Diane Roy
Director, Regulatory Services

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

Electric Regulatory Affairs Correspondence
Email: electricity.regulatory.affairs@fortisbc.com

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

November 5, 2014

Via Email
Original via Mail

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

Attention: Ms. Erica M. Hamilton, Commission Secretary

Dear Ms. Hamilton:

Re: FortisBC Energy Inc. (FEI)

Application for Approval of Code of Conduct (COC) and Transfer Pricing Policy (TPP) for Affiliated Regulated Businesses Operating in a Non-Natural Monopoly Environment (ARBNNM) (the Application)

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

On June 27, 2014, FEI filed the Application as referenced above. In accordance with Commission Order G-160-14 setting out the Amended Regulatory Timetable for the review of the Application, FEI respectfully submits the attached response to BCUC IR No. 1.

If further information is required, please contact the undersigned.

Sincerely,

FORTISBC ENERGY INC.

Original signed by: Ilva Bevacqua

For: Diane Roy

cc (email only): Registered Parties

1.0 Reference: Exhibit B-7, Supplementary Information, Request No. 1, pp. 1-2
Exhibit B-1, Tab B1, COC pp. 11, 21; Transcript T1:47
Conflict of Interest

FEI concludes that no conflict of interest exists that will negatively impact natural gas ratepayers when FEI (seller of services) performs work for FortisBC Alternative Energy Services Inc. (FAES) (purchaser of services) because there is no incentive to favour FAES' needs (human resources, procurement, regulatory affairs, corporate communications), or that the nature of the work performed does not lend itself to a conflict of interest (financial management, information technology) (Exhibit B-7, pp. 1-2).

"Renewable thermal energy solutions such as geoexchange systems, waste heat recovery systems and solar thermal systems can displace both existing and future expected demand for natural gas. While the FEU do not offer these services to their customers, <u>the potential for other third party service providers to do so creates a risk to the FEU's annual demand profile and thus to the FEU's revenue requirements.</u>" ………. "With today's limited but growing market penetration of renewable thermal energy systems, the FEU will continue to monitor thermal energy demand in order to gauge its impact over time on the Utilities' natural gas load and system capacity." (FortisBC Energy Utilities, 2014 Long Term Resource Plan, Exhibit B-1, p. 152) [underlined added for emphasis]

On page 11 in Tab B-1 COC (Exhibit B-1), in response to the wording proposed by Commission staff, FEI posed the question regarding how the sharing of operating personnel in FEI's situation would have a negative impact to FEI's ratepayers. On page 21 in Exhibit B-1 Tab B-1 COC, FEI states that the use of FortisBC by an ARBNNM operating in a non-natural monopoly environment is an acceptable business practice, and that the name FortisBC is owned by Fortis Inc.

1.1 Currently FAES has 10 staff who are engaged in business development. Is it reasonable to conclude that FAES would not be able to safely and effectively serve its existing customers as well as pursuing strategic growth without the management and operational staff from FEI?

<u>Response:</u>

Not all FAES employees are engaged in business development. As per the organization chart provided in the response to COC IR 1.2.1, FAES has 7 employees that provide admin, finance, regulatory, engineering, project management and operational services.

If FAES did not utilize any of the services of FEI staff, FAES would procure services elsewhere. However, FAES would not benefit in such case from the background experience and knowledge of the existing FEI staff. FAES would also face the additional challenge of procuring these services from a third party for a few hours at a time.

1.2 Is it reasonable to conclude that the FEI staff are, for all intents and purposes, assignable to any FortisBC operations but are labelled FEI staff for payroll purposes? For example, as a mature utility, FEI may not require a higher than existing level of regulatory affairs and corporate communications staff but more staff-hours are required because of the requirement to serve future business growth in thermal energy services and the staff performing both FEI and FAES work are referred to as FEI staff for payroll purposes.

Response:

No. FEI draws a distinction between assigning staff to another operation, and that other operation being able to utilize a limited number of hours of FEI staff time as available. In the case of the 10 FEI staff who were assigned to work on matters now done by FAES, they have been removed from FEI payroll and assigned to FAES's payroll. This is consistent with FEI's general approach.

FEI staff that provide corporate and operational services to FAES are providing them a few hours at a time when other work priorities allow[1]. In many cases, that additional time is incurred outside of regular working hours. It is not always feasible or practical to perfectly match resource availability with work requirements. It is more practical to re-deploy a percentage (i.e. 5 percent) of an employee's time to serve FAES requirements than it is to eliminate a percentage of a position. This is the case for the corporate services currently being provided by FEI to FAES as none of the individual positions providing services are providing a number of hours that constitute anywhere near the equivalent of a full-time position. Therefore, it is not possible that FEI is staffing at a higher level than required to support its ongoing business requirements.

