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British Columbia Utilities Commission
Sixth Floor, 900 Howe Street
Vancouver, BC V6Z 2N3

**Attention: Ms. Erica M. Hamilton,
Commission Secretary**

Dear Sirs/Mesdames:

Re: FortisBC Energy Inc. - Application for Approval of a Multi-Year Performance Based Ratemaking Plan for 2014 through 2018

In accordance with the Regulatory Timetable set for this proceeding, we enclose for filing the electronic version of FortisBC Energy Inc.'s Reply Submission regarding Non-PBR Issues.

FortisBC Energy Inc. is also contemporaneously filing in this proceeding a joint reply submission with FortisBC Inc. on PBR Plan Design.

Sixteen hard copies of the enclosed will follow by courier.

Yours truly,

FASKEN MARTINEAU DuMOULIN LLP

[Original signed by Christopher Bystrom]

Christopher Bystrom

CRB/ccm
Encl.

* Fasken Martineau DuMoulin LLP is a limited liability partnership and includes law corporations.

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BRITISH COLUMBIA UTILITIES COMMISSION

IN THE MATTER OF THE UTILITIES COMMISSION ACT,

R.S.B.C. 1996, CHAPTER 473 (THE "ACT")

and

RE: FORTISBC ENERGY INC.

APPLICATION FOR APPROVAL OF A MULTI-YEAR PERFORMANCE

BASED RATEMAKING PLAN FOR 2014 THROUGH 2018

REPLY SUBMISSION OF

FORTISBC ENERGY INC.

REGARDING NON-PBR ISSUES

June 12, 2014

TABLE OF CONTENTS

PART ONE: INTRODUCTION **1**

PART TWO: 2014 DEMAND FORECAST **2**

A. The Scope of the RSAM 3

B. Customer Additions Forecast 4

PART THREE: 2013 BASE O&M **5**

A. The CEC's Unprincipled Approach 6

B. The Base Year is 2013, not 2011 or 2012 7

C. The Use of 2013 Actuals 8

D. 2013 Approved as Basis for the PBR Plan 10

E. The 2013 Base O&M Reflects Labour Savings of $9.4 Million 11

F. Justification of 2013 Expenditures in Operations, ES&ER and the Engineering Services and Project Management Departments 15

G. Operations Department Costs 18

H. Regulatory Savings during PBR do not affect the 2013 Base O&M 19

PART FOUR: 2013 BASE CAPITAL **22**

A. The CEC's Unprincipled Approach 22

B. Sustainment Capital 24

(a) Principles 24

(b) The LTSP Supports FEI's Capital Expenditures 25

C. IT Capital 31

D. Deferred Capital Expense not Applicable 33

PART FIVE: FINANCING, TAXES, ACCOUNTING POLICIES AND DEFERRALS **33**

A. Accounting Changes 34

B. Deferrals 34

PART SIX: BCUC UNIFORM SYSTEM OF ACCOUNTS **35**

PART SEVEN: THERMAL ENERGY SERVICES **35**

A. Code of Conduct and Transfer Pricing Policy 35

B. Safety Messaging and Other Advertising Costs 36

C. FortisBC.com Website 39

D. Shared and Corporate Services 40

PART EIGHT: EEC EXPENDITURES 43

A. The Proposed Level of Expenditures is in the Public Interest 43

B. Administration of Funds for EEC Projects with a Thermal Energy Component 44

PART NINE: CONCLUSION 48

PART ONE: INTRODUCTION

1. FortisBC Energy Inc. ("FEI") filed its Application for Approval of a Multi-Year Performance Based Ratemaking Plan for 2014 through 2018 (the "Application") on June 10, 2013, with evidentiary updates filed on July 16, 2013, August 23, 2013 and February 21, 2014.[1] On May 25, 2014 FEI filed a joint submission with FEI's sister company, FortisBC Inc. ("FBC"), on the methodology of its proposed Performance Based Ratemaking ("PBR") plan (the "PBR Submission"). FEI also filed a Final Submission on the aspects of the Application that fall outside the methodology of the PBR plan.

2. This Reply Submission will respond to intervener submissions on the non-PBR components of the Application. The following interveners filed final submissions related to FEI non-PBR issues:

(a) Commercial Energy Consumers Association of British Columbia ("CEC");

(b) British Columbia Pensioners and Seniors' Organization et al ("BCPSO");

(c) Coalition for Open Competition ("COC"); and

(d) B.C. Sustainable Energy Association and Sierra Club British Columbia ("BCSEA").

3. As the BCSEA submission is supportive, only the CEC, BCPSO and COC have taken issues with any non-PBR aspects of FEI's Application.

4. In considering the issues raised by the CEC, BCPSO and COC, FEI submits that the Commission must make its decisions based on evidence and rational argument, and must reject claims that are unsupported by, or are contrary to the evidentiary record or sound principles. As described further in this Reply Argument, many of the interveners' submissions lack any

[1] Exhibits B-1, B-1-1, B-1-3, B-1-5 and B-15. Errata and amendments to the Application were filed on December 13, 2013 regarding the total factor productivity report in Appendix D (Exhibit B-1-4) and on March 3, 2014 regarding the cost-effectiveness test for low-income demand side management programs (Exhibit B-43).

reasonable basis in the evidence, ignore relevant evidence that is contrary to the intervener's position, or are based on mischaracterizations of the evidence. In particular, FEI notes the lack of any principled approach on the part of the CEC to the setting of the 2013 base year costs ("2013 Base Costs"). FEI's goal has been to provide a reasoned approach to setting the 2013 Base Costs, based on principles consistent with PBR and cost of service ratemaking generally. FEI has therefore used the expenditures approved by the Commission for 2013 ("2013 Approved"), with specific, known adjustments as set out in its amended and updated Application and Final Submission. In contrast, interveners have approached the 2013 Base Costs opportunistically, attempting to reduce the 2013 Base Costs to the detriment of the utility without regard to the principles involved or the impact on the PBR plan as a whole. In this regard, it is notable that interveners have not responded to FEI's evidence and arguments put forward in its Final Submission regarding the setting of the 2013 Base Costs. As such, FEI respectfully submits that it is clear that the weight of evidence demonstrates that FEI's Application is just and reasonable, prudent and in the public interest, and should be approved by the Commission.

5. FEI responds to the issues raised by CEC, BCPSO and the COC following the organization of FEI's Final Submission for ease of reference for the Commission. In many cases, FEI anticipated the positions of interveners in its Final Submission. Between FEI's Final Submission and this Reply Submission FEI believes it has responded to all material issues. Silence on FEI's part, however, should not be taken as agreement with intervener positions.

PART TWO: 2014 DEMAND FORECAST

6. In its Final Submission on FortisBC Inc. and FortisBC Energy Inc. PBR Methodology, the CEC makes submissions on two topics related to the demand forecast:

(a) treatment of industrial revenues; and

(b) the residential demand forecast.

7. FEI responds to the CEC's submissions below.

A. The Scope of the RSAM

8. The CEC asserts that "industrial revenues can and should be treated like the other customer class revenues, being appropriately adjusted to actual through a regulatory mechanism."[2] FEI addressed this issue in Part Two of its Final Argument under the heading "The Scope of the RSAM", in which FEI addressed suggestions in the IRs that the Revenue Stabilization Adjustment Mechanism ("RSAM") be expanded to include industrial customers.

9. As FEI has submitted, an RSAM mechanism for industrial customers is both unnecessary and problematic. It is unnecessary because, unlike residential and commercial classes, the vast majority of the revenues from industrial customers are fixed and therefore do not vary with the actual volume of gas delivered.[3] Therefore, the amount of revenue that would be subject to the RSAM would be relatively small. Expanding the RSAM to industrial customers would also be problematic for interruptible industrial customers under Rate Schedules 7, 27, and 22, who receive non-firm service and only pay for the volumes delivered. An RSAM would effectively impose a fixed revenue stream on these customers, which would be inconsistent with the interruptible service that they receive.[4] In short, expanding the RSAM to industrial customers would be inconsistent with the rate design for these customers who either pay a fixed amount, or who are interruptible customers.

10. The CEC has not responded to FEI's submissions and had not established any need to adjust industrial revenues to actual using an RSAM. FEI submits that the CEC's position should be rejected.

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2 CEC, Final Submission on FortisBC Inc. and FortisBC Energy Inc. PBR Methodology, p. 177.

3 Exhibit B-11, BCUC IRs 1.57.2 and 1.212.1.

4 Exhibit B-11, BCUC IR 1.67.2.

B. Customer Additions Forecast

11. In the context of its argument that a "retroactive true up" or use of actuals for customer additions is required in the PBR formula, the CEC asserts that the "evidence is that customer additions forecast is consistently excessive on average and that it appears likely to continue."[5] The evidentiary record clearly demonstrates that this is not the case.

12. FEI filed a detailed analysis in Appendix E5 of the Application of the impact of variances in the forecast of customer additions. FEI's analysis clearly shows that there has been no consistent historical trend of over or under forecasting customer additions. Moreover, the historical 10 year average would suggest it is more likely for FEI to experience a slight decrease in earned return (approximately $227 thousand) compared to the forecast due to actual customer additions being, in general, less than forecast.[6] In summary, this analysis demonstrates that FEI's customer additions forecast methodology of relying on third-party residential housing forecasts and historical trends for commercial additions[7] is reasonable and that there is no evidence of bias in these forecasts. The CEC makes no reference to this analysis.

13. In its submission, the CEC references the incorrect observations of the BCPSO in the preamble to BCPSO IR 2.7.1[8] regarding the history of actual and forecast customer additions. The correct history on the customer additions forecast was clearly presented in Appendix E3 of the Application as follows:

RESIDENTIAL (RATE 1)		
YEAR	Actual	Forecast
2004	10,716	8,000
2005	11,427	9,652
2006	9,595	12,204
2007	12,003	12,764

[5] CEC, Final Submission on FortisBC Inc. and FortisBC Energy Inc. PBR Methodology, p. 75.

[6] Exhibit B-1, pp. 115-116 and Exhibit B-1-1, Appendix E5.

[7] Exhibit B-1, pp. 94 to 96.

[8] Exhibit B-21.

2008	7,959	11,098
2009	4,822	8,012
2010	6,824	4,777
2011	4,994	4,983
2012	4,475	6,507

14. As shown above, during these nine years, FEI under forecast customer additions in four years (2004, 2005, 2010 and 2011) and over forecast in five years (2006-2009 and 2012). This is consistent with FEI's overall conclusion that that there is no evidence of bias in its residential additions forecasts. It is also consistent with the small runs test conducted by FEI as described in response to BCPSO 2.7.1.

