

Fasken Martineau DuMoulin LLP *

Barristers and Solicitors
Patent and Trade-mark Agents

2900 - 550 Burrard Street
Vancouver, British Columbia, Canada V6C 0A3

604 631 3131 Telephone
604 631 3232 Facsimile

www.fasken.com



Matthew Ghikas

Direct +1 604 631 3191
Facsimile +1 604 632 3191
mghikas@fasken.com

November 12, 2014
File No.: 240148.00739/14797

BY E-MAIL

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

Attention: Erica Hamilton
Commission Secretary

Dear Sirs/Mesdames:

Re: FortisBC Energy Inc.
Application Approval for Code of Conduct and Transfer Pricing Policy for
Affiliated Regulated Businesses Operating in a Non-Natural Monopoly
Environment

We enclose for filing in the above proceedings the Final Submission on behalf of FortisBC Energy Inc. dated November 12, 2014.

Ten hard copies of the Final Submission will follow by courier.

Yours truly,

FASKEN MARTINEAU DuMOULIN LLP

[original signed by Matthew Ghikas]

Matthew Ghikas

MTG/fxm
Enc

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

BRITISH COLUMBIA UTILITIES COMMISSION

IN THE MATTER OF THE UTILITIES COMMISSION ACT

R.S.B.C. 1996, CHAPTER 473

and

FORTISBC ENERGY INC.

**APPLICATION FOR APPROVAL OF CODE OF CONDUCT AND TRANSFER
PRICING POLICY FOR AFFILIATED REGULATED BUSINESSES OPERATING
IN A NON-NATURAL MONOPOLY ENVIRONMENT**

FINAL SUBMISSION OF

FORTISBC ENERGY INC.

November 12, 2014

TABLE OF CONTENTS

PART ONE: INTRODUCTION	1
PART TWO: THE FACTS	2
A. FACTS PERTINENT TO THE CODE OF CONDUCT	2
B. FACTS PERTINENT TO THE TPP	4
C. COMPLIANCE MEASURES	5
PART THREE: GOVERNING LEGAL FRAMEWORK	6
A. REGULATION OF RATES, NOT MARKETS	6
B. STATUTORY OBLIGATIONS TO PUBLIC UTILITIES AND THEIR CUSTOMERS	8
(a) <i>The Regulatory Compact Applies to FEI and FAES</i>	8
(b) <i>Benefits to FAES Customers and FAES Shareholder</i>	8
PART FOUR: SUBMISSIONS ON AREAS OF SUBSTANTIVE DISAGREEMENT	11
A. CODE OF CONDUCT PRINCIPLES	11
B. CODE OF CONDUCT SECTION 2 - SHARED SERVICES AND PERSONNEL	11
(a) <i>Sharing of Business Development Personnel Precluded</i>	12
(b) <i>Corporate Services Employees</i>	12
(c) <i>Directors and Executives</i>	13
(d) <i>Summary</i>	15
C. TRANSFER PRICING POLICY – SECTION 1 PRICING RULES, (II) AND SECTION 2 DETERMINING COSTS	16
(a) <i>FEI is Already Charging Rates Consistent With Market Rates</i>	16
(b) <i>FEI’s Proposal Consistent with Regulatory Principles and Jurisdiction</i>	18
(c) <i>Consistent With Cost Causality</i>	18
(d) <i>Consistent With Jurisdiction of Commission</i>	19
PART FIVE: APPROPRIATE SAFEGUARDS IN PLACE	20
A. SAFEGUARDS RELATING TO COMPLIANCE WITH CODE OF CONDUCT	20
B. SAFEGUARDS RELATING TO TRANSFER PRICING	21
PART SIX: CONCLUSION	23

PART ONE: INTRODUCTION

1. Codes of conduct (“CoC”) and Transfer Pricing Policies (“TPP”) are appropriate tools for advancing the legislative objective of ensuring that public utility rates are and remain just and reasonable. It is fundamental to the Commission’s consideration in this proceeding that, unlike circumstances where a regulated utility is providing labour and administration to a non-regulated business (“NRB”), both FortisBC Energy Inc. (“FEI” or “the Company”) and an Affiliated Regulated Business Operating in a Non-Natural Monopoly Environment (“ARBNNM”) are public utilities. The Commission owes both utilities and both sets of regulated ratepayers a statutory duty to ensure that rates are just and reasonable.

2. FEI has proposed a TPP and a CoC that promote just and reasonable rates for FEI and its customers by ensuring that (a) FEI receives fair value for its services and (b) FEI takes reasonable steps to protect information in its possession. At the same time, the proposal is fair to the ARBNNM (which, in reality, is only FortisBC Alternative Energy Services Inc. (“FAES”)) and its customers by allowing the ARBNNM/FAES to access corporate and operational services from FEI at a reasonable price in appropriate circumstances. FEI respectfully submits that the Commission should approve the Company’s proposed CoC and TPP.

3. The remainder of this Final Submission is organized as follows:

- Part Two summarizes the essential facts.
- Part Three addresses the legal framework that governs the Commission’s determination of this Application.
- Part Four addresses each of the four areas of substantive disagreement¹, supplementing the written submissions filed by the Company in advance of the pre-hearing conference (“Pre-Hearing Conference Submission”).²
- Part Five outlines the safeguards in place to advance the objectives of the TPP and CoC.