As an example, FEI provided the following information in the response to BCUC IR 2.250.1 (Ex. B-24) in its PBR proceeding, showing the staffing levels in the Finance and Regulatory department since 2008. FEI did not start providing finance and regulatory services to FAES

[1] Transcript Volume 1, page 125, lines 20-26 and page 126, lines 1-6.

until 2010, and it can be seen that there has been a decline in the FTEs since that time, rather than an increase as would have occurred to maintain a higher level of staff to support FAES.

Business Unit	**2008**	**2009**	**2010**	**2011**	**2012**	**As of Sept 2013**
Finance & Regulatory	63	65	63	63	58	56

FEI's staffing and O&M levels are extensively reviewed in its revenue requirement filings. Where additional resources are added to the natural gas revenue requirement, these are subject to review in that context.

1.3 The Long Term Resource Plan states that thermal energy services create in a risk to the revenue requirements of FortisBC Energy Utilities. Since the use of the utility name FortisBC can refer to either FEI or FAES, doesn't this blurred identity lead to a lack of allegiance to FEI by its own management and operational staff and exacerbate the risk to FEI's revenue requirements and FEI's ratepayers?

Response:

The risk to the demand profile for FEU exists from the provision of thermal energy services, irrespective of the service provider. Many developers will have determined to adopt thermal energy solutions, whether due (for example) to municipal requirements or for marketing purposes. FAES provides services that make use of natural gas, and in doing so supports the natural gas utility, as compared to a third party provider that may not consider natural gas in the solution.

Therefore, FEI staff and management support the success of both FEI and FAES, and there is no conflict or lack of allegiance that exists.

2.0 Reference: Exhibit B-7, Supplementary Information, Request No. 1, pp. 1-2

Exhibit B-1 p. 11

Conflict of Interest

FEI concludes that allowing executive management services will result in no harm to its own ratepayers and this conduct is similar to the FortisAlberta's Code of Conduct. Any concerns regarding commonality of officers and management could be addressed through confidentiality disclosure agreements. (Exhibit B-7, pp. 1-2)

2.1 On page 11 in Tab B1 COC (Exhibit B-1), in response to the proposed wording from Commission staff, FEI posed the question regarding what is intended to be considered confidential information. Can FEI clarify what it has in mind when describing "confidentiality disclosure agreements" by its officers and management?

Response:

If a confidentiality disclosure agreement were to be required by the Commission, then, an FEI officer or senior management employee of FEI that also holds a position with FAES would be required to execute a non-disclosure agreement in favour of FEI. The non-disclosure agreement would obligate the person to keep confidential any commercially sensitive information obtained in the course of his/her work for FEI that is not otherwise in the public domain and, if disclosed to FAES, would create the potential for material harm to FEI. However, FEI does not believe such a confidentiality disclosure agreement is appropriate or required as there is an existing FEI Business Ethics policy which provides guidance.

3.0 Reference: Exhibit B-7, Supplementary Information, Request No. 3, p. 6

Conflict of Interest

The FEI business development staff who were dedicated to serving FAES, that is, those sales staff precluded from shared services, were transferred out of FEI effective January 1, 2014 and are now residing in separate FAES offices.

3.1 Please clarify if the sales staff in separate FAES offices since January 1, 2014 continue to have equal access to the FEI intranet @fortisbc.com, Microsoft Lync and Microsoft SharePoint sites and all other FortisBC sites. If so, please describe whether the FAES staff's access are more limited and restricted relative to a regular FEI staff's access. If FAES staff's access is not restricted, please comment on the effectiveness of the FortisBC's proposed separation of employees.

<u>Response:</u>

As there is no confidential information posted on the FEI intranet, Microsoft Outlook and Lync, FAES staff have the same access as all FEI employees to these sites. FAES staff's access to sharepoint sites is restricted to only the sites that are granted access to them by the sharepoint site administrator(s). The administrator limits access to circumstances where FAES employees require access, such as FAES regulatory applications. Additionally, FAES staff do not have access to the FEI customer information system.

FEI believes the controls and separation of information system access described above is consistent with the guidelines of FEI's proposed Code of Conduct whereby FEI will not provide any information to FAES that would inhibit the market from functioning and that customer information should only be released by FEI with the written consent of the customer.

3.1.1 For illustrative purposes, if IT resources were invested in separating FEI and FAES employees, are the time and material costs allocated to FAES? Is the time spent being tracked on time sheets?

<u>Response:</u>

With regards to creating and maintaining user profiles for FAES employees, there are no costs of materials involved. For the FEI IT labour resources required, the employees are required to complete timesheets for work related to FAES. The one-time effort involved to adjust FAES employee user profiles is minimal.

3.2 Please clarify if the respective business development divisions from FEI and FAES, who may be competitors in a project, report to the same office of VP Market Development and External Relations.

Response:

Not confirmed. The Energy Solutions group, who deal with adding natural gas customers for thermal energy use to the FEI system as well as the Energy Efficiency and Conservation groups now report to the Executive Vice President, Customer Service and Regulatory Affairs.