15. CEC concludes that "the evidence is there are clearly extended periods of time during which the forecasting is on average consistently above or below the actual result experience and that there is no reason to expect that this will not continue."[9] It is obvious that a forecast is a forecast and will be "consistently above or below the actual". This is not a reasonable basis to question any forecast. As explained in detail in Appendix E3 of the Application, FEI's forecast has been demonstrated to be reasonable and there is no evidence of any bias.

16. CEC's position is therefore based on a clear mischaracterization of the evidence and should be rejected. This undermines the CEC's position that a "retroactive true up" or use of actuals for customer additions is required in the PBR formula, which FEI has further addressed in its PBR Submission.

PART THREE: 2013 BASE O&M

17. FEI addressed the 2013 base year O&M ("2013 Base O&M") in Part Three of its Final Submission. FEI replies to the CEC and BCPSO submissions on the 2013 Base O&M below. FEI notes that while the CEC made submissions on a department-by-department basis, to avoid

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[9] CEC, Final Submission on FortisBC Inc. and FortisBC Energy Inc. PBR Methodology, p. 76.

duplication, FEI responds below to the underlying reasons for the CEC's recommendations where they are common amongst the departments.

A. The CEC's Unprincipled Approach

18. The CEC's submission on the 2013 Base O&M relies on principles that are inconsistent with PBR. A key example of the CEC's approach to the 2013 Base O&M appears at paragraph 20 of the CEC's submission, as follows:[10]

> "The CEC submit that to insure the 2013 O&M amount provides a realistic representation of expenditures expected during the PBR term, care must be taken to ensure that all non-recurring O&M cost items are removed from the 2013 O&M Base."

19. There are a number of issues with this statement. First, the 2013 Base O&M is not set to represent expenditures "expected during the PBR term". This is a fundamental tenet of PBR. As the CEC should be well aware, under PBR the base year costs should represent the resources required by the utility in the base year, which in this case is 2013. PBR is not based on a forecast, cost-of-service review for the term of the PBR. In addition, as the PBR term is 5 years (the "PBR Period"), it is simply not possible to set a single base year that reflects the expenditures "expected during the PBR term". In short, the CEC's statement cannot be reconciled with any rational theory of PBR.

20. Second, the CEC's assertion that "all non-recurring O&M cost items" must be removed from the 2013 Base O&M[11] is unfair to the utility and not consistent with cost-of-service principles or the PBR plan. FEI has generally not identified its expenditures as either recurring or non-recurring. However, non-recurring items are legitimate costs of the utility which occur in every year, although by their nature they change from year to year. There has been no suggestion that any of FEI's non-recurring (or recurring) expenditures in 2013 were imprudently incurred. As prudently incurred costs, they are recoverable in rates in accordance

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[10] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base O&M, p. 6.

[11] Ibid.

with cost-of-service principles. Removing prudently incurred, non-recurring expenditures would underrepresent what the resources required by the utility are going into PBR. This in turn distorts the PBR plan by embedding productivity improvements in the 2013 Base O&M that are over and above the productivity included in the X-factor and stretch factor in the PBR formula. This would be patently unfair to the utility and compromise the ability of FEI to recover its prudently incurred costs and earn a fair return.

21. In the sections below, FEI addresses the more particular submissions of the CEC which also demonstrate the CEC's lack of any principled approach to the 2013 Base O&M.

B. The Base Year is 2013, not 2011 or 2012

22. In setting the 2013 Base O&M, the CEC asserts that 2012 should be given "considerable weight" because actual labour and non-labour costs were not provided for 2013.[12] This is not an acceptable reason to favour 2012 over 2013. The CEC clearly prefers 2012 as in this year FEI had difficulty spending the 2012 Approved amounts due to the timing of Order G-44-12 (the "2012-2013 RRA Decision"), and other factors,[13] which the CEC itself notes in its argument.[14] The CEC also sometimes shows a preference for 2011 when the numbers are suitable for its purpose.[15] Thus, the pattern is for CEC to "cherry-pick" a conveniently lower-cost year for its recommendations. The base year for the PBR plan, however, is 2013, and it is essential that the 2013 Base Year reflect the resources required by the utility going into PBR, rather than some other arbitrary time period. For this reason, the most reasonable and appropriate starting point is the 2013 Approved O&M, which is an amount vetted and approved by the Commission in a recent and thorough regulatory process. There are simply no reasonable grounds to pick a different year than 2013 for the 2013 Base Costs, and no reasonable grounds to disregard the Commission's approved amounts for that year.

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[12] Ibid.

[13] Exhibit B-11, BCUC IR 2.82.1.

[14] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base O&M, p. 6.

[15] Ibid, p. 21, para. 85 and p. 23, para. 96.

23. The CEC's only attempt at a rationale for favouring 2012 is that "a breakdown of labour and Non-labour actual Expenditures has not been provided for 2013, and … the amount of temporary and sustainable savings in 2012 has been identified and quantified by department".[16] To clarify the record, the amount of temporary and sustainable savings has been identified and quantified by department for 2013[17] and FEI has provided the labour and non-labour breakdown for both the 2013 Approved and 2013 Projection. Thus, the only information not on the record is the breakdown between labour and non-labour for 2013 Actual. The CEC provides no rationale as to why the breakdown between labour and non-labour for 2013 Actual is required, or why the breakdown between labour and non-labour in the 2013 Projection is not sufficient for its purposes. If the CEC truly believed that this breakdown was so important, it should have requested the information. In any case, it is not reasonable for the CEC to argue that 2013 as a whole should be disregarded or given less weight. The evidence on the record is substantive and there is no indication that the lack of a breakdown between labour and non-labour for the 2013 Actual amounts in any way inhibited the CEC's ability to make its submissions.

24. In summary, the CEC has failed to identify any cogent rationale as to why 2012 or earlier years are to be used when setting the <u>2013</u> Base O&M. The 2013 Approved remains the most appropriate and reasonable starting point as it represents expenditures that have been reviewed and approved by the Commission in a recent and thorough regulatory process. The CEC's choice of earlier years is a blatant attempt to arbitrarily reduce the 2013 Base O&M, and must be rejected.

C. The Use of 2013 Actuals

25. The CEC asserts that a number of the smaller departmental variances between the 2013 Projection and the 2013 Actual should be incorporated into the 2013 Base O&M.[18]

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[16] Ibid, p. 6.

[17] Exhibit B-11, BCUC IR 1.83.1; Exhibit B-1-5, Evidentiary Update, Updated Table C3-2.

[18] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base O&M, p. 4.

Along similar lines, the BCPSO asserts that FEI's proposed 2013 Base O&M should be reduced by $4 million to reflect 2013 Actuals.[19] This is a significant reduction to FEI's proposed 2013 Base O&M. Generally, every dollar variance between the 2013 Projection and the 2013 Actual should not be used to reduce the 2013 Base O&M without consideration of whether the saving is sustainable or not. FEI's approach has been to begin with the 2013 Approved O&M, which has then been reduced for sustainable savings and deferred and accounting changes to reach a reasonable level for the 2013 Base O&M that reflects the required resources of FEI going into PBR.

26. BCPSO attempts to support its position by asserting that the Commission has reduced FEI's proposed O&M in previous revenue requirements applications ("RRAs").[20] However, BCPSO conveniently ignores the fact that the referenced reductions are already included in the 2013 Approved. FEI's 2013 Base O&M begins with 2013 Approved amount, rather than FEI's 2013 Forecast in the 2012-2013 RRA. As such, the 2013 Base O&M already includes the reduction imposed in the 2012-2013 RRA. Furthermore, FEI already proposed to reduce the 2013 Approved by sustainable savings realized over the last test period. As FEI explained, the Commission gave FEI a productivity challenge in the 2012-2013 RRA Decision and FEI exceeded that challenge. As such, FEI proposed to give the benefits of that productivity focus to customers through a reduction in the 2013 Base O&M, which will then last throughout the PBR term.

27. FEI explained that in contrast to the sustainable savings for which FEI has reduced the 2013 Base O&M, temporary savings "include initiatives or hiring that was delayed pending the 2012-2013 RRA Decision, employee vacancies where recruiting was planned or underway, as well as any one-time events either positive or negative that were not forecast to

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[19] BCPSO, Final Submission on Non-PBR Issues, section 1.1.

[20] Ibid.

re-occur."[21] Such one-time savings do not reflect a reduction in the resources required by FEI heading into the PBR Period.

28. BCPSO also incorrectly asserts that underspending of the O&M budget reflects budgetary "padding". Contrary to the BCPSO's assertion, FEI has explained the savings it has achieved over the 2012-2013 Test Period, which demonstrates that the spending below Approved was due to a variety of factors including the result of a number of productivity improvements.[22] Moreover, regardless of the reason for the savings, FEI has proposed to reduce the 2013 Base O&M by the sustainable savings achieved, so customers are in fact benefiting from these reductions.

29. In summary, the 2013 Approved amounts already reflect reductions ordered by the Commission in the 2012-2013 RRA Decision, including FEI's share of the $4 million productivity improvement factor. In addition, FEI's proposed 2013 Base O&M reflects the sustainable savings that FEI has achieved over the 2012-2013 period. Thus, the CEC and BCPSO's proposal would reduce the 2013 Base O&M further by removing temporary savings due to factors such as hiring delays and temporary employee vacancies, which would result in the 2013 Base O&M not reflecting the resources required by FEI going into PBR. FEI submits that its proposed 2013 Base O&M is reasonable and appropriate and should be approved as filed.

D. 2013 Approved as Basis for the PBR Plan

30. The CEC asserts that: "The Commission did not approve the 2013 approved amount with the intention or expectation that it might be used as the basis for future PBR formula."[23] This is legally problematic and factually incorrect.

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[21] Exhibit B-24, BCUC IR 2.275.2.

[22] Savings were addressed in Part Three, Section A(a) of FEI's Final Submission.

[23] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base O&M, p. 12.

31. The CEC's argument is legally problematic because the Commission approved FEI's 2013 rates as just and reasonable. The CEC's argument amounts to the suggestion that the Commission would arbitrarily or capriciously reduce costs that are just and reasonable simple because it was a base year for PBR. To the contrary, the Commission must apply the same just and reasonable standard regardless of whether it is a base year for a PBR plan. The CEC's argument would lead the Commission into legal error.

32. In addition, the Commission directed FEI in the 2012-2013 RRA Decision to come back with a productivity plan or a PBR proposal.[24] It is reasonable to believe that the Commission knew that the 2013 Approved amount would be a likely candidate for the base costs if FEI came back with a PBR proposal.

33. In any case, FEI submits that it is not relevant whether the 2013 Approved amounts were approved with the specific intention of being used as the basis for a PBR plan or not. The 2013 Approved remains the most reasonable starting point in developing the 2013 Base O&M for the PBR plan.