¹ The substantive disagreements among stakeholders were identified in the spreadsheet filed by FEI on September 2, 2014, Exhibit B-3.

² Exhibit B-4.

PART TWO: THE FACTS

4. The essential facts in this Application are summarized below. The evidence demonstrates that: (i) FAES is the only ARBNM; (ii) the services provided by FEI to FAES represent a limited amount of work by a limited number of FEI staff; (iii) FAES is paying a fair price to FEI for corporate and operational services; and, (iv) FEI is taking appropriate steps to protect confidential information.

A. FACTS PERTINENT TO THE CODE OF CONDUCT

5. The facts most pertinent to the Commission's consideration of the proposed CoC are:

- The FEI staff that had originally been dedicated to supporting thermal energy services were transferred to FAES at the beginning of 2014.³
- FEI staff that continue to provide corporate and operational services to FAES are providing FAES with "a few hours at a time when other work priorities allow."⁴
- None of the individual positions providing services to FAES are providing a number of hours that constitute "anywhere near the equivalent of a full-time position".⁵
- The apparent perception that the FEI Regulatory department has had to increase staff to address FAES workload is mistaken. The fact that finance and regulatory staffing has declined over the period since FEI began dealing with thermal energy services underscores this point.⁶
- When FEI staff carry out their responsibilities, natural gas customers receive priority of service and FAES' requirements are in secondary priority.⁷

³ Ex. B-7, FEI Supplemental Information, Response to Question 2, p.4.

⁴ Ex. B-9, BCUC IR 1.1.2.

⁵ Ex. B-9, BCUC IR 1.1.2.

⁶ Ex. B-9, BCUC IR 1.1.2; Ex. B-11, COC IR 1.1.1.

⁷ Ex. B-11, COC IR 1.1.2.

- FAES staff's access to technology is restricted to ensure they have no access to FEI confidential information.⁸
- There are only three individuals at FAES who are engaged in business development.⁹ FAES and FEI business development staff no longer report to the same individual.¹⁰
- There are only three officers of FEI that are also officers of FAES. Only two of those individuals are engaged in market development (the third is a corporate governance support role only),¹¹ and those two individuals play very different roles for each corporation:
 - Doug Stout is the President of FAES and FEI's VP Market Development & External Relations. His market development role within FEI has recently changed; he is now focused on the development of major projects such as the Tilbury LNG facility expansion and LNG/CNG market development.¹²
 - Gareth Jones is the Vice President and General Manager of FAES and Director, Business Development with FEI. Mr. Jones' responsibilities for FEI relate to FEI's natural gas transportation business and the Tilbury LNG plant expansion.¹³
- FAES has been investigating alternatives to provide greater separation from FEI and to replace some of the services currently provided by FEI.¹⁴

⁸ Ex. B-9, BCUC IR 1.3.1.

⁹ Ex. B-9, BCUC IR 1.1.1.

¹⁰ Ex. B-9, BCUC IR 1.3.2.

¹¹ The same individual fills the roles of FEI's Assistant Corporate Secretary and FAES' Corporate Secretary.

¹² Ex. B-11, COC IR 1.2.1.

¹³ Ex. B-11, COC IR 1.2.1.

¹⁴ Ex. B-9, BCUC IR 1.6.3; Ex. B-10, COPE IR 1.1.3.

B. FACTS PERTINENT TO THE TPP

6. With respect to the Commission's consideration of the proposed TPP, FEI charges to FAES the costs of providing those services.¹⁵ The key facts in this regard are:

- Direct costs include costs for activities that relate to a particular FAES project or projects. The direct costs are allocated based on work effort. FEI staff use time sheets to charge FAES for the time they spend in providing services, which is a long-established practice.¹⁶
- Management time incurred to provide oversight of FEI employees working on specific FAES activities is separately included as part of the direct overhead costs.¹⁷ Since May 2014, all non-executive FEI employees providing services to FAES have been completing timesheets to allocate their time to FAES. FEI will thus be able to provide the details necessary to support the overhead allocation to FAES in 2014 and subsequent years.¹⁸
- FEI charges time for executive management using estimates of time, given the nature of the work that they perform.¹⁹
- FEI charges an indirect overhead charge of 10 percent for FEI employees providing support to FAES and located at FEI's offices (i.e. general overhead loading represent services that facilitate the day-to-day functions of all employees including Human Resources/Payroll, Corporate Safety, Office Services), plus a facilities charge of \$100 per day. The facilities charge represent a list of related expenses including office space, telephone, office supplies, office furniture and equipment, SAP and Microsoft licenses.²⁰ The 10 percent general

¹⁵ Ex. B-9, BCUCs IR 1.6.8 to 1.6.10 provide a comparison to what was being done prior to the dedicated thermal energy services employees being transferred to FAES.

¹⁶ Ex. B-7, FEI Supplemental Information, Response to Question 6, p.11.

¹⁷ Ex. B-9, BCUC IR 1.6.2.

¹⁸ Ex. B-9, BCUC IR 1.6.5.