4.0 Reference: Exhibit B-7, Supplementary Information, Request No. 4, pp. 7-8; Exhibit B-1, Tab A1, TPP Appendix A Determining Full Cost for Three Types of Services; Tab C-3, Slides 54 to 56

Fully Allocated Cost and Market Price

Slide 56 illustrates the calculation of FEI's full cost which is composed of calculating chargeable hourly rate, chargeable daily rate, and applying the general overhead and facilities charges. The definitions used in the example are:

- Chargeable hourly rate = annual base salary + 39 percent benefits ÷ 1636 hours
- Chargeable daily rate = 7.5 hours x chargeable hourly rate
- General overhead = 10 percent x chargeable daily rate
- Facilities charge = $100 per day
- Total full costs = chargeable daily rate + general OH + facilities charge

In almost all categories of position in the comparison table on page 8, FEI's charge-out rates at costs are higher than market, with the exception of junior engineers and junior accountants whose cost and market rates are equal.

4.1 On page 5 of Tab B-1 TPP (Exhibit B-1), FEI states that proposed use of "no greater than full cost" rather than higher of market price or fully allocated cost is in recognition of the need to protect the interests of both FEI's and FAES' ratepayers and prevent cross-subsidization from occurring. Wouldn't it be in the interest of the FAES ratepayers to pursue receiving services at market rates?

Response:

In FEI's view, it is in the interest of FAES ratepayers to receive services as required and at a cost that is no greater than the full cost. A comparison of FEI's rates to market rates in isolation of a consideration of the expertise and familiarity of the FEI staff with FAES' requirements, and the availability to provide services for a limited number of hours at a time, is missing a key component of the benefit to both FAES and FEI ratepayers.

In those situations where FEI's rates are above market after also accounting for the value provided for each hour contracted, it would make sense for FAES to receive the service from the market.

4.2 Absent surplus capacity at FEI, does it make business sense to offer services to FAES at market instead of “no greater than full cost”?

Response:

There is no situation that exists where there is enough surplus capacity at FEI to constitute an entire position where an employee could otherwise be redeployed. Therefore, it makes sense to offer services to FAES at any amount, since it is a recovery that would not otherwise be realized by FEI and its ratepayers.

5.0 Reference: Exhibit B-7, Supplementary Information, Request No. 5, p. 9

Exhibit B-3 Summary of Participants' Positions Table, p. 1

Fully Allocated Cost and Market Price

FEI states that in terms of rate setting, FEI charges are considered a cost of doing business for FAES as are any other third party charges FAES incurs.

5.1 Given the comparison of hourly charge-out rates between FEI to Market for 2014, please clarify that FAES' ratepayers would be better off securing services in the market rather than at full cost from FEI.

Response:

Please refer to the response to BCUC IR 1.4.1.

5.2 FEI proposes that "With Commission approval, the cost may be set at below full cost." (Exhibit B-3, Table p. 1,) Please clarify if FEI would only likely seek Commission approval to charge FAES at below full cost if it has surplus capacity or if its full cost is above market.

Response:

No, that is not the correct conclusion to draw from this proposal.

FEI clarifies that it included the words "With Commission approval, the cost may be set at or below full cost." in its proposed Code of Conduct and Transfer Pricing Policy, recognizing that circumstances may arise in the future which may support charging less than fully allocated costs. While FEI does not have specific examples at this time in support of a request to charge less than full cost, FEI provides the following discussion of possible circumstances which may warrant FEI requesting approval from the Commission.

Similar to the language included in the current Transfer Pricing Policy for NRBs regarding Designated Subsidiary/Affiliate whereby the Commission can approve the use of a reduced loading (i.e. less than full cost) for services provided to designated affiliates, FEI envisions potentially similar circumstances arising in the future. The current language in the Transfer Pricing Policy for NRBs states the following:

A Designated Subsidiary/Affiliate is a related company that is designated by [FortisBC Energy] and approved by the Commission to receive reduced loadings in the Transfer Price. The designation relates to the additional benefits that the related company provides to [FortisBC Energy]'s customers, employees or to the economic development of the Province of British Columbia.

The benefits to FEI of such a provision may include higher revenues that exceed FEI's incremental cost of providing the service(s), and efficiencies from human resource sharing between FEI and its affiliate. As indicated in the response to BCUC IR 1.1.2, it is not always feasible or practical to perfectly match resource availability with work requirements. It is more practical to re-deploy a percentage of an employee's time to serve FAES requirements than it is to eliminate a percentage of a position. Sharing of an FEI employee's time in these circumstances would serve to reduce costs to FEI to the benefit of its ratepayers. Efficiencies from human resource sharing between FEI and its affiliate can also arise when both entities require an individual with similar skills and attributes, but the time commitment required by each entity is insufficient to justify the hiring of a full-time person. In the absence of a sharing arrangement, the entities involved would likely incur higher costs in hiring its own full time person.