E. The 2013 Base O&M Reflects Labour Savings of $9.4 Million

34. The CEC incorrectly asserts that the Operations, Energy Solutions and External Relations ("ES&ER") and Engineering Services and Project Management department costs should be materially reduced because the CEC does not see the $9.4 million in labour savings and FTE reductions discussed in BCUC IR 2.252.1 reflected to the degree it expects in the 2013 Projected labour costs compared to 2013 Approved. For example, regarding the Operations department the CEC asserts:[25]

> "The total sustainable earnings proposed for the PBR term by the CEC for the Operations Department, i.e. - $2,352 thousand, is appropriate given that FEI is projecting a $9.4 million in utility wide sustainable labour savings for the PBR term. Of the 166 projected reductions in FTE positions, 43 are attributed to the

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[24] At pages 39-40.

[25] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base O&M, pp. 11-12.

> Operations Department. This alone (at $55-60 thousand per FTE equates to $2,400 - $2,600 thousand in sustainable labour savings within the Operations Department. There is no indication in the cost history that the Operations Department has contributed toward this $9.4 million in sustainable labour saving FEI submits is included in the PBR."

35. With respect to ES&ER, CEC similarly asserts that there should be a significant $1 million reduction because it "finds no evidence of a five position reduction, per Order G-44-12, or a seven position reduction, has in fact been reflected in the 2013 Approved amount, the 2013 projection or 2013 actual costs."[26] The CEC again asserts that not enough of the $9.4 labour savings have been attributed to the Engineering Services and Project Management department.[27] The CEC's assertions are incorrect for the reasons explained below.

36. First, the $9.4 million in labour savings is already reflected in the 2013 Base O&M. These savings were determined by comparing the 2013 Projection to the 2013 Approved, as discussed on page 193 of the Application. As stated in the IR referenced by the CEC:[28]

> "The inclusion of the $9.4 million sustainable labour savings in the 2013 Base O&M is a direct transfer of benefits to ratepayers for the duration of the PBR"

The CEC's primary mistake is that it incorrectly assumes that the $9.4 million in labour savings is attributed solely to FTE reductions. This is not the case, as explained in the Application:[29]

> "The labour savings arise primarily in the Operations, Information Technology, Engineering Services & Project Management, Operations Support, Human Resources and Finance/Regulatory departments. …. The labour savings are primarily driven by integration activities with FBC, savings in IBEW training through the use of new delivery models, refinement of the requirements for supporting capital activities, streamlining processes and the use of technology, and a shift to the use of contractors to allow more flexibility in staffing levels."

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[26] Ibid, para. 55.

[27] Ibid, paras. 91-92.

[28] Exhibit B-24, BCUC IR 2.252.1.

[29] Exhibit B-1, p. 193.

As indicated by the quote above, the labour savings are due to many factors other than labour savings. Further, the Operations, ES&ER, and Engineering Services and Project Management departments are not listed as a primary source of the labour savings. For these reasons, the CEC's assertions that there should be further reductions to these departments to reflect the $9.4 million in labour savings is factually incorrect. Such a reduction would simply double-count the labour savings already included in the 2013 Base O&M, resulting in a gratuitous and arbitrary reduction to the 2013 Base O&M.

37. Second, the CEC is not interpreting the FTE reductions shown in BCUC IR 2.252.1 correctly. What is shown in BCUC IR 2.252.1 is a comparison of the Net O&M FTEs Forecast in the 2012-2013 RRA for the end of 2013, to the Net O&M FTEs as of September 30, 2013.[30] Some reductions in the FTE count as of September 30, 2013 may not be reflected in the 2013 Projection labour costs. For example:

(a) If a department was experiencing vacancies as of September 30, 2013, these would result in a reduction in the FTE count at that time, but would not be reflected in the projected labour costs for 2013.

(b) FTE's included in the 2013 Projection may have been reduced during the year and substituted with contract labour.

38. Furthermore, a number of FTE reductions are already embedded in the 2013 Approved amount:

(a) The five position reduction for the ES&ER department due to the 2012-2013 RRA Decision noted in the table in the IR response is a consequence of the Commission's approval of $1 million of the total of $2.7 million requested for 2012 and 2013 for the Long Term Resource Plan. The 2012-2013 RRA Decision states (at p. 59): "the Commission Panel will only approve additional funding in

[30] Exhibit B-24, BCUC IR 2.252.1. BCUC IR 2.250.1 explains the FTE counts provided in the 2012-2012 RRA, stating: "Any forward looking FTE or employee information provided in the FEU 2012-13 Application would have pertained to the FTEs as at end of calendar year".

the amount of $400 thousand in 2012 and $600 thousand in 2013 for resource planning of the $1.2 million requested in 2012 and $1.5 million in 2013." Thus, the five FTE reduction related to this disallowance is already included in the 2013 Approved amount, so one would not see any reduction in labour costs when comparing the 2013 Projection to the 2013 Approved.

(b) The FTE reduction is partially attributable to FEI's efforts to meet the $4 million productivity savings mandated by the Commission in the 2012-2013 RRA Decision. This productivity savings is included in the 2013 Approved amount, so one would see no corresponding reduction between 2013 Approved and the 2013 Projection.

39. Thus, the fact that many of the FTE reductions may not be reflected in the 2013 Projection or are already embedded in the 2013 Approved explains in part why there is not a direct correlation between the FTE reductions shown in BCUC IR 2.252.1 and the labour savings between the 2013 Projection and 2013 Approved.

40. Third, the CEC makes the mistake of assuming that there is straightforward relationship between O&M FTEs and labour costs. FEI explained why this is not the case:[31]

> "There are a number of reasons why O&M FTE is not a straightforward calculation and should not be expected to tie directly to O&M labour costs. First, the O&M FTE is the remainder after removing an estimated allocation for employees working on capital, but includes employees that sometimes work on deferral items, since these charges vary from year to year. In addition, the O&M FTE will be influenced by the same accounting changes that influence O&M vs. capital activities. Finally, FEI's labour O&M costs are driven by changes in the mix of contractor utilization, variations from year to year in overtime requirements, increases in pension and OPEB costs that escalate faster than general labour inflation, and the extent to which shared and integrated services offset what otherwise would be changes in the number of employees and associated labour dollars."

[31] Exhibit B-24, BCUC 2.253.1.

As also noted in BCUC IR 2.253.3 that "Premium payments, overtime, timebank accrual and other salary adjustments … fluctuate and vary year over year." Thus, a reduction in net O&M FTEs is not directly tied to a reduction in overall labour costs. The numbers demonstrate that the reduction in labour costs due to the reduction in FTEs has been offset by increases in other labour costs, such as pension and OPEB costs premium payments, overtime, timebank accrual or other salary adjustments.

41. In summary, the CEC incorrectly assumes that the $9.4 million in labour savings are due entirely to the FTE reductions and that the FTE reductions translate directly into overall labour savings, and that these labour savings should be seen directly by comparing 2013 Approved to the 2013 Projection. As explained above, none of these assumptions are correct. Moreover, the 2013 Base O&M has already been reduced by the $9.4 million in labour savings. Therefore, the CEC's asserted reductions are completely gratuitous and unfair and should be rejected.

F. Justification of 2013 Expenditures in Operations, ES&ER and the Engineering Services and Project Management Departments

42. For FEI's Operations, ES&ER and Engineering Services departments, the CEC asserts that FEI has not justified the incremental expenditures in 2013 compared to 2012, and instead asserts that the 2013 amount should be based on an inflation factor compared to 2012. For example, for the Operations department, the CEC claims:[32]

> "…the CEC submits that the net increase of 6.2%, that the 2013 projected amount is above 2012 Actual costs, is excessive because no justification, or explanation is provided for spending to that decree [sic] above historical levels. The CEC notes that 2013 actual expenditures exceeded the 2013 approved amount by $1 million.
>
> The CEC therefore submits that the 2013 sustainable amount, and thus the 2013 base amount should be reduced $2,672 thousand, which provides a 2013 projection 2.4%, or the average rate of inflation, greater than 2012 actual

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[32] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base O&M, paras. 36-37.

> expenditures prior to adjustments. This reduction would provide for labour expenditures at or near levels experienced in 2012."

For the ES&ER department, the CEC similarly asserts that it "finds no explanation or justification supporting a net 16.1%, or $1,555 thousand, increase in labour expenditures in 2013 from 2012 actual levels and therefore submits that this projected increase in 2013 labour expenditures is excessive."[33] A similar claim is made with respect to the Engineering Services and Project Management department.[34] The CEC's assertions misconstrue the evidence, defy logic and legal principles, and must be rejected.

43. The CEC reductions are based on the incorrect theory that FEI needs to justify its 2013 costs as if 2013 was the test period in a forecast cost-of-service application. This is plainly not the case: 2013 was part of the previous test period, for which FEI justified its 2013 costs in its 2012-2013 RRA and the Commission approved a 2013 amount. The Commission did not in its 2012-2013 RRA Decision restrict these department's costs to inflation. Instead, the Commission appropriately considered FEI's evidence related to its cost of service for that year and made a determination. As discussed in the 2012-2013 RRA Decision, the Commission rejected some proposed expenditures, but accepted other incremental expenditures that FEI proposed for 2012 and 2013. The CEC's submissions are flatly contrary to the Commission's 2012-2013 RRA Decision.

44. In accordance with well-established regulatory principles, FEI's 2013 costs are presumed to be prudent unless the presumption is rebutted. For each of the three departments, FEI has provided evidence explaining the reasons for incremental expenditures in 2013:

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[33] Ibid, para. 53.

[34] Ibid, pp. 21 to 24, paras. 85, 90, and 96.

(a) FEI provided an overview of the Operations department's 2013 expenditures in section C3.4.3 the Application (pp. 138-141) and provided detailed responses to IRs on the history of expenditures in the Operations department.[35]

(b) FEI summarized the reasons for the increased expenditures in the ES&ER department in the Application (pp. 156-159) and in BCUC IR 2.254.1 and the IRs referenced in that response. BCUC IR 1.99.1 describes the incremental expenditures requested and approved as part of the 2012-2013 RRA and why it is appropriate that they should be included in the 2013 Base O&M. A comprehensive description of the changes in business drivers to the ES&ER department is provided in BCUC IR 2.284.1.

(c) Section C3.9 of the Application reviews the Engineering Services and Project Management drivers and costs. In response to BCUC IR 1.135, FEI has described increases in costs from 2012 to 2013 as well as the drivers of cost increases in the Engineering and Project Management department since 2008. These include changes to the BC Safety Authority Gas Safety Regulations and the CSA Z662 standard.[36]

45. The CEC has not referenced, let alone refuted, any of FEI's evidence related to the 2013 expenditures for the departments in question. The CEC has therefore not rebutted the presumption of prudence in any way, as it has ignored FEI's evidence with respect to the expenditures and the fact that the Commission has approved increases for 2013 above 2012. FEI submits that prudently incurred expenditures in 2013 must form part of the 2013 Base O&M, as these reflect the resources required by the utility in the base year going into PBR.

