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September 17, 2013

Via Email
Original via Mail

British Columbia Public Interest Advocacy Centre
Suite 209 – 1090 West Pender Street
Vancouver, B.C.
V6E 2N7

Attention: Ms. Tannis Braithwaite, Acting Executive Director

Dear Ms. Braithwaite:

Re: British Columbia Utilities Commission (BCUC or the Commission) Generic Cost of Capital (GCOC) Proceeding – Stage 2
FortisBC Inc. (FBC) Response to the British Columbia Public Interest Advocacy Centre on behalf of the British Columbia Pensioners' and Seniors' Organization et al (BCPSO) Information Request (IR) No. 2

In accordance with the Regulatory Timetable set out for Stage 2 of the GCOC proceeding by Commission Order G-77-13, FBC respectfully submits the attached response to BCPSO IR No. 2.

If further information is required, please contact the undersigned.

Sincerely,

FORTISBC INC.

Original signed:

Dennis Swanson

Attachments

cc: Commission Secretary
Registered Parties (email only)



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1 **1.0 Reference: BCPSPO 1.4.2**

2 1.1 When did the EPA with BC Hydro come into effect?

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4 **Response:**

5 A redacted version of the EPA is attached as Appendix E to Exhibit C13-7 in the Company's
6 2009 Rate Design Application process. The document indicates an effective date of January
7 27, 2009.

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11 1.2 Given Celgar is required to “self-supply” (under its EPA with BC Hydro) the first
12 40 MW of its requirements and BC Hydro supplies the load in excess of 40 MW
13 (when required by Celgar), under what conditions has FortisBC supplied Celgar
14 now that the EPA is in effect?

15
16 **Response:**

17 FortisBC supplies Celgar when its generation is below 40 MW and insufficient to meet mill load,
18 or when its generation is offline.

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1 **2.0 Reference: BCUC 1.9.5 and BCUC 1.9.7**

2 2.1 Please confirm that the \$41.9 M in Wholesale class revenue (per BCUC 1.9.5) is
3 meant to cover commodity as well as delivery (i.e. transmission) costs.

4
5 **Response:**

6 Confirmed. The revenue projection contains charges for Demand, Energy, and the fixed
7 Customer Charges.

8
9

10
11 2.2 Please confirm that accompanying the reduction in revenue identified in BCUC
12 1.9.7 would be a reduction in purchase power costs which would also be
13 recorded in FortisBC's deferral accounts.

14
15 **Response:**

16 Confirmed. The \$32 million reduction in revenue, which results in a substantial rate increase of
17 approximately 5 percent, takes into account the reduction in power purchase costs.

18



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1 **3.0 Reference: BCUC 1.9.7 and BCU 1.11.9**

2 3.1 Please check/confirm the references in both responses to Exhibit B1-74,
3 Appendix B.

4
5 **Response:**

6 The references in response to BCUC FBC IR 1.9.7 and 1.11.9 of Exhibit B1-74, Appendix B
7 should be to Exhibit B1-72, Appendix B.

8



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1 **4.0 Reference: BCUC 1.15.2**

2 4.1 To the Company's knowledge, how many residences have installed air source
3 heat pumps since 1999? How many in the last 5 years?

4
5 **Response:**

6 There have been 6,339 projects registered in the ASHP program to-date, of which 2,037 were
7 enrolled in the last five years. This is a lower bound estimate as some projects have multiple
8 units in their data-base entry. FBC's recent residential end-use survey indicates 6.9% of
9 respondents use an ASHP as their main type of heat, which increases the ASHP count to about
10 9,000.

11



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1 **5.0 Reference: BCUC 1.14.4, BCUC 1.14.5 and BCUC 1.16.1**

2 **ICG 11 b)**

3 5.1 Based on these responses, it would appear that the of risk BC Hydro
4 experiencing high rate increases in the future (i.e. higher than FortisBC's other
5 cost increases) both increases FortisBC business risk (i.e. leads to higher overall
6 cost increases for FortisBC) and decreases FortisBC's business risk as it will
7 reduce the differential between BC Hydro's and FortisBC's rates. On net, does
8 FortisBC view the prospect of higher rate increases for BC Hydro (relative to
9 FortisBC) as having a favourable or unfavourable impact on its business risk?