¹⁹ Ex. B-9, BCUC IR 1.6.4.1.

²⁰ Ex. B-7, FEI Supplemental Information, Response to Question 6, p.13; Ex. B-9, BCUC IR 1.6.2.

overhead loading and facilities charge of \$100 per day are supported by a study prepared by KPMG.²¹

- Any other overhead costs in addition to the labour charges, such as equipment charges (as outlined in Appendix A of the FEI proposed TPP) will be charged directly to FAES.²²
- As a result of FAES investigating alternatives to provide greater separation from FEI and to replace some of the services currently provided by FEI, FEI expects the overhead allocation for 2014 and 2015 to be lower with decreasing amounts of time required from FEI employees.²³

C. COMPLIANCE MEASURES

7. The measures and processes in place to reinforce compliance with the CoC and TPP are addressed in Part Five of this Final Submission. The submissions in Part Five demonstrate that FEI has taken appropriate steps to augment its existing compliance framework.

²¹ Ex. B-9, BCUC IR 1.6.2.

²² Ex. B-7, FEI Supplemental Information, Response to Question 6, p.13.

²³ Ex. B-9, BCUC IR 1.6.3; Ex. B-10, COPE IR 1.1.3.

PART THREE: GOVERNING LEGAL FRAMEWORK

8. Part Two addresses two key aspects of the legal framework that bear on the Commission's determination of this Application:

- The Commission regulates rates, not markets; and
- The Commission owes statutory duties to FEI and FAES and their respective customers to ensure that utility rates are just and reasonable.

A. REGULATION OF RATES, NOT MARKETS

9. The Commission regulates rates, not markets. FEI's proposed TPP and CoC are consistent with the statutory purpose of ensuring just and reasonable public utility rates. The changes proposed by Corix and the Coalition are inconsistent with that purpose.

10. As a statutory body, the Commission's powers extend only to those conferred by legislation, i.e., the *Utilities Commission Act* ("UCA"). The Supreme Court of Canada emphasized in the *ATCO* decision²⁴ the centrality of just and reasonable rates to the jurisdiction of a utility regulator:

The limits of the powers of the Board are grounded in its main function of fixing just and reasonable rates ("rate setting") and in protecting the integrity and dependability of the supply system.²⁵

All of the powers conferred upon the Commission under the UCA, including the powers to approve a TPP and CoC, flow from one or both of these two main functions.

11. Competition and markets are regulated under a separate legislative framework. The Commission, in the AES Inquiry Report, expressly acknowledged that the regulation of Competition was not the role of the Commission:

²⁴ *ATCO Gas & Pipelines Ltd. ("ATCO") v. Alberta (Energy & Utilities Board)* 2006 SCC 4
<https://scc-csc.lexum.com/scc-csc/scc-csc/en/item/17/index.do>.

²⁵ *ATCO*, para.7

While the Commission does not regulate competition per se, the Panel accepts that it should not act to hinder competition, where competition is feasible. In this regard, the Commission Panel confirms that there must be no cross-subsidization when a utility purports to enter a competitive market.²⁶

12. The effect on the competitive market from the avoidance of cross-subsidization (“not hindering competition”) must only be a by-product of the Commission ensuring that the utility rates are just and reasonable (i.e., ensuring that rates reflect no more than a reasonable cost for the nature of the service provided, per section 59(4)). Any step taken for the purpose of affecting the market would be invalid. This point is underscored by the legal opinion of Commission Counsel (Gordon Fulton, Q.C.) that was requested by, provided to, and quoted by the Commission Panel in the 1997 Retail Markets Downstream of the Utility Meter proceeding. Mr. Fulton had concluded:

2. The Commission has the jurisdiction to regulate the relationship between a public utility and an affiliated NRB to the extent that the relationship affects ratepayers. For example, the Commission has the jurisdiction to ensure that an NRB is not 'subsidized' by a public utility to the detriment of ratepayers.

3. The Commission does not, however, have the jurisdiction to regulate the relationship between a public utility and an NRB so as to ensure the relationship does not affect the competitive retail market downstream of the meter. The Commission's jurisdiction is limited to consideration of the effects of the relationship on ratepayers.²⁷ [Emphasis added.]

13. The Commission’s jurisdiction is relevant in the current Application because the content of FEI’s TPP/CoC should be determined based on what is reasonably necessary to ensure that utility rates remain just and reasonable. FEI customers receive incremental revenues from providing administrative and operational services to FAES.²⁸ Measures intended to limit sharing of FEI resources with FAES beyond what is reasonably required to either ensure FEI rates to remain fair or to safeguard the interests of FEI ratepayers, by definition, could only be intended to achieve some market result with respect to thermal energy services. It would represent an implicit subsidy to competitors of FAES at the expense of both FEI, FAES and their

²⁶ AES Inquiry Report, p.14.

²⁷ *Retail Markets Downstream of the Utility Meter Guidelines*, April 1997, p.8.

²⁸ Approximately \$850K was included in FEI rates in each of 2012 and 2013 as a recovery from FAES.

respective customers. That type of subsidy would stray well beyond the Commission's jurisdiction.