46. In summary, the CEC's assertions with respect to reductions in FEI's 2013 Base O&M are based on inappropriate principles and a mischaracterization of the evidentiary record. FEI submits that they should be rejected.

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[35] Exhibit B-11, BCUC IR 1.124 to 130; Exhibit B-24, BCUC IR 2.258.1, 2.261 and 2.262.

[36] Exhibit B-11, BCUC IR 1.135.4.

G. Operations Department Costs

47. With respect to the Operations department, the CEC asserts:[37]

> "The CEC proposes this reduced projection then be reduced an additional $784 thousand, which is net of the 2012 temporary expenditure increases, $1,004 thousand, less $220 for permanent new expenditures in 2013."

48. This submission is confusing and without any merit. The CEC has not explained, and there is no rational basis for why, the 2013 Base O&M should be reduced by 2012 "temporary expenditure increases." Based on the IR referenced by the CEC (Exhibit B-11, BCUC IR 1.82.1), the 2012 "temporary expenditure increases" are in fact the "2012 temporary savings" identified by FEI for 2012. There is simply no logical connection as to why the 2013 Base O&M should be reduced by temporary savings realized in 2012.

49. The CEC lists a number of what it claims to be "reasons" in support of its recommendations with respect to the Operations department. FEI has responded to some of these reasons above and in some cases no response is required. FEI does wish to address the following statement from the CEC:[38]

> "One of the Business Drivers for the Operations Department is the number of customers; therefore the cost per customer should be a significant guide when developing the 2013 projection and base amount."

FEI has listed and discussed six business drivers of the Operations department.[39] Number of customers is only one element of one of these six business drivers, which is Customers, System Size and Condition. The 2013 Projection and 2013 Base O&M cannot be derived based on only one aspect of six different Business Drivers. For example, vegetation management has no direct relation to the number of customers. Moreover, as discussed above, the CEC's proposed reductions are not in fact based on cost per customer, but instead based on applying an inflation factor to 2012 Actual amounts, so the CEC's submissions are contradictory. Finally, FEI

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[37] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base O&M, para. 38.

[38] Ibid, p. 11, para. 40.

[39] Exhibit B-1, pp. 136-137.

notes that the 2013 Approved remains the most appropriate basis for developing the 2013 Base O&M, as it has been reviewed and approved by the Commission in a recent and thorough regulatory process. The 2012-2013 RRA Decision did not set the 2013 O&M by reference to either cost per customer or an inflation factor.

H. Regulatory Savings during PBR do not affect the 2013 Base O&M

50. BCPSO groundlessly asserts that the 2013 Base O&M should be reduced by an unspecified amount[40] because (a) the 2013 Projection in the Finance and Regulatory department is above the 5-year average and that (b) spending should be expected to decrease due to regulatory savings attributable to PBR.[41] The CEC similarly asserts in its PBR Submission that it is not appropriate that "regulatory costs should be subject to formulaic increases under PBR" when "the proposition is that regulatory costs will be dramatically reduced."[42] As discussed below, these assertions ignore the evidentiary record which show that the expected regulatory savings during PBR do not impact the 2013 Base O&M, including the Finance and Regulatory department, and should be rejected.

51. BCPSO has presented no rationale for why a 5-year average is to be preferred to the Commission-approved amount or even actual or projected amounts. The fact that the 2013 Approved amount for Finance and Regulatory is above the 5-year average is reflective of rising costs as discussed on pages 191-192 of the Application as approved by the Commission. The use of a 5-year average would therefore not reflect FEI's required level of resources in the base year. As FEI stated in BCUC IR 1.117.1:

> "A review of the historical numbers shows that, for each of the past 5 years, with the exception of 2011, FEI's costs have increased. In the context of labour, benefit and non-labour inflation alone, it is not realistic to expect that the 2013 projection would be equal to the average of the previous 5 years. Rather, the expectation would be that

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[40] BCPSO states "greater than $4M", which apparently includes its other recommendations for an approximately $4M reduction.

[41] BCPSO, Final Submission on Non-PBR Issues, section 1.2.

[42] CEC, Final Submission on FortisBC Inc. and FortisBC Energy Inc. PBR Methodology, p. 83, para. 312.

> the 2013 projection would be higher than the 2012 actual, all else equal. The average annual increase in the departmental O&M over the five year period is approximately 2.6%. At a minimum, the cost increase would be expected to be in line with this. But given the one-time efficiencies that are reflected in the historical numbers (the elimination of executive and support positions and unfilled vacancies), this historical average increase is understated when looking forward."

Furthermore, the 2012-2013 RRA Decision did not consider it appropriate to use a 5-year average of costs for any departmental O&M expenditure. FEI also notes that there is no suggestion that any expenditures in the Finance and Regulatory department in 2013 (or any year) have not been prudent. Therefore, the 5-year average cost of the Finance and Regulatory department is not a relevant factor when determining the 2013 Base O&M.

52. The implicit assumption in CEC and BCPSO's submission is that the Finance and Regulatory department or other costs included in the 2013 Base O&M should be expected to be reduced due to regulatory savings related to PBR. It is first important to understand the source of the regulatory efficiencies from PBR. FEI explained the types of regulatory efficiencies in response to CEC IR 1.23.2:[43]

> "Regulatory efficiency is an inherent benefit of a PBR plan which helps the utility staff to shift their focus from time and resource-consuming regulatory proceedings to focusing on providing service to customers and on finding productivity opportunities that may eventually benefit the company and its customers. …
>
> Another smaller component of regulatory efficiency pertains to lower costs for hearings, including Commission hearing costs and intervener funding allowances. These costs are normally collected in deferral accounts and recovered in rates. Savings during the PBR in this category will flow 100% to customers through lower amounts being recorded in deferral accounts."

[43] Exhibit B-8, CEC IR 1.23.2.

53. Significantly, as noted above, the savings to be achieved from the lower costs for hearings, including Commission hearing costs and intervener funding allowances, are captured in deferral accounts, and therefore are not reflected in the 2013 Base O&M.[44]

54. FEI explained the other type of savings further in response to CEC IR 2.74.1, as follows:[45]

> "In the context of O&M, the resources consumed referred to in the response to CEC IR 1.23.2 are primarily related to the time of employees in various departments throughout FEI. Although these departments include Finance and Regulatory, for developing the financial models and developing rate forecasts, every department in the company is involved in developing forecasts, writing sections of applications and responding to information requests. For example, the Finance and Regulatory department does not craft the descriptions of the activities of the Distribution department, nor does it respond to IRs relating to these activities. There are also external resources that are utilized in regulatory proceedings (external legal, expert witnesses and consultants, Commissioner costs, PACA awards, administrative costs such as courier expenses) that do not reside in O&M."

55. With respect to the impact of PBR on the Finance and Regulatory department costs, FEI responded to this directly as follows:[46]

> "FEI has taken into account the fact that FEI would not have to prepare revenue requirement applications during the PBR period; however, there are no forecast savings in the Regulatory department due to other significant regulatory applications and processes that are anticipated over the PBR period. If FEI were not under PBR, the forecasts for Finance and Regulatory department staff may be increasing rather than staying at existing levels."

56. Thus, for the reasons quoted above, and as also discussed in the responses to BCUC IR 2.292.1, 2.292.2 and 2.292.3, the PBR framework will not lead to savings as compared to the Base O&M costs, but rather allow existing resources to refocus their efforts on either

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[44] Exhibit B-23, CEC IR 2.75.1.

[45] Exhibit B-23, CEC IR 2.74.1.

[46] Exhibit B-24, BCUC IR 2.292.3.

completing other regulatory applications (in the case of Finance and Regulatory) or running the business (in the case of other departments).

57. In addition, even if the O&M costs were to be projected to go down over the PBR term due to regulatory efficiencies, it is contrary to the principles of PBR to reduce the 2013 Base Year Costs to reflect the anticipated costs during the PBR Term. The PBR formula already incorporates an efficiency and stretch factor. FEI has addressed this in Part Three of its Final Submission under the heading "Future Efficiencies".

58. For these reasons, the 2013 Base O&M should not be reduced for any regulatory savings due to PBR. Also see FortisBC's PBR Submission with respect to the CEC's assertion that Finance and Regulatory costs should not be subject to the O&M formula.

PART FOUR: 2013 BASE CAPITAL

59. FEI addressed the 2013 base year capital costs ("2013 Base Capital") in Part Four of its Final Submission. The CEC and BCPSO's final submissions on the 2013 Base Capital are addressed below.

A. The CEC's Unprincipled Approach

60. The CEC's submissions on FEI's 2013 Base Capital are based on incorrect and contradictory principles and must be rejected. This is apparent from the CEC's summary of its position, as follows:

(a) The CEC's position that Sustainment capital expenditures should be reduced is not based on the perspective of what resources were required and approved for FEI in the base year of 2013, but are improperly based on the forecast of expenditures over the PBR Period. CEC asserts that its reduced amount "reflects the fact the detailed capital forecast for 2014 & 2015 and prioritized capital work

program for as much as 20 years in the future are not complete."[47] [Emphasis added.] The CEC's position is inconsistent with PBR. FEI is not justifying its capital expenditures over the PBR Period as if it had filed a forecast, cost-of-service application. Rather, Sustainment Capital expenditure limits will be determined by formula as set by the PBR plan.

(b) The CEC's position that Information Technology (IT) capital expenditures be reduced "to provide a provision that is more in accord with historical expenditure history" is also not based on the perspective of what resources were required by and approved for FEI in the base year of 2013, but on an historical perspective. As FEI has submitted in its Final Submission as well as above, this is not a reasonable position in the context of PBR, as it has the effect of embedding assumed efficiencies into the base year, thus skewing the efficiency factors in the PBR formula.

61. CEC's submission in the section entitled "The Financial Foundation of the PBR Proposal- Capital"[48] also reveals the incorrect basis of the CEC's position. In this section, the CEC's focus on the expectation of capital expenditures over the test period is clear. Notably, the CEC asserts:[49]

> "the CEC submits that no snapshot of capital spending (including that used to develop the 2013 capital base amount) can accurately provide an indication of the total amount of capital that will be actually required in future years or the relative mix of capital expenditures that can be reasonably expected in the future years." [Emphasis added.]

62. The purpose of setting the 2013 Base Costs is not to estimate the amount of capital that will actually or reasonably expected to be required in future years. As FEI has emphasized, it is central to the PBR Plan that the 2013 Base Capital be based on the resources required by the utility in the base year, not over the PBR Period. The level of productivity that

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47 CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base Capital, p. 1.