FEI believes sharing of its resources at no greater than full cost with FAES benefits both FEI and FAES's ratepayers. This position was echoed by some of the participants during the Code of Conduct and Transfer Pricing consultation process. FEI refers to comments provided by participants included in Exhibit B-2, Tab B1, page 7. The BCOAPO commented that "the interests of ratepayers on both sides of the FEI/FAES divide are best advanced by requiring FAES to pay the LOWER of market or fully allocated cost as long as FEI recovers incremental cost plus a premium." The BCSEA commented that "sharing of resources between two large utilities such as FEI and BC Hydro, will benefit both sets of ratepayers. It's more an issue of how to value the service."

5.2.1 Please provide some examples where FEI would likely set its charges to FAES at below full cost.

Response:

Please refer to the response to BCUC IR 1.5.2.

5.2.2 Please comment whether setting charges at below full cost would also be proposed by FEI in its transactions with: (a) affiliated Non-Regulated Businesses, and (b) other arm's length entities.

Response:

With regards to setting charges below full cost to affiliated non-regulated businesses, please refer to the response to BCUC IR 1.5.2. FEI would have to assess the circumstances at the time and determine the additional benefits that may be provided to FEI's customers, employees or to the economic development of the Province of British Columbia, from charging less than the full cost.

With regards to setting charges below full cost to arm's length (third party) entities that are not affiliated with FEI, please refer to the response to COC IR 1.1.10. The services provided by FEI under the proposed Code of Conduct and Transfer Pricing Policy for ARBNNMs are for its affiliates only. As a result, the issue of setting charges at below full cost for other arm's length entities would not be applicable to FEI and is not relevant to this proceeding.

5.2.3 Would there be circumstances under which FEI would provide services to FAES at a cost lower than it would provide the same services to a non-regulated company operating in the thermal energy services market?

Response:

Based on the TES Guidelines, all TES are regulated. FEI assumes the question intended to ask about non-affiliated companies operating in the thermal energy services market. FEI would only provide tariff services to these non-affiliated companies. The services covered under the FEI Code of Conduct and Transfer Pricing Policy would not be considered tariff services.

6.0 Reference: Exhibit B-7, Supplementary Information, Request No. 6, pp. 11-13; Exhibit B-1, Tab C2, Slides 10 and 11

Cost Collection Processes and Controls

On page 13, FEI states that overhead costs include those for direct overhead costs (i.e., corporate services) and indirect overhead costs (i.e., facilities and IT support related to employees providing corporate services).

For indirect overhead costs, FEI states that approximately $250,000 of the total $600,000 forecasted overhead for 2014 is for indirect overhead (facilities and IT support activities), the determination of which is less dependent on timesheet allocations.

6.1 Please clarify whether the “facilities and IT support” (as appeared in Slide 11 in Tab C2) refers to the facilitates and IT support to the 10 FAES employees or do they refer to the facilities and IT support provided to FEI employees who are providing services to FAES?

Response:

The facilities and IT support as shown in Slide 11 in Tab C2 includes both the facilities and IT support for the FAES dedicated employees and the facilities and IT support provided to FEI employees who are providing services to FAES.

6.2 If a proportion of FEI’s service time, e.g., the Regulatory Group, was spent on FAES matters, would the overhead charges also reflect a percentage of Human Resources’ time needed to staff and maintain the Regulatory Group, as well as an appropriate percentage of facilities costs and management time driven by the Regulatory Group? Is the practice of 10 percent load factor (Slide 54, Tab C3) supported by a study or research?

Response:

The indirect overhead charge of 10 percent includes the costs of the Human Resources group providing support to FEI employees (i.e. employee services, development, labour relations, etc). Additionally, the facilities charge of $100 per day covers the related facilities costs for an FEI employee. Management time incurred in support of specific FAES activities would be separately included as part of the direct overhead costs.

The overhead loading factors (ie. facilities charge and 10 percent general overhead loading) are supported by a study titled Transfer Pricing Methodology Review prepared by KPMG in June 2009. FEI retained KPMG to perform an independent review of the Transfer Pricing Methodology and to verify that the methodology used by FEI was complete and reasonable. Although there was no explicit determination in that study about the 10 percent, KPMG found that FEI's Transfer Pricing Methodology (which included that 10 percent charge) was reasonable. This review was filed as Appendix H-6 in the FEI (then Terasen Gas Inc.) 2010-2011 Revenue Requirement Application.

6.3 Slides 10 and 11 in Tab C2 show the FEI FAES overhead allocation. Please update the overhead allocation in Slides 10 and 11 for 2014 taking into account the recent Commission Decision on the FEI 2014-2018 PBR RRA. Please include year 2015 in your update.