B. STATUTORY OBLIGATIONS TO PUBLIC UTILITIES AND THEIR CUSTOMERS

14. In the context of this Application, there are two regulated public utilities involved, FEI and FAES. Each of those utilities has customers and a shareholder to whom the UCA and the regulatory compact applies. The Commission meets its statutory duties to FEI customers, FEI, FAES customers, and FAES by approving a CoC/TPP that allows FEI to optimize its resources for the benefit of its own customers by providing FAES and/or FAES customers with access to FEI resources at a fair price where FEI can do so without compromising its own operations.

(a) The Regulatory Compact Applies to FEI and FAES

15. FEI and FAES are public utilities under the UCA.²⁹ The Commission must approve just and reasonable public utility rates. Section 59(4) of the UCA, in particular, establishes the requirement to approve public utility rates that are (to paraphrase) neither too high for the nature of the service provided, nor too low so as to deny a reasonable opportunity to earn a fair return. This is a reflection of the regulatory compact. The fact that the regulatory compact applies to both FEI and FAES is well established. For instance, the Commission applied the Fair Return Standard to both FEI and FAES in the 2013 Generic Cost of Capital (Phase 1 and 2) Decisions.

(b) Benefits to FAES Customers and FAES Shareholder

16. One of topics canvassed at the Pre-Hearing Conference³⁰ and in a supplemental question from the Panel is the extent to which FAES *customers* (as opposed to FAES' *shareholder*) benefit from FAES obtaining human resources from FEI. FEI has demonstrated that FAES customers are affected by the price and quality of services obtained by FAES.³¹ FEI's

²⁹ Even FAES' micro-TES and Stream A thermal energy projects remain subject to Commission oversight.

³⁰ Discussion starting at T1: 129, line 22.

³¹ Ex. B-7, FEI Supplemental Information, Response to Question 5, pp.9-10

proposal is not predicated on demonstrating that 100% of any of FAES' cost savings are passed on dollar for dollar in the rates paid by FAES customers. We say this for three related reasons.

17. First, FEI customers are already benefitting from capitalizing on economies of scope.³² Provided that FEI and FEI customers are being treated fairly under the CoC/TPP, the Commission should view the result as favourable irrespective of how benefits accruing to FAES are allocated as between FAES' shareholder and FAES customers.

18. Second, any benefits to FAES from economies of scope that are not passed on directly to customers promote the sustainability of what amounts to a start-up utility business. The Commission must give weight to the desirability of FAES being able to maintain its operations as a profitable going concern. The Supreme Court of Canada recognized this obligation in the *ATCO* case, where the Court cited the principle of "sustainability" as one of the three objectives of utility rate regulation:

Rate regulation serves several aims — sustainability, equity and efficiency — which underlie the reasoning as to how rates are fixed:

...the regulated company must be able to finance its operations, and any required investment, so that it can continue to operate in the future.... Equity is related to the distribution of welfare among members of society. The objective of sustainability already implies that shareholders should not receive "too low" a return (and defines this in terms of the reward necessary to ensure continued investment in the utility), while equity implies that their returns should not be "too high".

63 These goals have resulted in an economic and social arrangement dubbed the "regulatory compact", which ensures that all customers have access to the utility at a fair price — nothing more. As I will further explain, it does not transfer onto the customers any property right. Under the regulatory compact, the regulated utilities are given exclusive rights to sell their services within a specific area at rates that will provide companies the opportunity to earn a fair return for their investors. In return for this right of exclusivity, utilities assume a duty to adequately and reliably serve all customers in their determined territories, and are required to have their rates and certain operations regulated.

³² FEI Ex. B-9, BCUC IR 1.1.2.

64 Therefore, when interpreting the broad powers of the Board, one cannot ignore this well-balanced regulatory arrangement which serves as a backdrop for contextual interpretation. The object of the statutes is to protect both the customer and the investor. The arrangement does not, however, cancel the private nature of the utility. In essence, the Board is responsible for maintaining a tariff that enhances the economic benefits to consumers and investors of the utility.³³ [Italics and ellipses in original; underlining added for emphasis.]

19. Third, the allocation of risk, cost and reward as between FAES and its customers is a matter of FAES rate design, and the Commission has already provided clear direction to FAES to adopt more market-based rates rather than classic cost of service ratemaking.³⁴ Part and parcel of any market-based approach is that FAES is being encouraged to reduce its cost structure for its own benefit as well. Having made a policy decision in favour of more market-based rates, the Commission should decide this Application without delving into FAES rate design.

20. In short, realizing economies of scope benefits FEI, FEI customers, FAES and FAES customers. It is a “win-win-win-win” as it relates to the Commission’s mandate.

³³ ATCO, paras. 62-64 (in-text citations omitted).

³⁴ *In the Matter of FEI’s Application for CPCN for Approval of Contracts and Rate for Public Utility Service to Provide Thermal Energy Service to Delta School District No. 37*, Decision, p.83. “In a competitive environment, the Panel is not convinced that a COS model, where any cost overruns are paid by the ratepayer, is the most appropriate pricing model as competition itself will incent the service provider to determine a fair price. It is clear that the own/operate model contains much stronger built-in incentives to increase efficiency, reduce costs and enhance performance, which a regulator would struggle to emulate within the COS model. In the presence of an actively competitive market, there appears to be no reason to apply a model which was developed to be a surrogate for competition. The Panel sees the traditional COS rate-base model as the ‘model of last resort’ that was initially developed for traditional utilities with natural monopoly attributes.”