48 Ibid.

49 Ibid, p. 3.

FEI is expected to achieve compared to the 2013 Base Capital is set by the PBR formula. Reducing the 2013 Base Capital for potential savings would be asymmetrical, as there are many cost increases that FEI will also encounter during the PBR Period that it will be required to manage. Furthermore, the result would be that FEI would have no opportunities remaining to achieve its significant productivity target during the PBR Period. This would be contrary to the intent of PBR, and would potentially deny FEI its right to a reasonable opportunity to earn a fair return.[50]

63. As can be seen from the above, the CEC's position is not based on sound principles and is inconsistent, either based on a future perspective of what costs may be required during PBR, or based on an historical perspective of what costs were required previously. As FEI has submitted, the appropriate starting point for the 2013 Base Capital is the 2013 Approved, which reflects the capital expenditures for FEI that have been vetted and approved by the Commission in a recent and thorough regulatory process.

B. Sustainment Capital

64. The CEC asserts that the 2013 Base Capital should include a reduced amount for Sustainment capital, although the CEC does not suggest a quantum by which it should be reduced.[51] As described below, the CEC's asserted reasons for requesting a reduction in Sustainment capital in the 2013 Base Capital amount are based on inappropriate principles and a mischaracterization of the evidentiary record.

(a) Principles

65. The CEC's reasons for requesting a decrease in Sustainment Capital expenditures in the 2013 Base Capital rest entirely on its (incorrect and misleading) views of the forecast test period. In summary, the reasons provided by CEC include that the forecast is not supported by a "fully developed" Long-Term Sustainment Plan (LTSP) and that the spike of asset

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[50] Exhibit B-24, BCUC IR 2.272.2.

[51] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base Capital, pp. 6-9.

replacements has passed.[52] FEI reiterates that this is a PBR application, not a cost of service review, and it is not logical to set the 2013 Base Capital based on the forecast for the PBR Period. FEI refers to its submission above and Part 4, Section B(d) of its Final Argument for a discussion of this issue. Further, the CEC's suggestion is not even rational for a cost-of-service review, as the 2013 Base Capital is for 2013 and the PBR Period is for entirely different years (2014-2018). Thus, it is not only unprincipled, but simply impossible to set the 2013 Base Capital (one year) to reflect expenditures over a 5-year period.

66. In contrast to CEC's illogical approach, it is completely appropriate and reasonable to base the 2013 Base Capital on the 2013 Approved amounts as proposed by FEI.

(b) The LTSP Supports FEI's Capital Expenditures

67. The CEC recited and summarized FEI's evidence in its submission, but in doing so was selective and mischaracterized the evidentiary record. FEI responds in detail below in order to set straight the evidentiary record for the benefit of the Commission Panel.

68. The CEC has attempted to paint the picture that FEI's LTSP is inconsistent with FEI's historical expenditures and its forecast capital expenditures. This is incorrect. FEI provided a detailed explanation of the LTSP in the body of its Application (pp. 211-216) and in the LTSP Update in Appendix C3, which the CEC has not fairly represented. In response to BCUC IR 1.143.2, FEI explained that the LTSP has not undermined the need for the capital expenditures in the past 3 years or the forecast need for capital expenditures in future years:[53]

> 'The increase in the level of sustainment capital spending has been previously approved by the Commission through an oral hearing in the 2012-2013 RRA and fully documented in that proceeding.
>
> In the past 3 years, FEI has increased its expenditures on Sustainment Capital, while also recognizing the need to balance the rate impact on customers with those expenditures necessary to support the continued safe and reliable delivery

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[52] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base Capital, p. 9.

[53] Exhibit B-11, BCUC IR 1.143.2.

of natural gas to its customers. The level of Sustainment Capital expenditures from 2010 through 2013 has been required to proactively address concerns identified at the time, and the subsequent conclusions in the LTSP do not change this conclusion. There are several drivers behind the escalation in capital expenditures over the period 2010 through 2013 that have been previously discussed in FEI's last two RRAs.

Overall, the increase in sustainment capital expenditures over the past 3 years is a result of FEI's transition from a reactive approach to a proactive, long-term approach in managing its natural gas assets, and also as a result of changing regulations and heightened public expectations regarding the safety of natural gas infrastructure. The sustainment capital expenditures relating to integrity and reliability, as well as mains replacements, were proposed to address known issues and integrity concerns and to avoid the potential of more costly repairs in the future. Another driver of expenditures was additional pipe replacements to accommodate the increased activities of municipalities and the Ministry of Transportation in upgrading their respective infrastructures. As discussed above, the reasons for the increased level of spending were provided in the 2012-2013 RRA and subsequently approved in Order G-44-12. FEI's actual expenditures for Sustainment Capital were within the levels forecasted and approved in that decision. As per the 2012-2013 RRA, Section 6.2.2:

> "For this Application, sustainment capital spending budgets have been developed using existing sustaining capital and some enhanced asset management practices. It should be noted that FEU[54] is also addressing hazards and risks that the Company believes require immediate attention. Over the longer term, FEU will continue to improve its asset management practices with the further development of a Long Term Sustainment Planning process. Asset replacement costs are expected to continue to rise in the future because the cost of new assets will be higher than that of the original equipment."

The conclusions of the LTSP continue to support the increased level of Sustainment Capital expenditure. FEI is responsible for gas transmission and distribution assets with a rate base value of approximately $2.6 billion and an approximate replacement value of $6.1 billion. Approximately 27% of distribution mains were installed over 40 years ago. The installation practices and materials used during that era mean that many of these pipes possess characteristics which have been demonstrated to be a concern, such as increased susceptibility to corrosion. Although the LTSP does not consider age to

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[54] The FEU, or FortisBC Energy Utilities, consists of FEI, FortisBC Energy (Vancouver Island) Inc. and FortisBC Energy (Whistler) Inc.

> be a risk factor, the presence of corrosion over time does cause pipe condition to deteriorate. The LTSP enables FEI to concentrate on areas of interest and reduce asset risks more cost-effectively; it does not eliminate the need to replace assets. Given the higher costs and more stringent requirements to install new assets, this level of Sustainment Capital expenditures addresses only a tiny fraction of FEI's assets and is far less than the cost to replace assets reactively or on the basis of asset age alone.' [Emphasis added.]

69. More specifically, the CEC misleadingly and incorrectly states that: "In the absence of a fully developed LTSP, there is no objective data or plan to support the level of proposed sustainment capital spending for the entire PBR term."[55] The CEC also asserts that once the LTSP is "fully developed" expenditures in 2017 and 2018 will be less than forecast, and also that earlier replacements "without the support of the LTSP methodology" will be premature.[56] First, it is misleading to say that the LTSP is not "fully developed". FEI has, in fact, completed the first iteration of the LTSP which has been used in the development of FEI's capital plans for its distribution and transmission assets.[57] FEI expresses an intent to continually improve the LTSP when it states that it "expects that all elements of the LTSP will continue to evolve and improve as more experience and knowledge is gained."[58] However, it is misleading to suggest, as the CEC has, that this in any way undermines the utility of the current iteration of the LTSP. In fact, FEI's detailed account of the LTSP demonstrates its usefulness for capital planning.

70. Second, it is misleading and incorrect to say that there is a lack of "objective data or plan" to support the proposed Sustainment capital expenditures and that the Forecast is not supported by the LTSP. While FEI reiterates that it is not obliged in this proceeding to justify its forecast over the PBR Period as if it had filed a forecast, cost-of-service application, FEI specifically described the use of the LTSP in developing the Sustainment capital expenditures in

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[55] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base Capital, p. 9.

[56] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base Capital, p. 9.

[57] Exhibit B-1, p. 215, ll. 10-11.

[58] Exhibit B-1-1, Appendix C3, p. 15.

Section 2 of the LTSP Update.[59] Given the extent to which the CEC has misrepresented this issue, FEI quotes at length from this evidence as follows:

> "The development of the LTSP has enhanced the FEU's understanding of the risk factors relevant to pipe failures. The reality is that a significant proportion of the FEU's assets, due to the technology and practices used in the era of installation, do possess characteristics which have been demonstrated through experience to be a concern so replacement may be more reasonable than repairs and mitigation. The LTSP results also bring to the forefront indications of asset conditions that warrant mitigation, whereas in the past Asset Management may not have had the capability to pinpoint these concerns before they develop into leaks. In order to act proactively on this data, the FEU are seeking to increase its resources in order to execute an increased level of sustainment capital expenditure over the long term.
>
> FEI has challenges in obtaining resources to execute an increased level of sustainment capital in 2014. Therefore for 2014 FEI forecasts maintaining the same level of sustainment capital expenditure as in 2013. For 2015-2018, FEI is forecasting to gradually increase sustainment capital by an average of $1 million per year starting in 2015 to a total of $82.3 million in 2018. Regardless of the level of expenditures, <u>the process enhancements developed by the LTSP have been applied towards developing a list of capital replacements to be undertaken during the PBR period and will be an integral part of FEI's capital planning processes for future years.</u>
>
> …
>
> The LTSP enhances the FEU's Asset Management and capital planning processes and works in conjunction with the FEU's continuing Integrity Management Program (IMP). The FEU's IMP activities work to prevent, monitor and remediate hazards/threats that can potentially impact the operation and integrity of its assets. Selected IMP activities such as In-Line Inspections may rely on quantitative risk assessment methods which are common practice. Requests for sustainment capital work may arise directly from IMP activities, and data from IMP activities can be a valuable input into the LTSP. The LTSP can also support IMP activities by directing attention to areas of interest.
>
> Contrary to the framework outlined in the previous RRA, the project team found it impractical to define a strict level of risk exposure beyond which action would be triggered. Risk is subjective and the timing and location of failures cannot be

[59] Exhibit B-1-1, Appendix C3, pp. 13-14.

> predicted with absolute certainty. It is not feasible, and may not be possible, to reduce risk to zero. In every system there always exists a non-zero risk of an undesirable outcome, and the marginal increase in cost of service for mitigating actions must be balanced against the marginal reduction in risk. The team's approach was not to define what an "acceptable" level should be, but rather to ensure the FEU undertake reasonable and effective measures to enhance its ability to maintain safety and reliability over the long term. The decision on whether to replace an asset based on its risk level is still subject to the judgment of experienced staff, not a mathematical formula. The output of the LTSP provides an additional tool that helps ensure that the FEU's asset sustainment capital is spent on projects that deliver the highest relative cost-benefit. The mains with the highest relative risk scores are continually addressed. With future annual iterations of the risk assessment, improved data and comparisons will be available to judge the effectiveness of the risk mitigation measures and the level of expenditures will be adjusted accordingly to achieve a balance between risks, customer impacts, the FEU's ability to execute work, corporate strategy and external factors.
>
> The projected Sustainment Capital Expenditures and Base Capital are shown in Figure C3-3. This projection is based on project-specific estimates of pipe replacements in areas of interest. Further work is still required to refine the estimates. Nevertheless, it provides an enhanced level of accuracy compared to previous projections and represents a reasonable and prudent level of expenditures to support the continued safe and reliable delivery of natural gas to FEIs customers."