Response:

The estimated overhead allocation is not affected by the Commission Decision in the FEI 2014-2018 PBR RRA. FEI anticipates the overhead allocation for 2014 will be approximately $625 thousand as indicated at the February 20, 2014 workshop and possibly lower. FAES has been investigating alternatives to provide greater separation from FEI and to replace some of the services currently provided by FEI. As a result, FEI expects the overhead allocation for 2014 and 2015 to be lower. For details of the $625 thousand overhead allocation estimate provided at the February 20, 2014 workshop, please refer to the response to BCUC IR 1.6.11.

The difference between the $625 thousand and the amount embedded in delivery rates for 2014 will be recorded in the TESDA Overhead Allocation Variance deferral account in FEI, and recovered from customers in 2015 in accordance with Order G-138-14 where at page 232 of the attached decision the Commission stated:

> *"The Commission Panel approves the establishment of the TESDA Overhead Allocation Variance deferral account. The Panel directs that the ending balance at December 31 each year be amortized over the following year."*

6.4 Counsel for FEI indicates that parent company Fortis Holding, Inc. allocates cost to FAES based on the Massachusetts Formula (T1:47). Please confirm, or otherwise explain, that the FEI executive management time cost is also allocated to FAES based on the Massachusetts Formula. Please confirm or explain whether the executive time cost is or is not reflected in the $850,000 overhead estimates in Slides 10 and 11. Please provide details in the allocation of the executive management time and how it is reviewed and tracked.

Response:

The statement by Counsel for FEI was in relation to the approved methodology to allocate corporate services costs from FortisBC Holdings Inc. to its subsidiaries, not the allocation of FEI costs to FAES. However, a clarification is still required. The Massachusetts formula is used to allocate FHI costs to FEI, but is not used to allocate FHI costs to FAES. Using the Massachusetts formula for FAES would result in little to no allocation to FAES because of its small size. FHI costs are allocated to FAES based on time estimates as is the case with the time of FEI executives allocated to FAES.

Note that the $850 thousand allocated from FEI to FAES for overhead is the amount determined by the Commission in the 2012-2013 RRA, not the amount that was based on FEI's assessment of time and overhead. This was explained in the response to BCUC Confidential IR 2.3.1 (Exhibit B-22) in the PBR proceeding:

> *3.1 Please confirm which services and support functions are included in the "overhead" allocation?*
>
> *<u>Response</u>:*
>
> *FEI provided a breakdown of the services and costs included in the overhead allocation for 2012 and 2013 as Attachment 78.1 provided in the response to BCUC IR 1.78.1 to the 2012-2013 RRA Application. FEI submitted that the appropriate amounts for 2012 and 2013 were $497,377 and $511,586 respectively. The supporting calculations for these amounts have also been provided in Attachment 353.1 provided in response to BCUC IR 2.353.1 in this proceeding. Since Commission Order G-44-12 for the 2012-2013 RRA Application directed that the allocation be adjusted to $750 thousand plus $92 thousand and $104 thousand for IT services in 2012 and 2013, FEI is unable to explain what additional costs might be included in the difference between the approximately $500 thousand and the approximately $850 thousand.*

In essence, FEI believes that the amount determined by the Commission in the 2012-2013 RRA far exceeded the amount that was justifiable based on the evidence in that proceeding relating to time and overhead costs. It should not be used as the baseline point of comparison for this year. The response to BCUC IR 1.6.11 provides the estimated amount of executive charges included in the original $511,586 estimate for 2013 and the current estimate of $625 thousand for 2014. As indicated in the respose to BCUC IR 1.6.3, in the future with the alternatives that FAES is investigating to replace some of FEI's services, FEI expects the overhead allocation to FAES to be lower.

6.4.1 Going forward, is it the position of FEI that the allocation of its executive management time to affiliate in an ARBNNM environment will be on the basis of the Massachusetts Formula? Time sheet? If other, please specify.

<u>Response:</u>

FEI has proposed that it would charge time for executive management using estimates of time.

6.5 In addition to the descriptions of mechanisms in place at FEI to ensure compliance on allocation of both direct and overhead activities (pages 11-12 of Exhibit B-7 for the proposed COC), please clarify if these mechanisms are newly introduced to FEI (as opposed to well-established) and that the $850,000 cost allocation introduced in the 2012-2013 RRA Decision has not been tracked, verified or supported by time sheets or any other tracking mechanisms.

<u>Response:</u>

Newly introduced is the requirement to have FEI employees who provide services to FAES complete timesheets on a regular basis. Previously, the company only estimated the time spent on FAES activities in support of the approximate $500 thousand overhead allocation proposed as part of FEI's 2010 and 2011 revenue requirement. The requirement to have FEI employees record their time spent in support of FAES' activities retroactively back to the beginning of 2014 was introduced in May 2014 shortly after the second stakeholder COC and TPP workshop, and in response to concerns expressed by Commission staff about validating the proposed overhead allocation to FAES. Since that time, FEI employees providing services to FAES have been completing timesheets to allocate their time to FAES, except for executive management's time which is still based on time estimates given the nature of executive support provided.