10
11 **Response:**

12 It is difficult to assess the net impact on the business risk of FBC from BC Hydro rate increases,
13 as the rate increases present risks to different aspects of FBC's business risk. For instance, as
14 described in BCUC FBC IRs 1.14.4, 1.14.5 and 1.16.1, BC Hydro rate increases also impact
15 FBC's rates through higher power supply costs. As a result, over the short to medium term it is
16 likely that BC Hydro's rates will still be lower than FBCs, therefore moderating any change in the
17 competitive risk relative to BC Hydro rate increases. Over the longer term, BC Hydro increases,
18 if significant enough, will result in BC Hydro rates equivalent to or higher than FBC rates and
19 therefore, BC Hydro increases would reduce the competitive risk to FBC. However, as noted,
20 BC Hydro increases put further pressure on FBC rates, and could result in a greater overall
21 business risk if FBC becomes less competitive relative to competing energy forms such as
22 natural gas or alternative energy. To the extent that the primary competition is against such
23 competing energy forms as opposed to solely BC Hydro, the rate increases from BC Hydro, on
24 a net basis may be more likely to increase business risk.

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1 **6.0 Reference: BCUC 1.16.5**

2 6.1 Please comment on the in volatility over the past 5 years in FEI's overall prices
3 charged its customers (i.e. customers that use commodity supplied by the utility)
4 relative to the price volatility experienced by FortisBC's customers.
5

6 **Response:**

7 The referenced response to BCUC 1.16.5, discusses FBC's power supply risk being higher than
8 FEI's as a result of FBC's generation supply risk. This is a separate and distinct issue from
9 energy supply price risk. As discussed in that response, as a vertically integrated utility FBC
10 meets the majority of its power supply requirements with its own generation or under long term
11 supply contracts related the output of specific generating facilities. As a result, FBC's exposure
12 to market price volatility is limited to meeting small energy and capacity gaps, and to its ability to
13 mitigate costs through market displacements or surplus sales. FBC also faces energy supply
14 price risk related to the uncertainty of the future costs of supply from BC Hydro, however this is
15 not directly related to market price volatility. FEI, on the other hand, procures all of its
16 commodity supply in the wholesale natural gas markets, and must manage underlying market
17 price volatility in the setting of its commodity rates. This creates greater uncertainty and the
18 potential for more frequent changes in FEI's commodity rates, and subsequently in FEI's overall
19 prices charged to customers.

20 As a result of these two different factors, the Company has ranked FBC's power supply risk as
21 higher than FEI's, but has it has ranked FBC's energy supply price risk as lower.

22 The tables below show the 5 year history of annual bills for a residential gas customer and a
23 residential electric customer. As can be seen, over this period FEI's overall costs for
24 customers have declined largely as result of a shift in natural gas market price environment due
25 to shale gas development. On the other hand, although wholesale market power prices have
26 also shifted lower in recent years, FBC's overall costs have increased over the same period.

FEI Residential Lower Mainland Rate History	Jan 1, 2008	2008 Prorated	2009 Prorated	2010 Prorated	2011 Prorated	2012 Prorated	Jan 1, 2013
Sample Annual Bill	\$1,179	\$1,292	\$1,085	\$1,092	\$995	\$906	\$889

All components of rates include applicable rate riders.
Typical Annual Use Rate (Gigajoules) 95



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FortisBC Residential Rate History	Jan 1, 2008	2008 Prorated	2009 Prorated	2010 Prorated	2011 Prorated	2012 Prorated	Jan 1, 2013
Sample Annual Bill	\$1,027	\$1,032	\$1,091	\$1,184	\$1,319	\$1,351	\$1,416

Typical Annual Use Rate (kW.h) 12,600
Typical BiMonthly Use Rate (kW.h) Tier 1 1,600
Typical BiMonthly Use Rate (kW.h) Tier 2 500

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Note: All rate changes shown in the above tables were approved by the BCUC.

6.2 Does FortisBC agree that customers are concerned about price volatility as well as price levels? If not, why not?

Response:

FBC agrees that customers may be concerned with both uncertainty of prices due to market price volatility, as well as the level of price.