PART FOUR: SUBMISSIONS ON AREAS OF SUBSTANTIVE DISAGREEMENT

21. Part Four addresses each of the four areas of substantive disagreement, either supplementing or summarizing FEI's Pre-Hearing Conference Submission.³⁵ The four areas of substantive disagreement are:

- CoC Principles;
- CoC Section 2 - Shared Services and Personnel;
- CoC Section 8 - Financing and Other Risks; and
- TPP Section - Pricing Rules and Determining Costs

A. CODE OF CONDUCT PRINCIPLES

22. The dispute over the CoC principles centres on the fact that FEI's proposal contemplates consideration being given to the interests of both FEI customers and FAES customers (see, e.g., principle 1³⁶). Interveners are divided in to two "camps" on this issue. Customer groups and COPE support FEI's proposal, and FAES' competitors (Corix and Coalition for Open Competition) oppose consideration of FAES ratepayers.³⁷ FEI submits that its proposal is appropriate because it reflects the governing legal principles articulated in Part Two above.

B. CODE OF CONDUCT SECTION 2 - SHARED SERVICES AND PERSONNEL

23. FEI's proposal with respect to Shared Services and Personnel is set out on p.7 of the Application. It precludes the sharing of business development staff, but otherwise provides flexibility for resource sharing arrangements that (i) benefit both FEI customers and ARBNNM/FAES customers, and (ii) present limited potential for disclosure of confidential information. FEI addressed why the Company's proposed wording with respect to sharing of services and personnel with an ARBNNM is appropriate on p.6 of its Pre-Hearing Conference

³⁵ Exhibit B-4.

³⁶ Ex. B-1, Application, Appendix A1, p.3, principle 1: "The advancement and the protection of the interests of the regulated ratepayers of [FortisBC Energy] and the ARBNNM should be considered."

³⁷ Exhibit B-3.

Submission. FEI elaborates below, with these submissions organized according to the three relevant employee groups: business development personnel; support employees; and, directors and executives.

(a) Sharing of Business Development Personnel Precluded

24. The primary objection raised in the past by FAES' competitors when it came to sharing of FEI personnel with FAES related to business development personnel. FEI has addressed this issue:

- The individuals responsible for FAES' business development (of which there are three³⁸) have already been transferred to FAES effective January 1, 2014.³⁹ There is currently no sharing of business development employees.
- FEI's proposed CoC language precludes sharing of FEI's business development personnel.⁴⁰

(b) Corporate Services Employees

25. FEI's proposal permits FEI to provide corporate services to an ARBNNM. FEI submits that there is no principled reason to preclude FEI corporate services employees from providing those services. FEI says this for three main reasons.

26. First, the work performed by FEI's corporate services is of a nature such that a conflict of interest that could result in a negative impact on FEI ratepayers is unlikely to arise.⁴¹ The corporate services provided by FEI are operational, technical or administrative in nature, not related to business development. The employees involved would be unlikely to come into

³⁸ Ex. B-9, BCUC IR 1.1.1. The other seven employees provide admin, finance, regulatory, engineering, project management and operational services.

³⁹ Ex. B-7, FEI Supplemental Information, Response to Question 2, p.4.

⁴⁰ Ex. B-7, FEI Supplemental Information, Response to Question 1, p.1.

⁴¹ Ex. B-7, FEI Supplemental Information, Response to Question 1, p.1.

contact with information that would be of use to FAES from a business development perspective. As FEI stated in its supplemental evidence:⁴²

The employees or functions of FEI that continue to serve FAES for functions other than business development do so only as a small portion of their responsibilities, and remain primarily dedicated to serving FEI. Among these, the functions or personnel who are likely to have commercially valuable information are limited in number. They could potentially include other sales personnel including key account managers and energy solutions managers who may have access to customer specific information. FEI notes that it has already dealt with this potential conflict by precluding sales personnel from the definition of shared services included in FEI's proposed Code of Conduct. Other areas of the business – operational and support, IT, and regulatory – are unlikely to come into contact with customer specific information as it is not required to perform their day to day roles.

27. Second, the incentive for FEI staff is to first complete work required by FEI, and only to do FAES work to the extent that their workload allows. FEI staff are compensated based on FEI's Balanced Scorecard with the scorecard objectives focused on meeting customer, safety, regulatory and financial targets related to FEI and not FAES. FEI staff has no financial incentive that will pay an employee of FEI more for performing more work related to FAES (i.e. more FAES applications, providing superior service to FAES).⁴³

28. Third, 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.⁴⁴ As discussed later, FEI is proposing to recover the full cost in any event.

(c) Directors and Executives

29. FEI's proposal is to permit sharing of directors and officers. FEI submits that this is an appropriate organizational structure that serves the interests of FEI.

⁴² Ex. B-7, FEI Supplemental Information, Response to Question 1, p.1.