Newly introduced also is the insertion of the Director of Finance role into the monitoring process. The Director of Finance will also review charges on a quarterly basis and seek confirmation from department managers that the allocations to FAES are appropriate. Additionally, FAES may also review the validity of the charges.

The established controls include:

- annual reminder to all employees of the COC and TPP;
- reference in the company's Business Ethics course which all employees are required to take;
- monitoring of costs by the Financial Accounting group; and
- use of internal orders to track costs.

With the above process and controls in place for 2014, FEI is tracking and would be able to provide the details necessary to support the overhead allocation to FAES. As indicated in the response to BCUC IR 1.6.3, FEI's current estimate of the 2014 overhead allocation to FAES is approximately $625 thousand and are expected to be lower and not the $850 thousand introduced in the 2012-2013 RRA Decision.

6.6 In Slide 11, the chart shows that FEI allocated approximately $500,000 to FAES as overhead allocation in 2012. Please confirm that, as a result of this allocation, the $500,000 was not captured in the FEI revenue requirement. If confirmed, please clarify if the $500,000 was included in the FAES revenue requirement or if the amount, or some of the amount, is in the deferral account TESDA which is described in Slide 10.

Response:

Not confirmed.

The $500 thousand overhead allocation was captured for 2010 and 2011 in the 2010 and 2011 FEI revenue requirement and not in the 2012 and 2013 FEI revenue requirement. $842 thousand and $854 thousand were the relevant amounts of overhead for 2012 and 2013 respectively in the 2012 and 2013 revenue requirement. These amounts reduced the FEI revenue requirements in those two years to the benefit of the FEI ratepayers.

As indicated in Slide 10, the $500 thousand was recorded in the TESDA account for 2010 and 2011. The 2012 and 2013 amounts were also recorded in the TESDA account.

6.7 Please provide a continuity schedule for TESDA for the period 2010 to 2014 to show the opening balance, the annual allocation to TES projects, the amortization of the overhead balance, and the ending balance.

Response:

The follow table is a continuity schedule of TESDA for the period of January 1, 2010 to September 30, 2014. The credit amounts under "Projects Specific Costs" are the transfers to the TES projects in FAES. The "General O/H" line is the amount being allocated from FEI to the TESDA.

	2010	**2011**	**2012**	**2013**	**2014**
Opening balance	0	2,530	5,770	13,112	10,759
General O/H	500	500	842	854	653
Project Leads Gen Business Dev	1,435	1,635	670	845	492
Regulatory/Inquiry Costs	0	107	543	70	71
General Development Costs	1,935	2,242	2,054	1,769	1,217
Project Specific Costs	1,196	1,848	4,767	(4,153)	1,493
Net of tax	(682)	(1,125)	0	(507)	(662)
AFUDC	82	274	521	537	640
	(600)	(851)	521	30	(22)
Total	2,530	5,770	13,112	10,759	13,446

The following excerpt is from FEI's 2010-2011 FEI Negotiated Settlement Agreement, where the parties agreed that the costs incurred to provide alternative energy services would be captured in a deferral account:

The Parties agree that the costs incurred by TGI to provide AES should not be recovered as part of natural gas service rates, and visa versa. The Parties agree that TGI's proposed New Energy Solutions Deferral Account, attracting AFUDC, is an appropriate mechanism to address allocation issues as between TGI's gas customers and TGI's AES customers. Therefore, the Parties agree that the new Energy Solutions Deferral Account will remain in effect pending a future rate design application at an unspecified future date after 2011 and will capture and record the following (plus AFUDC) to be recovered from AES customers:

(a) Direct costs associated with AES projects as outlined on pages 267-268 of the Application, including cost of design, equipment, etc. constructing and financing; and

(b) Sales and marketing O&M and other development costs will be directly charged to the deferral account by time sheets or other direct charge (estimated at $1.0 million in 2010 and $1.5 million in 2011, representing a portion of the agreed upon Gross O&M reduction from gas customers of $4.0 million in 2010 and $5.5 million in 2011); and

(c) An appropriate overhead allocation, which the parties have agreed will be $500,000 in each of 2010 and 2011 (representing a portion of the agreed upon Gross O&M reduction from gas customers of $4.0 million in 2010 and $5.5 million in 2011).

Revenues received from customers for all AES projects, which are based on contracts approved by Commission will be recorded in the AES deferral account.

6.8 Please confirm that each of the identified costs (a, b, c above) are all captured in the TESDA. Please clarify the following: (1) Is category (b) no longer applicable because FAES has its own business development staff? and (2) Is it the position of FEI that the current COC/TPP Application proceeding reviews only the transfer pricing policy of item (c) above? If yes, please comment on what principles should be involved in reviewing the cost allocations of items (a) and (b) above?