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1 **7.0 Reference: BCUC 1.20.1**

2 7.1 The table entry for “Ontario Electricity Transmitters and Distributors” suggests
3 that the Alberta approach is used whereby the common equity ratio varies by
4 utility. Please confirm whether this is actually the case.

5
6 **Response:**

7 It is confirmed that, in Ontario, all of the utilities regulated by the Ontario Energy Board (OEB)
8 are allowed the same ROE and differences among companies or sectors are reflected in
9 different capital structures. For example, while all the electricity distributors have the same
10 deemed common equity ratio, Ontario Power Generation (a regulated electricity generator) has
11 a higher common equity ratio than the distributors due to its higher business risk. Hydro One
12 Transmission has the same deemed equity ratio as the electricity distributors because the OEB
13 did not find evidence of a difference in business risk between electricity transmission and
14 electricity distribution. Natural Resource Gas has the same ROE as the two major gas
15 distribution utilities, Enbridge and Union Gas, but a higher common equity ratio.

16



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1 **8.0 Reference: BCUC 1.22.3**

2 8.1 For the historic period when FortisBC was under PBR, are the reported
3 “achieved” values before or after earnings sharing?

4

5 **Response:**

6 The reported values in response to BCUC FBC 1.22.3 are after earnings sharing.

7



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1 **9.0 Reference: Corix Response to BCPSO 1.1.2**

2 9.1 Do FortisBC and Ms. McShane agree with the calculation of FEI's market
3 capitalization value as set out in the above response? If not, what is the
4 appropriate value?
5

6 **Response:**

7 No. Ms. Ahern's calculation of FEI's market capitalization appears to be equal to FEI's 2012
8 year end common equity reported on its audited financial statements using US GAAP multiplied
9 by the market/book ratio of Ms. McShane's U.S. utility sample. This calculation does not take
10 account of the push down accounting for the Fortis Inc. acquisition of FEI that is required by US
11 GAAP. As a result, applying the average market to book ratio of the sample to FEI's reported
12 equity will overstate the market value. A more appropriate value for FEI is approximately \$1.8
13 billion.

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17 9.2 Does Ms. McShane agree with Ms. Ahern's categorization of FEI as belonging in
18 SBBI Decile 4-5?
19

20 **Response:**

21 No, as stated in Ms. McShane's testimony (Exhibit B1-72, Appendix B) at page 34, lines 872-
22 874, "In the context of the U.S. data, FEI, the benchmark utility, would most likely fall into the 6th
23 decile, which in the most recent study included firms in the \$1.3 to \$1.9 billion range."

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27 9.3 Please provide Ms. McShane's determination of FEI's market capitalization that
28 led to the conclusion it "would likely fall into the 6th decile" (per Exhibit B1-72,
29 page 34).
30

31 **Response:**

32 A likely range of market capitalizations was estimated by applying a range of Price/Earnings
33 (P/E) ratios to a range of earnings (net income). The range of earnings was based on the book
34 value of the equity component of rate base, estimated using the 2012 rate base (\$2,694)
35 multiplied by the 38.5% currently allowed common equity ratio (\$1,037 million). A range of



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1 earnings rates (ROEs) was applied to the equity base, ranging from 8.75% to 9.25%, which
2 produced a range of earnings, from approximately \$91 to \$96 million.

3 As regards the price/earnings ratios to be applied to the range of earnings, the recent (past two
4 years, from mid-2011 to mid-2013) price/earnings ratios of Value Line's group of natural gas
5 utilities were reviewed, along with the corresponding price/earnings ratios of the two relatively
6 pure-play publicly-traded Canadian utilities, Emera and Fortis. The data indicated likely P/E
7 ratios ranging from 15 to 22. The range of estimated earnings was multiplied by the range of
8 P/E ratios to arrive at a range of market capitalizations (\$1.4 to \$2.1 billion) with the central
9 tendency in the approximate range of \$1.6 to \$1.9 billion. The calculations are provided in
10 Attachment 9.3.

11

Attachment 9.3

REFER TO LIVE SPREADSHEET MODEL

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