71. As made clear from the above, the LTSP was used in the development of, and supports, FEI's 2014-2018 Sustainment capital forecast.

72. FEI has made it clear that further analysis needs to be done to identify all the actual projects over the PBR Period. For example, in response to BCUC IR 2.296.1, FEI states:[60]

> "the identification, analysis and planning of system sustainment is an ongoing function and, as influencing factors change (e.g. system condition, code requirements) the actual projects that will be required may change as compared to the high level forecasts provided, to ensure that the resources are invested in addressing the conditions with the highest risk. This dynamic analysis approach ensures that FEI will continue to operate safely and reliably while protecting customers from unwarranted costs and rate impacts."

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[60] Exhibit B-24, BCUC IR 2.296.1.

Thus, FEI will continue to refine the actual work required from year to year as a prudent operator of the system.

73. The CEC also asserts that the "spike" in asset replacements has largely passed due to FEI's efforts since 2008 to reduce the assets nearing the end of their useful life.[61] The CEC here is again misconstruing or directly contradicting the evidentiary record to suit its purposes. FEI explained in the Application that: "Nearly 25 percent of distribution mains and 35 percent of intermediate and transmission pressure pipelines (Figure C4-2) have been in service for 40 to 55 years."[62] FEI also produced figures showing the proportions of these assets approaching life expectancy.[63]

74. As stated in the Application, based on only the average service life of FEI's pipeline assets, it could be projected that a significant portion of the pipes would need to be replaced starting within the next 10 years.[64] FEI goes on to explain that it is using the LTSP, amongst other tools, to avoid a potential spike in costs for asset replacement. The LTSP allows FEI "to better understand asset condition and to plan required work in an effort to ensure all expenditures are appropriate and in the best interest of maintaining a safe and reliable natural gas delivery system."[65] While FEI has learned through the development of the LTSP that age should not in itself be considered a risk factor, the LTSP does not eliminate the need to replace assets:[66]

> "Although the LTSP does not consider age to be a risk factor, the presence of corrosion over time does cause pipe condition to deteriorate. The LTSP enables FEI to concentrate on areas of interest and reduce asset risks more cost-effectively; it does not eliminate the need to replace assets."

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[61] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base Capital, p. 9.

[62] Exhibit B-1, p. 211.

[63] Exhibit B-1, Figure C4-2, p. 212.

[64] Exhibit B-1, p. 212.

[65] Exhibit B-24, BCUC IR 2.296.3.

[66] Exhibit B-11, BCUC IR 1.143.2.

75. With this background, one can then understand the CEC's observation that "during the middle of the PBR term, i.e. - 2015 & 2016, the amount of assets projected to be replaced or upgraded annually are forecast to decease or maintain a constant level, in every class of sustainment capital except Distribution Mains and Service Renewal Alternations." [67] This observation does not support the CEC's incorrect assumption that the spike in asset replacement has passed; rather, the leveling off of expenditures in these areas reflects FEI's use of the LTSP to successfully manage the need for asset replacements on the system.

76. In summary, the CEC's position on Sustainment capital is incorrectly based on the forecast expenditures over the PBR period, rather than the 2013 base year. The CEC has also mischaracterized the evidentiary record on the nature of the LTSP and its relationship to the need for asset replacements in the future. As such, the CEC's position should be rejected.

C. IT Capital

77. The CEC's position on IT capital expenditures is that the 2013 Approved amount, which FEI has used in its 2013 Base Capital, should be reduced by $3,000 thousand, which would be $6,600 thousand less than the 2013 Projection. The CEC asserts that this would "better represent historical IT capital spending levels". In principle, resetting the 2013 Base Capital with reference to historical trends is inappropriate for a number of reasons:

(a) The theory of PBR and the basis of the PBR plan requires that the 2013 Base Capital be set on the requirements of the utility for that year using cost of service principles, which is why the 2013 Approved Capital - determined by the Commission in a full oral hearing - is the most reasonable starting place. There is no need to reanalyze the need for capital expenditures that have already been previously justified by FEI and approved by the Commission.

(b) Resetting the 2013 Base Capital to the level of expenditures from historical periods undermines the PBR plan by "baking in" an arbitrary level of efficiencies

[67] CEC, Final Submission on FortisBC Energy Inc. Non-PBR Base Capital, p. 9.

into the 2013 Base Capital. It is also asymmetrical as FEI will also be experiencing many cost pressures over the PBR Period, which are not similarly "baked in" to the 2013 Base Capital. Overall, adjusting the 2013 Base Capital in this asymmetrical fashion has the potential effect of denying FEI's right to a reasonable opportunity to earn a fair return.

78. In response to the CEC's asserted reasons in support of its request, FEI responds as follows:

CEC Assertions[68]	**FEI Response**
"There is no IT capital plan to support a higher sustained higher level of spending."	Given that this is a PBR Application, it is not necessary or reasonable to require FEI to provide a more detailed IT capital plan for the PBR Period. Nonetheless, FEI has supported its 2014-2018 Forecast with the descriptive account of expenditures in each of the 5 areas of IT capital on pages 246-248 of the Application. FEI has also provided details of the Project Portfolio Management approach it will apply to IT capital expenditures over the PBR Period. The Forecast IT capital expenditures over the PBR Period are consistent with 2012 and 2013 Actual experience.[69]
"The IT expenditure history shows that in subsequent years after which expenditures significantly increase, total expenditures decreased."	The CEC's statement is incorrect. As shown in the IR referenced by the CEC, BCUC IR 1.143.1, there is no trend of significant increases, followed by significant decreases.
"There is no apparent reason that the inventory of assets created by capital expenditures should increase annually beyond historical rates for the entire PBR term."	The total 2012-2013 Actual amount was very close to the total 2012-2013 Approved amount on a combined basis. Consistent with the latest two years of experience, FEI is forecasting relatively stable levels of IT capital expenditures over the PBR term for the reasons explained in the Application.[70]

68 Ibid, p. 12.

69 Exhibit B-1, p. 169, Table C3-21 and p. 171, Table C3-22.

70 Exhibit B-1, p..

79. FEI submits that the CEC's position is improperly based on historical and future cost considerations, and that FEI's proposed 2013 Base Capital is appropriately and reasonably based on the 2013 Approved amount and should be approved.

D. Deferred Capital Expense not Applicable

80. BCPSO's sole submission on the 2013 Base Capital is not applicable to FEI. BCPSO states:

> "As per our submission for FBC, BCPSO submits that FEI should create a deferred capital expense account to recognize that ratepayers have already paid for forecast capital spending that is deferred to subsequent periods."[71]

81. FEI does not have any deferred capital expense for 2013. As described in Section C4 of the Application, the total of the 2012 Actual and the amounts projected by FEI for 2013 (the "2013 Capital Projection") were very close to the amounts approved in the 2012-2013 RRA Decision. 2013 Actual capital expenditures were $6.4 million higher than the 2013 Capital Projection, after removing the Biomethane interconnect facilities and, overall, the combined 2012 and 2013 Actual spending was $5.3 million above the 2012 and 2013 Approved.[72] As such, there is no basis to establish any deferred capital expense account. FEI submits that BCPSO's argument is inapplicable and must be rejected.

PART FIVE: FINANCING, TAXES, ACCOUNTING POLICIES AND DEFERRALS

82. BCPSO was the only intervener to take issue with any aspect of FEI's Application regarding financing, taxes, accounting policies and deferrals. Notably, no interveners opposed FEI's proposed modifications to, and financial treatment for, deferral accounts. This part of FEI's Reply Submission responds to the submissions of BCPSO on the topics of accounting changes and deferrals.

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[71] BCPSO, Final Submission on Non-PBR Issues, section 1.3.

[72] Application, p. 61, as revised by Exhibit B-1-5.

A. Accounting Changes

83. FEI's 2013 Base O&M includes adjustments for two accounting changes: the allocation of retiree pensions/OPEBs and the capitalization of annual software costs. BCPSO has expressed opposition to these changes on the sole basis that FEI would earn a return on the capitalized expenses.[73] This is not a reason to reject this approach. FEI has sought to make these changes to align its practices more closely with GAAP and with FBC. BCPSO has not responded to any of FEI's evidence or argument on these matters as described in Section D3.1 of the Application and addressed in Part Five of FEI's Final Submission.

84. BCPSO also makes the surprising assertion:[74]

> "...that capitalizing O&M costs that were formerly expensed is detrimental to ratepayers to the extent that ratepayers are not able to meet or exceed the return allowed to Fortis shareholders. For most ratepayers, achieving a return in excess of 9% is not realistic in the current economic conditions."

85. While not clear, the thrust of this claim would appear to be that FEI's rate of return should be capped by what return ratepayers may be expected to make. This assertion is contrary to the fair return standard. The Commission has set a fair return for FEI and it is not open to BCPSO to argue in this proceeding that a different standard should apply. FEI submits that BCPSO's position must be rejected.

86. With respect to BCPSO's submission on capitalized overhead, FEI refers to its Final Submission, Part Five, Section A(g) which addresses this topic.

B. Deferrals

87. BCPSO "questions whether FEI has taken out all non-controllable costs for which they retain deferral accounts under their proposal."[75] While all ongoing O&M accounts that

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[73] BCPSO, Final Submission on Non-PBR Issues, section 1.1.

[74] Ibid.

[75] Ibid.

have deferral accounts have been removed, except BCUC fees, this does not make a difference to rates. If the items subject to deferral are not removed, then the difference between the formula-escalated amount in the base and the actual amount is captured in the deferral account.[76] Thus, there are no potential rate impacts whether the amounts are included or not.

PART SIX: BCUC UNIFORM SYSTEM OF ACCOUNTS

88. Consistent with the lack of interest from interveners during the proceeding, there were no intervener submissions on the topic of the BCUC Uniform System of Accounts.

PART SEVEN: THERMAL ENERGY SERVICES

89. The COC has made a number of submissions with respect to thermal energy services ("TES"), to which FEI responds below. As noted by FEI in Part Seven of its Final Submission, these issues will be dealt with in the ongoing Code of Conduct and Transfer Pricing ("CoC/TPP") Review proceeding, and should not be addressed in this proceeding. FEI has responded to the COC as it has maintained the contrary position that the Commission should determine some issues in this proceeding despite the CoC/TPP Review proceeding being a more appropriate forum.

A. Code of Conduct and Transfer Pricing Policy

90. Under the heading "Use of FEI Resources by Affiliates", the COC makes submissions on the CoC/TPP that are not relevant to this proceeding and are more appropriately canvassed in the CoC/TPP review, if at all. FEI responds only to the COC's suggestion that it has "no way of independently verifying" that FEI has in fact done what it claims to have done. FEI has put evidence on the record in this proceeding which spells out in detail the different cost allocation processes in place between FEI and FAES. The COC had the full opportunity to participate in this proceeding and test that evidence. Beyond this, the COC has no right or need to "independently verify" FEI's claims. Moreover, FEI takes exception to

[76] Exhibit B-11, BCUC IR 1.12.1.

the COC's insinuations that FEI could have deliberately falsified evidence and misled the Commission. Such insinuations are without any foundation and completely unacceptable.