Response:

Most of these costs (a, b, c) are now directly incurred by FAES. Direct costs in (a) are primarily incurred by FAES and captured in the TESDA. Category (b) is no longer applicable in the case of FEI because FAES has its own business development staff; but these costs, which are now incurred by FAES, are also captured in the TESDA.

The current process reviews item (c) and the direct costs of FEI that remain from item (a). There are no FEI cost allocation principles to be reviewed for the remainder of the items since the costs are incurred directly by FAES. As confirmed by Order G-151-14, determinations regarding the disposition of the balance in the TESDA will be the subject of a future application from FAES.

6.9 Please explain how Sales and Marketing and other Business Developments costs (item c above) differ from item (b) above.

Response:

Item (b) has the sales and marketing and business development costs that are now directly incurred by FAES and charged to the TESDA. FEI does not see any reference to sales and marketing or business development costs in item (c) and confirms it does not contain these costs.

6.10 In the Supplementary Information, the response to Request No. 6, FEI describes "direct cost" to include costs for activities that relate to a particular FAES project or projects; and "overhead costs" as costs including corporate services. Are these descriptions of costs similar to the cost descriptions in the NSA referred to in question 6.8 above?

Response:

Yes. Direct costs are included in item (a) from the NSA and overhead costs are equivalent to item (c) from the NSA. Sales and business development activities and costs item (b) from the NSA are incurred by FAES and no longer provided from FEI.

The list of life cycle costs originally set out to be captured in item (a) on pages 267 and 268 of the 2010-2011 RRA included:

- Capital expenditures (equipment, materials, land, installation costs, capital replacements, contributions);
- O&M expenditures (direct labour, replacement parts, equipment, material and administration);
- Inflation;
- Income tax;
- Depreciation;
- Capital Cost Allowance; and
- Cost of Capital.

These types of costs are now directly incurred by FAES and allocated to TES projects.

6.11 Please provide a list of cost that makes up the total overhead allocation of $850,000 as shown in Slide 11 in Tab C2. In responding to this question, it would be helpful to provide a table that shows all of the types of costs that are allocated to FAES as overhead costs. Please breakdown the types of costs into specific categories, i.e., overhead related to IT services provided to FAES, human resource services provided to FAES, executive management services, etc.

Response:

Following is the table requested showing the types of costs that are allocated to FAES as overhead costs and totaling to $854 thousand as indicated in the Commission's decision on FEI's 2012/2013 revenue requirement. In that decision, the Commission found that "a more reasonable allocation of overhead and sales and marketing cost is $750 thousand for each year of the test period."[2] In addition, the Commission directed an increase of $94 thousand in 2012 and $104 thousand in 2013 for IT related costs.

Included in the table is FEI's estimate of the overhead allocation. As indicated at the February 20, 2014 workshop, FEI reviewed and updated the overhead allocation and believes a more representative amount is approximately $625 thousand in 2014 and possibly lower. As noted in the response to BCUC IR 1.6.3, FAES has been investigating alternatives to provide greater separation from FEI and to replace some of the services currently provided by FEI. As a result, FEI expects the overhead allocation for 2014 and 2015 to be lower.

[2] Pages 4 and 65 of the Decision.

		2012 / 2013 RRA For Year 2013		2014	
Total Overhead Costs Allocated to FAES			854,000		624,505
Commission Ordered			342,314		-
	IT	104,000		-	
	Marketing and Customer Service	238,314		-	
Finance			40,381		78,851
Regulatory Affairs			122,443		121,860
Human Resources			11,280		10,968
Procurement			-		6,940
Information Technology			51,228		120,610
Facilities			228,319		214,817
Communications			-		2,925
Executive			58,035		67,534

In the recent 2014-2018 FEI PBR RRA proceeding, in response to a Commission Information Request question on FEI cost allocation to FAES, FEI responded as follows:

> “205.4.1 On what basis would the FEU allocate costs to the requested deferral account for TES? The Massachusetts Formula? If not, what is the placeholder amount based on?

Response: The placeholder amount is based on the amount charged that was approved in BCUC Order G-44-12. As a result of the AES Inquiry, FEI will be undertaking a review of the Code of Conduct and Transfer Pricing Policy and any variance in this charge would be put into the deferral account. As submitted in the 2012-2013 RRA, the estimate of approximately $500 thousand that was provided was based on an estimate of time for executive and support services provided to the alternative energy business but this may not be the allocation methodology determined appropriate in the TPP/COC review.” (Exhibit B-11, BCUC IR 205.4.1, FEI 2014-2018 PBR RRA)

6.12 Given the response in the PBR RRA proceeding that the placeholder amount that was provided was based on an estimate of time, would FEI please clarify what has been done to date to provide evidence or support data on the $850,000 FEI FAES Overhead Allocation?

Response:

The response quoted in the preamble above did not say that the placeholder amount that was provided was based on an estimate of time. FEI stated that the amount was based on the approved amount per BCUC Order G-44-12. It was the $500 thousand amount that was originally proposed by FEI to be allocated to the TESDA that was based on an estimate of time. This is explained in the response to BCUC IR 1.6.4.