⁴³ Ex. B-7, FEI Supplemental Information, Response to Question 1, p.3.

⁴⁴ Ex. B-9, BCUC IR 1.4.2.

30. FEI and its customers benefit from having the right individuals on the senior leadership team. FEI has selected its leadership team, including those individuals who hold positions with FAES as well, to meet the current needs of the Company.

31. As set out in Part Two above, there are only three officers of FEI that are also officers of FAES. Only two of those individuals (Doug Stout and Gareth Jones) are engaged in market development (the third is a corporate governance support role only),⁴⁵ and those two individuals play very different roles for each corporation.⁴⁶ 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 someone other than Mr. Stout (Roger Dall'Antonia, Executive Vice President, Customer Service and Regulatory Affairs).⁴⁷ All FEI directors and senior management are subject to FEI's Business Ethics policy, which addresses confidentiality obligations.⁴⁸

32. The Code of Conduct in place in Alberta similarly has as its default position that:

- "A Utility may have common directors with its Affiliates."⁴⁹
- "a Utility...may share management team members or officers with other Affiliated Utilities."⁵⁰

In reviewing the Alberta Code of Conduct the Commission should note that it treats "Affiliated Utilities" differently from "Non-Utility Affiliates". ARBNNM's are the equivalent of "Affiliated Utilities", for which the Alberta Code of Conduct requirements provide greater flexibility.

⁴⁵ The same individual fills the roles of FEI's Assistant Corporate Secretary and FAES' Corporate Secretary.

⁴⁶ Ex. B-11, COC IR 1.2.1.

⁴⁷ Ex. B-9, BCUC IR 1.3.2.

⁴⁸ Ex. B-9, BCUC IR 1.2.1.

⁴⁹ FortisAlberta Inc. Code of Conduct, section 3.1.2

http://www.auc.ab.ca/rule-development/rule-0xx-inter-affiliate-code-of-conduct/Documents/Utility_Code_and_Plans/Fortis_Code.pdf.

⁵⁰ FortisAlberta Inc. Code of Conduct, section 3.1.3.

(d) Summary

33. FEI's proposed CoC wording is generally consistent with the wording contained in FEI's existing CoC for Non-Regulated Businesses, which has served to adequately protect FEI ratepayers from the misuse of utility information for many years. The general wording contemplated by FAES' competitors is too broad. FAES' competitors would preclude sharing of resources even in circumstances where customers of both utilities can realistically only benefit from sharing, and where there is little risk that confidential information could be abused by the ARBNNM. The Commission's focus should be on establishing a policy that results in appropriate protection and a fair allocation of costs (i.e., transfer pricing), rather than prohibiting sharing in circumstances where such a blunt mechanism is not required.

C. CODE OF CONDUCT SECTION 8 - FINANCING AND OTHER RISKS

34. FEI is proposing language that would permit FEI to provide financing or other financial assistance to an ARBNNM if FEI receives appropriate compensation for additional costs or risks, or Commission approval is obtained.⁵¹ FEI is not currently providing any financing to FAES; FAES obtains all debt financing from its unregulated parent company. While FEI has no plans to provide debt financing to FAES, there is no harm to FEI customers in allowing for that potential in the future. FEI would be compensated for any additional cost or risk. Debt issuance by FAES, whether with a third party or an affiliate, is reviewed and approved by the Commission under section 50 of the UCA on a case-by-case basis. FEI would require prior Commission approval pursuant to the ring-fencing conditions that were imposed when Terasen Gas Inc. was acquired by Fortis Inc.⁵² There is no need for a blanket prohibition when such safeguards exist.

⁵¹ Ex. B-1, FEI's Application (p.9) and Ex. B-4, Pre-Hearing Conference Submission (p.14) explain FEI's proposal (which had incorporated feedback from stakeholders), and the positions of various stakeholders on that proposal.

⁵² Order No. G-49-07, Reasons for Decision, p.1 of 15, Condition 7.2.1(3)(a): "No Terasen Utility will lend to, guarantee or financially support any affiliates of the Terasen Utilities, other than between TGI and TGS, or as otherwise accepted by the Commission."

http://www.fortisbc.com/About/RegulatoryAffairs/GasUtility/NatGasBCUCSubmissions/Documents/04-30_G-49-07_Reasons_for_Decision_Fortis_Acquisition.pdf.

35. The Alberta Code of Conduct contains no limitations on such transactions with “Affiliated Utilities” (akin to ARBNNMs), since it is silent on such transactions. It only addresses transactions with NRBs, and allows those transactions too provided that the terms are no more favourable than what the NRB would be able to obtain as a stand-alone entity from the capital markets.⁵³

D. TRANSFER PRICING POLICY – SECTION 1 PRICING RULES, (ii) AND SECTION 2 DETERMINING COSTS

36. FEI proposes a transfer pricing policy based on the use of “no greater than full cost” instead of “the higher of market price or fully allocated cost”. FEI submits that its proposal is appropriate and should be accepted. FEI highlights four points below:

- First, FEI’s pricing is consistent with market rates;
- Second, FEI’s proposal recognizes that both FAES and FEI are public utilities with customers and shareholders to whom the Commission owes statutory duties;
- Third, FEI’s proposal is more consistent with cost causality; and
- Fourth, FEI’s proposal reflects the Commission’s lack of jurisdiction over competition.