B. Safety Messaging and Other Advertising Costs

91. The COC greatly exaggerates the impact of the tag line "FortisBC, providing natural gas, electricity, propane and thermal energy services" on some of FEI's messaging. The COC says that the tag line "clutters the message" of FEI's natural gas odour safety radio ad and "distorts" it from a safety message to brand promotion.[77] However, it is not reasonable to think that the tag line has any detrimental effect whatsoever on the safety message or changes the purpose of the message. As explained in response to BCUC IR 2.284.1, the purpose of FEI's safety messaging is to meet industry standards and to reduce risk to the public:

> "In compliance with the CSA Oil and Gas System Standard Z662-07, FEI has a responsibility to provide on-going and continuous education to the public about the risk associated with natural gas and propane products. Such education and messaging meets the requirements of the CSA Oil and Gas System Standard Z662-07, where it is identified as recommended practice for operating companies to develop safety and education programming as part of their safety and loss management and integrity systems. Public safety education programs can reduce risk to the public, the environment and property by third party damage. The benefit to customers of the safety education is that awareness has steadily increased. The number of survey respondents who felt that they were "very prepared" in knowing what to do when a gas odour was detected increased from 15 per cent in Spring 2010 to 29 per cent in Q3 2013. The number of "not at all prepared" decreased from 70 per cent to 50 per cent over the same period. The increased O&M over this period is $1 million, which was approved by the Commission in past proceedings (Order G-141-09 and G-44-12). Throughout 2014 to 2018, public safety education will continue to be an integral part of the company's integrity management system. Please refer to the responses to BCUC IRs 1.99.1 and 2.283.1 for more details."

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[77] Final Submission of COC, p. 8.

92. Furthermore, contrary to the COC's suppositions, the tag line on FEI's safety and other messaging is important to provide for integrity and assurance that the safety advice is coming from a reputable source with expertise in the given area. FEI explains as follows:[78]

> "There is no confused message to the customer and … the mention of FortisBC and the services it provides is not a distraction to listeners. In fact it serves to provide customers with the reassurance that the actions they are being asked to take in the event that they smell gas or in improving excavation diligence are being delivered by a trusted energy provider and thereby an authority on the subject matter. Furthermore, a recent evaluation of the radio ads indicates that there has been an improvement in the percentage of respondents who are "extremely prepared or "very prepared" for such an incident if it were to occur."

The use of the brand therefore enhances the safety message rather than "distorts" it. This is borne out by the success of FEI's safety education messaging as reported in the IR response quoted above.

93. To clarify the record, the tag line does not appear on all advertisements. For example, the tag line only appears on two of FEI's radio advertisements.[79] It is also important to note that the common "tag line" is applied consistently whether used in a natural gas utility, electric utility or FAES advertisement.[80]

94. The COC asserts that FEI's cost allocation approach to advertising is "inherently wrong".[81] FEI's approach, however, is reasonable and properly allocates costs in accordance with cost causation principles. As stated in FEI's response to BCUC IR 2.310.1:[82]

> "Similar to how other costs are allocated in the Company, FEI's practice for allocating advertising costs to natural gas, electric or TES/FAES is based on the principle of cost-causality and which businesses benefit from the costs. In the case of advertising, costs are incurred primarily for the gas and electric businesses and the benefit of those customers served. Accordingly, our

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[78] Exhibit B-19, COC IR 1.15.3.1.

[79] Exhibit B-19, COC IR 2.15.5.

[80] Exhibit B-19, COC IR 2.15.3.2.

[81] Final Submission of COC, pp. 8-9.

[82] Exhibit B-24, BCUC IR 2.310.1.

> historical practice has been to allocate shared advertising costs based on the number of customers in the gas and electric utilities."

For example, neither existing nor potential TES customers are driving the need for or costs of the gas odour safety messaging and so are not allocated costs for these advertisements.[83]

95. However, where TES is a cost-driver of the advertisement in question, FEI has allocated costs accordingly. As stated in response to BCUC IR 2.311.3:

> "In the situation where the core content of the piece includes reference to the thermal energy business, the piece would be assessed to determine how much of the overall content is related to the thermal energy business, with the costs apportioned based on its share of content."

For example, 20% of the total cost for sponsorship of the 2012 EFMA conference was charged to the TESDA.[84]

96. The COC asserts that the question is whether the cost of advertising should be borne by natural gas ratepayers if the purpose is attempting to promote the brand.[85] The use of a tag line, however, does not transform a safety message into brand promotion. As discussed above, the use of the FortisBC brand is not an indicator of the purpose of the message, the substance of the message or the cost drivers of the message. The Commission has held in the AES Inquiry that use of the FortisBC brand name is an acceptable practice in the thermal energy services market space, and it surely is also an acceptable practice for FEI.

97. The COC also claims that the Commission should establish a formula that reflects "the market value of the advertisement in the 2014-18 Revenue Requirements."[86] For the reasons discussed above, there is no need for such an allocation. In any case, this is not the appropriate time to set any such allocation should the Commission conclude one is required.

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[83] Exhibit B-19, COC IR 2.15.3.2.

[84] Exhibit B-13, COC IR 1.5.4.

[85] Final Submission of COC, p. 7.

[86] Ibid, p. 9.

All of the advertising and cost allocations discussed on the record relate to historical costs and, as this is PBR application, FEI is not requesting specific approval for advertising costs during the term of the PBR. Since in the future cost allocations will be informed by the results of the CoC/TPP review, the Commission should refrain from making any determination in this proceeding. Instead, FEI submits that the Commission should rely on FEI's proposed TESDA Overhead Allocation Variance Account to capture any changes in cost allocations to the TESDA resulting from the CoC/TPP review. As FEI has submitted, the use of the TESDA Overhead Allocation Variance Account will keep both FEI and FAES customers whole pending the outcome of the review.

C. FortisBC.com Website

98. COC claims that the Commission should consider in this proceeding whether the natural gas ratepayer "is receiving fair value for the website that it is providing to FAES".[87] As FEI explained, the FortisBC website provides a single point of access for all FortisBC's regulated services. The landing page of the website is a FortisBC page, not an FEI page, and the FortisBC brand is not owned by FEI.[88] The website segregates between gas, electric and TES offerings so that, while the initial landing page is a common site, it allows for the customer to select the type of service(s) they are interested in. This approach is consistent with the Commission's determination on pages 40-41 of the AES Inquiry Report that "the use of the FortisBC brand name in the AES and New Initiatives market spaces is an acceptable business practice." Consistent with the AES Inquiry Report, FEI has taken care "to distinguish between the services offered by the traditional natural gas utility and services offered by Affiliated Regulated or Non-Regulated Businesses.". FAES contributes to the costs of the FortisBC website through the overhead allocation to the TESDA.[89] Any changes to the overhead allocation are more appropriately considered in the COC/TPP review proceeding.

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[87] Final Submission of COC, p. 10.

[88] Exhibit B-19, COC IR 2.12.2.3.

[89] Exhibit B-13, COC IRs 1.6.1 to 1.6.10.

99. It would be inappropriate to allocate any costs to FAES from FEI for any perceived marketing benefits of the website, as the COC would appear to be suggesting. If any such benefits exist, they are not bestowed upon FAES by FEI, as FEI does not own the FortisBC brand and the landing page through which customers can select the service of their choice is not an FEI page. Thus, the COC's position should be rejected.

D. Shared and Corporate Services

100. COC incorrectly asserts that FEI's Final Submission "is silent on [how] the allocation of [shared and corporate] costs specifically to FAES will be handled."[90] FEI addressed this topic in Part Seven, Section F, of its Final Submission. As stated there, FEI expects to continue to provide corporate and shared services to FAES during the PBR Period and will allocate an appropriate amount to the TESDA for these services.[91] The amount of O&M to be allocated to FAES in 2013 has already been decided by the Commission in Order G-44-12 at $854 thousand.[92] FEI's proposal is to use this amount for the 2013 Base O&M, and to escalate this amount by the O&M formula for the PBR Period.[93]

101. In addition, a portion of the FHI Management Fee is allocated to FAES as explained in response to COC IR 2.13.1:[94]

> "Of the $103 thousand in the FHI Management Fee Allocation to Other entities including FAES, using the Massachusetts Method, which relies on payroll, net operating revenue and average net book value of capital assets plus inventory, approximately $15 thousand (i.e. 0.12 percent of $12.4 million total corporate services cost pool) is calculated as the allocation to FAES. This amount along with the remainder of the $103 thousand for Other has been absorbed by FHI with no impact to FEI ratepayers (none has been allocated to FEI). As stated above in the pre-amble to this IR, the use of the Massachusetts formula for a business under development does not as work as well as for established utility operations."

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90 Final Submission of COC, p. 10.

91 See Exhibit B-24, BCUC 2.313.1 for a description of the items included in this allocation.

92 Exhibit B-24, BCUC IR 2.356.1.

93 Ibid.

94 Exhibit B-19.

102. Since FEI cannot predict with certainty the overhead allocations that will result from the CoC/TPP review, FEI's proposal is to establish the TESDA Overhead Allocation Variance Account. This account will capture the difference between the formula-determined amount of overheads recovered by FEI from thermal energy customers (as described in the preceding paragraph) and the final allocation, including any adjustments that will result from the CoC/TPP review. FEI proposes to address the disposition of any amounts recorded in this deferral account in its first Annual Review to be held in 2014.[95] FEI's proposed approach will keep both FEI's and FAES' customers whole.[96]

103. COC asserts that the Commission should instead deal with the allocation in this proceeding. There are a number of reasons why this proposal is not reasonable. Two key reasons are as follows:

(a) The Commission has already established a separate CoC/TPP review process. Determining an allocation in this proceeding in advance of the development of a new CoC/TPP is inefficient and would likely result in inconsistent decisions. Moreover, it is more appropriate to develop any new allocation in the context of, and with the benefit of, the new CoC/TPP. Given the CoC/TPP review, it is premature to consider the issues raised by the COC.

(b) FEI's proposal is a fair approach to dealing with the uncertainty created by the CoC/TPP review. Without this deferral account, it will not be possible for the amount recovered from FAES to reflect the results of the CoC/TPP that FEI and other stakeholders are currently undertaking to review; in other words, FEI customers would take the risk that the amount that should be charged under the approved CoC/TPP ends up being greater, while FAES customers would be at risk if the amount turns out to be lower than the allocated amounts.[97]

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[95] Application, Section D4.1.2, pp. 292-293.

[96] Exhibit B-24, BCUC IR 2.356.1.

[97] Exhibit B-24, BCUC IR 2.356.3.