Since the approximately $850 thousand amount is the sum of FEI's original estimate of approximately $500 thousand plus the additional amounts ordered by the Commission, FEI is unable to provide supporting data for the $850 thousand. Instead, FEI reviewed the allocation and believes a more a representative amount is $625 thousand and possibly lower. Please refer to the response to BCUC IR 1.6.3 for discussion of lower overhead allocation and also to to the response to BCUC IR 1.6.11 for details of the $625 thousand and $850 thousand amounts.

7.0 Reference: Exhibit B-7, Supplementary Information, Request No. 6, pp. 11-12

Exhibit B-1, Tab B5, Comments from the Coalition for Open Competition

Cost Collection Processes and Controls

FEI states that "completion of timesheets is done on an exception basis for all management and most unionized office staff employees, regardless of whether the allocation is to an FEI project, a deferral account, another department, or another entity, and is a well-established process. Employees are indifferent, whether financially or otherwise, as to where their time is allocated." [emphasis added]

The Application at hand began in mid-2013 and FEI senior management and officers led the consultative process which included stakeholders' meetings and workshops. In addition FEI prepared the Application and participated in the Commission Pre-hearing Conference. FEI has, throughout its engagement, been advocating a position which it believes is in the interests of both FEI and FAES ratepayers. The Coalition noted in its comments that Mr. Stout was listed in the minutes of the April 24th Workshop as an FAES participant in addition to his participation for FEI.

7.1 Please describe in detail the cost of representing FAES by FEI management and staff in this proceeding and how is the cost being allocated to FAES. Please affirm that the cost collection process and controls as described on pages 11 and 12 work in accordance with the established process. If the participation time of FEI management and staff has not yet been allocated to FAES since mid-2013, please provide comments on possible improvement to the tracking of both direct and overhead activities described on pages 11 and 12.

Response:

FEI time spent in the current proceeding in support of FEI's application on its proposed CoC/TPP is to the account of FEI and not FAES. To date, FEI has not tracked and allocated any time related to this proceeding to FAES, since FEI management has only been engaged in representing FEI. FAES has represented itself since the first workshop, with FAES employees investing their own time in attending workshops and in assisting with preparing material and responses to information requests as required. FAES also pays for its own separate legal representation in this proceeding.

As to Mr. Doug Stout's time in the proceeding, his time consists primarily of preparation and attendance at both workshops. Given that Mr. Stout represented the interests of both FEI and FAES, some of his time for the two workshops would be attributable to FAES. This is already addressed by the executive management provision provided for in the overhead allocation to FAES from FEI.

8.0 Reference: Exhibit B-7, Supplementary Information, Request No. 7, p. 15; Transcript (T1:120)

FEI PBR 2014-2019

FEI states that it would be prepared to file a summary of the charges by FEI to FAES as part of the Annual Review material in the FEI PBR 2014-2019. It also states that during these Annual Review processes, FEI will be bringing forward any revisions to methodologies for allocating existing corporate services, and any future proposals for implementing a shared services agreement with FortisBC Inc.

8.1 At the Pre-hearing Conference, the counsel for FEI indicated that FEI did not disagree with the long-term objective of moving towards a combined COC and TPP document that would address regulated affiliates (natural monopoly environment and non-natural monopoly environment) and non-regulated affiliates. Please comment on a timeline in working towards one integrated document?

Response:

The timeline on preparing a combined COC and TPP document depends to a large degree on the regulatory process required, the interest and availability of interested parties and the number of contentious issues. The current proceeding has taken more than a year, in part due to the number of contentious issues, the different perspectives of interested parties and the regulatory process directed.

In the development of a COC and TPP for NRBs, there may be contentious issues raised that result in an extended regulatory process including possibly stakeholder consultation required. This will affect and extend the overall timeline. Similarly, for a COC for natural monopoly affiliates, likely involving a different set of interested parties, the timeline would depend on the issues, and the regulatory process chosen including any stakeholder consultation.

Before any work on an integrated document is initiated, an approved COC and TPP in this proceeding for ARBNNMs is required. Given the current timeline to complete this proceeding, FEI anticipates that a decision may be forthcoming in the first quarter of 2015. The timeline to subsequently complete a COC and TPP for NRBs and natural monopolies would depend on the factors discussed above.

At this time, FEI believes the process could be completed as early as late 2015 or as late as early 2017, depending on the process and interest of other parties. If the Commission requires a consultative process, based on the recent experience on the COC / TPP for ARBNNMs, then it may be well into 2016 and early 2017 before this process would be complete. However, if the Commission is willing to accept an FEI-proposed amendment to the COC / TPP for ARBNNM to incorporate consideration of non-regulated affiliates, the process would likely be much quicker. The development of a COC for natural monopoly affiliates is expected to proceed more quickly as there will likely be less contentious issues.