This section should be reviewed in conjunction with FEI’s Pre-Hearing Conference Submission.⁵⁴

(a) FEI is Already Charging Rates Consistent With Market Rates

37. FEI is providing services to FAES at rates that are consistent with market rates. This fact renders the pricing issue largely moot from a practical perspective (although it is still important from the perspective of jurisdiction and principle). The key evidence in this regard is summarized below.

⁵³ FortisAlberta Inc. Code of Conduct, section 3.2.4.

⁵⁴ Ex. B-4, Pre-Hearing Conference Submission, p.9.

38. First, FAES has the ability to acquire services from third parties. It does so where FAES believes that it can get services on more favourable terms than FEI can provide. FAES already procures 24-hour service and routine maintenance and operation services from third parties.⁵⁵ FAES has been actively investigating alternatives to provide greater separation from FEI and to replace some of the services currently provided by FEI.⁵⁶ In effect, FEI is competing in a market for provision of services to FAES.

39. Second, the hourly charge-out rates for FEI labour services is comparable to the Hay study average results. In every case, the FEI charge out rate is equal to or greater than the Hay survey average price. This reflects the fact that FEI’s approach to compensation and benefits is to provide its employees with competitive base salaries and wages, incentive compensation, benefits and paid time-off.⁵⁷

Comparison of Hourly Charge-Out Rates - FEI to Market			
2014 Hourly Charge-Out Rates			
(includes time off and benefits)			
Position		<u>FEI</u> ⁽¹⁾	<u>Market</u> ⁽²⁾
Junior accountants		\$ 54	\$ 54
Intermediate accountants		\$ 61	\$ 57
Accounting/Finance manager		\$ 83	\$ 75
Recruitment staff		\$ 61	\$ 43
Communications specialists		\$ 65	\$ 60
Regulatory staff – regulatory manager, regulatory specialists		\$ 89	\$ 73
Procurement specialists		\$ 70	\$ 67
Junior engineers		\$ 56	\$ 56
(1) FEI Charge-out rates are based on 2014 included in SAP.			
(2) Based on Hay survey from designated peer group consisting of ~110 companies.			
(3) Rates indicated do not include any assigned overhead charges.			

⁵⁵ Ex. B-7, FEI Supplemental Information, Response to Question 5, p.9.

⁵⁶ Ex. B-9, BCUC IR 1.6.3; Ex. B-10, COPE IR 1.1.3.

⁵⁷ Ex. B-7, FEI Supplemental Information, Response to Question 5, p.8.

(b) FEI's Proposal Consistent with Regulatory Principles and Jurisdiction

40. In Part Three of these Final Submissions, FEI addressed: (i) the Commission's statutory duties to FEI, FEI customers, FAES and FAES customers; and, (ii) the applicability of the regulatory compact. FEI's proposed wording of "no greater than full cost" for setting of transfer prices for services provided to ARBNNMs recognizes that there are legitimate economies of scope that can be used to the benefit FEI, FEI customers, FAES and FAES customers - i.e., the four stakeholders to whom the Commission owes a statutory duty. FEI's proposal provides for cost recovery and a contribution towards natural gas rates (equal to the margin over incremental cost). An approach contemplating "the higher of market price or fully allocated cost" is less favourable in terms of permitting FEI to further optimize its resources. It is not in the interests of FAES and its customers either.

41. FEI's 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, for instance, 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."⁵⁸

(c) Consistent With Cost Causality

42. Cross-subsidization by FEI of the ARBNNM cannot occur, by definition, when FEI is charging the ARBNNM for services on the basis of full cost. Requiring FEI to charge an ARBNNM "market price" in circumstances where "market price" is deemed to be higher than the full cost would represent a deliberate cross subsidy of FEI customers by FAES customers. In arriving at an appropriate TPP, the Commission should be equally concerned about a transfer price that, through deliberate cross-subsidization to the detriment of FAES and its customers, will act as a disincentive to the realization of legitimate economies of scope.

⁵⁸ Ex. B-9, BCUC IR 1.5.2.

(d) Consistent With Jurisdiction of Commission

43. Since cost causality is addressed, and cross subsidization eliminated, by full cost alone, requiring FEI to charge the “higher of” full cost and market price can only be explained by a policy of actively promoting competition, i.e., a concern that even the full cost of service provided by traditional utilities might give FAES an advantage if other providers of TES cannot provide services at that rate. This is, in effect, an implicit subsidy of FAES’ competitors at the expense of FAES and its customers. The Commission should be regulating to ensure that the regulated ratepayers of FEI and FAES are treated fairly.

PART FIVE: APPROPRIATE SAFEGUARDS IN PLACE

44. FEI addressed in its Supplemental Information the existing safeguards and proposed enhancements to achieve the objectives of the TPP and CoC. In this Part of the Submission, FEI highlights aspects of that evidence. FEI submits that the mechanisms are appropriate and should provide the necessary comfort to the Commission that FEI will give effect to the intention of the CoC and TPP.