104. Notably, the COC has not responded to FEI's submissions on this topic and does not address the potential for conflict between a determination in this proceeding and the results of the CoC/TPP review, or the desirability of reviewing this issue in the context of the new CoC and TPP.

105. The COC also makes assertions regarding the allocation approaches that could be taken. While FEI does not believe this matter should be considered in this proceeding, the COC's allocation approaches are not reasonable or even relevant to shared and corporate services:

(a) The COC notes that Fortis Properties is a non-regulated business and asserts that Fortis Properties is a "striking parallel" to the situation with FAES.[98] There is no evidence of any "striking parallel" between Fortis Properties and FAES. While Fortis Properties is non-regulated, FAES projects are in fact regulated. There is simply no basis for the Commission to determine that the lump sum fee to Fortis Properties is just and reasonable for FAES. Moreover, the Commission has already established a lump sum fee of $854 thousand for FAES.[99]

(b) The COC also suggests another allocation that includes "direct labour expense, including management estimates or timesheets of those individuals to charge time to FAES as suggested by FEI as well as any executive time, employees of FAES and contract labour".[100] Such direct allocations are of course already done by FEI as explained by FEI in its IR responses[101] and Part 7, Section B, of its Final Submission. However, these direct allocations are not related to corporate and shared services, which are allocated through the $854 thousand overhead allocation to FAES.

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[98] Final Submission of the COC, p. 11.

[99] Exhibit B-24, BCUC IR 2.356.1.

[100] Final Submission of COC, p. 11.

[101] E.g., Exhibit B-24, BCUC 2.313.1, 2.313.2, 2.313.7, 2.313.8.

106. FEI respectfully requests that its approach to the allocation of overhead to the TESDA, in conjunction with its proposal for the TESDA Overhead Allocation Variance Account, be approved.

PART EIGHT: EEC EXPENDITURES

107. Interveners made submissions on FEI's EEC expenditures on the following topics:

(a) The overall level of expenditures; and

(b) The administration of Funds for EEC Projects with a Thermal Energy Component.

108. FEI responds to these submissions below.

A. The Proposed Level of Expenditures is in the Public Interest

109. BCPSO asserts that the level of expenditures sought by FEI for the 2014-2018 is too high, stating:[102]

> "EEC spending which was 20.7M, is proposed to be $34.4M in 2014 and rising to $39.0M in 2018 – almost 100% increase over actual 2012. This appears to be excessive and unlikely to be achieved. Accordingly, BCPSO submits that the proposed amounts should be reduced."

110. FEI addressed the level of expenditures it is seeking in Part 8B of its Final Submission. Briefly, the proposed level of expenditures is reasonable for the following reasons:

(a) FEI's actual levels of expenditures have been increasing since 2009, with total 2013 forecast expenditures of $27,936 thousand.[103] FEI's program has matured and FEI is now forecasting a relatively stable level of expenditures over the next five years.

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[102] BCPSO, Final Submission on Non-PBR Issues, Section 1.2.

[103] Exhibit B-1-1, Appendix I, p. 16; Exhibit B-8, CEC IR 1.80.1.

(b) FEI's proposed level of expenditures is supported by its detailed 2014-2018 EEC Plan in Appendix I, Attachment I-1 of the Application. The level of proposed funding levels are supported by the detailed program budgets presented in the 2014-2018 EEC Plan.[104] The budget creation includes a reasonable estimation of the number of participants that could be achieved.[105]

(c) The BCSEA Intervener Evidence states that the FEU's level of expenditures was "not unreasonable" and that its costs to achieve planned savings are in line with industry experience. While BCSEA states that "the FEU's annual gas savings plans are behind industry leaders," it notes that the FEU's depth of savings is "in the middle of the pack for gas DSM administrators in the U.S."[106]

(d) Consistent with the EEC deferral accounts approved for 2012 and 2013, FEI's proposed deferral account treatment negates any risk to ratepayers from FEI not being able to execute its EEC Plan over $15 million.[107]

111. The FEU submit that they have filed a robust EEC plan and have sought a reasonable level of expenditures for the PBR Period. BCPSO has not refuted any of FEI's evidence. As such, BCPSO's position should be rejected.

B. Administration of Funds for EEC Projects with a Thermal Energy Component

112. FEI has addressed the topic of the administration of funds for projects with a TES component in Part Seven, Section M of its Final Submission. The COC asserts that "it would be more appropriate practice that a common administrator should review all TES projects to ensure that they receive consistent review."[108] This is, however, exactly what FEI has proposed. According to its proposal, Price Waterhouse Coopers ("PWC") would perform all aspects of

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[104] Exhibit B-11, BCUC IR 1.224.1.

[105] Exhibit B-1-1, Appendix I-1, as amended by Exhibit B-43. Exhibit B-24, BCUC IR 2.373.4.

[106] Exhibit C4-8, BCSEA Evidence, p. 6 and p. 32.

[107] Exhibit B-1-1, Appendix I, p. 31.

[108] Final Submission of COC, p. 4.

individual project reviews, which would otherwise have been performed by FEU, as soon as a customer's intention to engage a third party thermal energy services provider has been established. Process diagrams indicating visually the tasks that PWC will perform are included in Exhibit B-1-1, Appendix I, Attachment I-4, Appendix A – Business Process Diagrams.[109]

113. The COC asserts that "If FEI is the reviewer of a TES application for EEC funds, it comes into a position of potential conflict of interest when it becomes aware of the application and its content."[110] This is incorrect as FEI would not be "the reviewer of a TES Application for EEC funds". Pursuant to the process outlined in the PWC proposal, the FEU would ask customers if they are or will be using a thermal energy provider. When the answer is yes, the FEU are immediately removed from the approval and administration of EEC funds, and any potential to inappropriately use such funds for the benefit of the FEU is eliminated.[111] Furthermore, mere awareness by FEI's EEC staff of an application for EEC funds does not give rise to any conflict of interest. The COC's concern with the mere awareness of the application goes well beyond the concerns of the Commission's directive in 2012-2013, which was focussed on the administration of the EEC funds. FEI notes, however, that contact between EEC and FAES staff has deliberately been minimal, and related only to regulatory matters.[112] FEI confirmed as follows:[113]

> "FEI confirms that FEI personnel with access to customer information do not communicate with FEI personnel working on FAES' TES projects regarding customer information including names, contact information, EEC applications, historical natural gas consumption or any relevant information known to FEI in the course of its business that is not in the public domain."

To the extent that there are concerns with information sharing, this is a code of conduct matter to be addressed in the CoC/TPP review, not in this proceeding.

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[109] Exhibit B-24, BCUC IRs 2.381.2 and 2.381.3.

[110] Final Submission of COC, p. 3.

[111] Exhibit B-24, BCUC IR 2.382.1.

[112] Exhibit B-13, COC IR 1.2.5.

[113] Exhibit B-13, COC IR 1.3.2.

114. The COC claims that there are scenarios that are not covered by the PWC proposal, particularly where a TES provider becomes involved later in the process. However, FEI has made it clear that it would be removed from the administration of the EEC funds as soon as a customer's intention to engage a third party thermal energy service provider has been established. FEI explained in response to COC IR 1.2.3:

> "Should the proposal for third party review of applications for EEC funds where there is a thermal energy services aspect to the project be approved, the Companies will incorporate a question up front in commercial program application forms that asks customers whether third party ownership of a thermal energy services project is in place or contemplated. <u>Should third party ownership become a factor during the time that a customer's application for an EEC program is underway, that application would go to PwC for processing until it is complete</u>." [Emphasis added.]

115. To summarize, if the customer itself does not know that the project involves or may involve a TES provider, there is no conflict of interest and it is completely appropriate for the FEU to remain as administrator of the EEC funds. If at some later point, a TES provider becomes involved, the FEU would be immediately removed from the approval and administration of the EEC funds.

116. FEI has explained in its Final Argument why removing the FEU as the first point of contact is unnecessary and not practical.[114] As submitted there, any concern can be substantially addressed by directing PWC to ask any EEC applicants submitted to its review whether or not any FEU staff member indicated that the availability or size of EEC incentives was dependent upon the customer's selection of FAES or any other company as a TES provider. PWC could then report on the findings.[115]

117. Finally, FEI reiterates that having PWC or any third party act as the front line in regards to EEC programs goes beyond "approval and administration of funds", but rather

[114] Exhibit B-24, BCUC IR 2.382.1.1.
[115] Ibid.

represents something more akin to program administration and delivery.[116] As the FEU have submitted, it is beyond the Commission's jurisdiction to require the FEU to outsource the delivery of its programs.

118. The COC asserts that FEI was "merely doing the minimum to comply with Commission's prior order".[117] This assertion is mere innuendo based on FEI's response to an IR in which it stated it was not aware if BC Hydro uses a third party to avoid conflicts of interest.[118] The record demonstrates that FEI works closely with BC Hydro on a number of EEC fronts,[119] and FEI was no doubt not aware of BC Hydro's use of any third party precisely because BC Hydro does not use any, which FEI was able to confirm.[120] In any case, FEI has described how it chose PWC as its fairness advisor, which was the highest rated vendor in a request for proposals for the fairness advisor for FEI's NGT program.[121] PWC has knowledge of FEI's program and is ideally suited for the position.[122]

119. The COC claims that the costs of any third party review should be treated differently than other administrative costs and should be recovered from the shareholder.[123] Contrary to the assertions of the COC, there is no basis on which the Commission could deny cost recovery. FEI's third-party proposal is in direct response to a Commission direction and any costs incurred would become part of FEI's prudently incurred costs for the administration of EEC programs. It is well established that a utility should be able to recover its prudently incurred costs in providing utility service. As such, it is reasonable and appropriate that the costs of any third party administration of EEC funds be recovered in the same manner as all other administrative funds.

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[116] Exhibit B-24, BCUC IR 2.382.1.1.
[117] Final Submission of COC , p. 4.
[118] Final Submission of COC , p. 4.
[119] See FEI's Final Submission, Part Eight, Section J: Integration with other Utilities.
[120] Exhibit B-24, BCUC IR 2.371.1.3.
[121] Exhibit B-11, BCUC IR 1.241.1; Exhibit B-24, BCUC IR 2.381.1.
[122] Exhibit B-1-1, Appendix I, Attachment I-4.
[123] Final Submission of COC, p. 4.

PART NINE: CONCLUSION

120. FEI submits that the evidence in this proceeding demonstrates that the approvals sought are just and reasonable and in the public interest. FEI respectfully requests that the Commission grant the approvals sought as set out in Section A2 of the Application as amended and in the Draft Order included in Exhibit B-1-5.

ALL OF WHICH IS RESPECTFULLY SUBMITTED.

Dated: June 12, 2014

[original signed by Christopher Bystrom]

Christopher Bystrom
Counsel for FortisBC Energy Inc.