness, the Commission incorrectly concluded that a region-specific rate design can more readily address low consumption and the use of high-carbon fuels. The number of low consumption customers in FEVI, compared to FEI, should have been a factor in favour of postage stamp rates because postage stamp rates would provide more flexibility in addressing the issue and would allow all low-consumption customers in the FEU's service areas to be treated the same. The use of alternative high carbon heating fuels on FEVI is simply not a factor in favour of regional rates. There is in fact no evidence that regional rates are beneficial in treating any regional differences. This demonstrates that in fact the similarity of the regions is the overriding consideration and weighs in favour of postage stamp rates.

   b. *Efficiency.* The Commission erroneously concluded that efficiency can be better improved through regional rate designs. For the reasons discussed on pages 36 to 38 the Reconsideration Application, as well as the FEU's submissions related to energy choices, cost savings and regulatory efficiencies and government energy policy discussed on pages 20 to 24, the

FEU submit that postage stamp rates have many advantages over regional rate design from an efficiency perspective.

c. *Rate Stability.* The Commission appears to have accepted the benefits of rate stability, but concluded that regional rates were the more appropriate mechanism to address rate stability issues. As the FEU have submitted, there is no evidence on which to reasonably conclude that regional rate mechanisms will resolve the rate stability challenges of FEVI and FEW. In the FEU's submission, the Commission should have concluded that from a rate stability perspective, postage stamp rates were clearly preferable.

11.15 Does FEU believe that any of the proposed errors in fact are material on an aggregate basis? Please explain which proposed errors combine together to have a material combined impact.

Response:

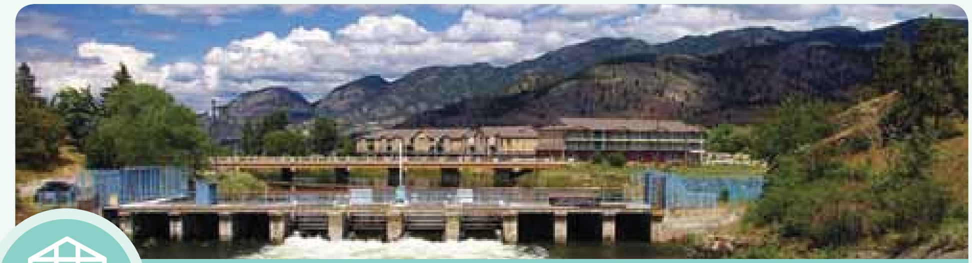
Please refer to the response to BCUC IR 1.11.13.

11.16 For any grouping of proposed errors in fact which together are believed to have a material impact on the Decision, identify which regulatory frame-work consideration (from the Bonbright model applied in the Decision) would be impacted by these proposed errors in fact, and then include an evaluation of how FEU believes these proposed errors in fact, would modify this evaluation.

Response:

Please refer to the response to BCUC IR 1.11.14.

Attachment 11.12



Electricity Sales 2011

	Customers (#)	Revenue ($000)	Sales (GW.h)
Crown-Owned Electric Utility			
BC Hydro and Power Authority	1,867,327	3,409,186	49,841
Municipally-Owned Electric Utilities			
City of Grand Forks	2,129	3,770	37.36
City of Kelowna	14,789	31,234	323.2
City of Nelson (urban)	5,729	7,715	93.64
City of Nelson (rural)	4,089	5,302	64.58
City of New Westminster	32,211	33,680	431.00
City of Penticton	17,055	31,170	328
District of Summerland	5,466	9,791	94
Total Municipally-Owned	**81,468**	**122,662**	**1,371.78**
Investor-Owned Electric Utilities			
FortisBC Inc.	113,254	218,640	2,247
Hemlock Utility Services Ltd.	238	257	1.49
Silversmith Light & Power Corporation	11	34	0.08
Corix Multi-Utility Services Inc.			
CMUS – Sun Rivers & Sonoma Pines	1,041	1,155	14.10
The Yukon Electrical Company Limited			
Lower Post BC	1	242	0.6
Total Investor-Owned	**114,545**	**477,322**	**2,263.27**
Total All Electrical Utilities	**2,063,340**	**3,752,176**	**53,476**

Electricity Notes

1. 1 gigawatt hour (GW.h) = 1 million kilowatt hours.
2. Figures reported are for the 2011 calendar year. Customers reported are as at December 31, 2011.
3. Revenues and sales for BC Hydro and FortisBC Inc. are net of sales to other reporting electrical utilities identified in this table.

Natural Gas Sales 2011

	Customers (#)	Revenue ($000)	Sales (GJ)
Investor-Owned Natural Gas Utilities			
FortisBC Energy Inc.			
Lower Mainland Division	591,964	984,790	123,739
Inland Division	232,901	290,639	48,966
Columbia Division	22,799	31,521	9,495
Fort Nelson Division	2,435	4,499	621
Revelstoke	1,562	4,387	220
FortisBC Energy (Vancouver Island) Inc.			
Vancouver Island, Powell River and Sunshine Coast areas	102,104	205,410	19,748
FortisBC Energy (Whistler) Inc.	2,649	12,176	737
Pacific Northern Gas (N.E.) Ltd.			
Fort St. John Inc./Dawson Creek Division	17,807	26,726	4,246
Tumbler Ridge Division	1,198	1,390	1,040
Pacific Northern Gas Ltd. (includes Granisle Grid)	20,570	43,146	4,122
Corix Multi-Utility Services Inc.			
Sun Rivers, Sonoma Pines	778	373	28
CMUS - Panorama	210	943	36
CalGas Inc. – Kickinghorse	13	372	20
CalGas Inc. – Canyon Ridge	23	20	1
Big White Gas Utility Ltd.	353	1,041	41
Port Alice Gas Inc.	248	429	13
Sun Peaks Utilities Co. Ltd.	884	1,900	79
Stargas Utilities Ltd.	266	249	38
Total All Gas Utilities	**998,764**	**1,610,011**	**213,190**

Gas Notes

1. 1 gigajoule (GJ) is approximately equivalent to 0.910 mcf (mcf = one thousand cubic feet) or 0.0258 $10^3 m^3$ of natural gas or 0.376 mcf of propane vapour in L.P. gas grid systems.
2. Figures reported are for the 2011 calendar year. Customers reported are as at December 31, 2011.
3. Sales of GJ shown include sales to end-use customers plus gas owned by customers and transported to their industrial operations by utilities.
4. Revenues reported for natural gas utilities include only transportation margins for large industrial customers who have purchased gas supplies directly from producers or aggregators.