A. SAFEGUARDS RELATING TO COMPLIANCE WITH CODE OF CONDUCT

45. FEI’s approach to CoC oversight, as described in the Supplemental Information, is summarized in the following table:

Safeguard	Status
Transfer from FEI to FAES individuals dedicated to supporting FAES, effective January 1, 2014. ⁵⁹	New as of January 1, 2014
Physical separation of premises, with FAES employees provided only with visitor access to FEI sites. ⁶⁰	New as of January 1, 2014
Communication with employees on a regular basis as to the importance of following the CoC/TPP. This includes <ul style="list-style-type: none">the Code of Conduct and Transfer Pricing Policy is referenced in the company’s “Business Ethics” eLearning course, a course that all employees are required to take.⁶¹quarterly reminders for employees who are likely to be directly involved with FAES activities.⁶²	Existing (first bullet) and new (second bullet)
The Director of Finance has responsibility for identifying and managing potential conflict of interest situations and monitoring compliance. ⁶³	New proposal

⁵⁹ Ex. B-7, FEI Supplemental information, Response to Question 2, p.4.

⁶⁰ Ex. B-7, FEI Supplemental Information, Response to Question 3, p.6.

⁶¹ Ex. B-7, FEI Supplemental Information, Response to Question 6, p.12.

⁶² Ex. B-7, FEI Supplemental Information, Response to Question 3, p.5.

⁶³ Ex. B-7, FEI Supplemental Information, Response to Question 3, p.5.

Safeguard	Status
<p>Annual compliance review is performed by the Internal Audit group, the results of which will be summarized in a report and filed with the Commission.</p> <p>Objectives:</p> <ul style="list-style-type: none"> • Confirm the existence of appropriate policies, processes, procedures and business information systems that ensure compliance with the CoC and TPP; • Review and determine whether the control procedures were in effect and operating effectively as of the date of the assessment; • Determine who the key business process owners are and their roles in the process; • Assess the activities of the individuals carrying out key functions or supervising the activities to ensure the Company’s control processes meet the criteria; and • Evaluate the alignment and consistency between the CoC/TPP and current business practices. 	Existing
<p>Third parties can state their complaints in writing to the Company’s Director of Finance and the Executive Vice-President, Customer Services and Regulatory Affairs, who will bring the matter to the immediate attention of the Company’s senior management and promptly initiate an investigation into the complaint. The Company will endeavour to complete this investigation within 30 days of the receipt of the complaint.⁶⁴</p>	Existing

B. SAFEGUARDS RELATING TO TRANSFER PRICING

46. There are several existing and proposed safeguards, summarized below, to ensure that all FEI charges, both direct and overhead costs, for activities in support of FAES are appropriately allocated to FAES.

Safeguard	Status
<p>Education and awareness:</p> <ul style="list-style-type: none"> • All employees are reminded of the importance of completing timesheets and the TPP.⁶⁵ • the CoC and TPP are referenced in the company’s “Business Ethics” eLearning course, a course that all employees are required to take.⁶⁶ 	Existing

⁶⁴ Ex. B-11, COC IR 1.3.1 to 1.3.4.

⁶⁵ Ex. B-7, FEI Supplemental information, Response to Question 6, p.11.

⁶⁶ Ex. B-7, FEI Supplemental Information, Response to Question 6, p.11.

Safeguard	Status
<p>Timesheets:</p> <ul style="list-style-type: none"> • FEI employees are expected to complete timesheets on a regular basis where there is costing or payroll information to be submitted. • For unionized employees, timesheets also require the review and approval of the department manager.⁶⁷ 	Existing
<p>Internal orders:</p> <ul style="list-style-type: none"> • provide a mechanism whereby costs specific to an activity (e.g., FAES work) are captured and reported separately from other costs. • Departments/employees providing support to FAES are advised of the internal order number(s) to be used and notified of the requirement to charge their time and related costs accordingly to FAES, in compliance with the CoC and TPP.⁶⁸ 	Existing
<p>Oversight by Director of Finance:</p> <ul style="list-style-type: none"> • will review charges on a quarterly basis, comparing actual charges in the quarter to that planned. • will seek confirmation every quarter from the FEI department managers who are responsible for managing the employees that may have performed work for FAES, that the actual charges recorded in the internal orders by their employees for the quarter are appropriate.⁶⁹ 	New proposal

⁶⁷ Ex. B-7, FEI Supplemental Information, Response to Question 6, p.11.

⁶⁸ Ex. B-7, FEI Supplemental Information, Response to Question 6, p.12.

⁶⁹ Ex. B-7, FEI Supplemental Information, Response to Question 6, p.13.

PART SIX: CONCLUSION

47. FEI's proposed TPP and CoC promote just and reasonable rates for FEI and its customers by ensuring that FEI can capitalize on legitimate economies of scope and receive fair value for its services, while using information appropriately. At the same time, FEI's proposal is also fair and beneficial to FAES and its customers. FEI respectfully submits that the Commission should approve the Company's CoC and TPP as proposed.

ALL OF WHICH IS RESPECTFULLY SUBMITTED.

Dated:

November 12, 2014

[original signed by Matthew Ghikas]

Matthew Ghikas
Counsel for FortisBC Energy Inc.