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March 8, 2016

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

Attention: Ms. Laurel Ross, Acting Commission Secretary and Director

Dear Ms. Ross:

Re: Project No. 3698864
FortisBC Energy Inc. (FEI)
2015 Price Risk Management Application (the Application)
Response to the British Columbia Utilities Commission (BCUC or the Commission) Information Request (IR) No. 1 – Scope A

On December 23, 2015, FEI filed the Application referenced above. In accordance with Exhibit A-8 setting out the Amended Regulatory Timetable for the review of the Application, FEI respectfully submits the attached response to BCUC Scope A IR No. 1.

If further information is required, please contact Mike Hopkins, Senior Manager, Price Risk & Resource Planning at (604) 592-7842.

Sincerely,

FORTISBC ENERGY INC.

Original signed:

Diane Roy

Attachments

cc (email only): Registered Parties



1 **1.0 Reference: REQUEST FOR COMMISSION APPROVAL**

2 **FortisBC Energy Inc. 2015 Price Risk Management Application**

3 **(Application),**

4 **Exhibit B 1, p. 3;**

5 **Exhibit A2-2, FEI 2014 Price Risk Management Review Report, pp.**

6 **31–49**

7 **Portfolio of price risk management alternatives**

8 On page 3 of the Application, FortisBC Energy Inc. (FEI) has requested approval of a

9 medium-term fixed-price hedging strategy and enhancements to FEI’s quarterly

10 commodity rate setting mechanism.

11 In Section 5 of the 2014 Price Risk Management Review Report (Exhibit A2-2), FEI

12 describes a number of physical and financial price risk management alternatives, some

13 of which are already used by FEI and some of which are potential alternatives.

14 1.1 The following table lists a number of price risk management alternatives. In order

15 to provide a comparative analysis of the price risk alternatives that are or may be

16 available to FEI and its customers, please populate the table. Please add any

17 price risk management alternatives that FEI considers are missing.

18

Price risk management tool	Description	Degree to which volatility is mitigated	Limitations of tool
Alternatives currently used or available to FEI and its customers			
Physical Tools			
Contracting with multiple counterparties			
Receipt Point allocation			
Allocation between monthly and daily index priced gas purchases			
Fixed AECO-Station 2 Basis Differential Contracts			
Quarterly rate setting (versus annual)			
12 month amortization of CCRA deferral account balance			



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0.95/1.05 cost-recovery ratio deadband			
\$0.50/GJ minimum rate change threshold			
Consideration of full circumstances to vary from standard guidelines for commodity rate setting (e.g. 24 month amortization)			
Equal Payment Plan			
Customer Choice Program			
Customer moving from sales to transportation service			
Financial Tools			
Sumas AECO/NIT Swaps			
Approvals requested in the Application			
Physical Tools			
Capping quarterly rate changes at \$1.00/GJ			
Established criteria for moving to 24 month amortization			
Fixed price purchases			
Financial Tools			
Fixed prices swaps			
Potential tools			
Physical Tools			
Alternate rate offerings			
Volumetric Production Payments			
Investment in Reserves			
Financial Tools			
Call options			
Costless collars			



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- 1
- 2 **Response:**
- 3 FEI has added the use of natural gas storage and long term index priced purchases to the
- 4 alternatives currently used or available to FEI and its customers and long term fixed price
- 5 purchases to the potential physical tools. FEI notes that it is difficult to quantify the volatility
- 6 mitigation impacts of these tools and so has provided the impacts at a high level.



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Price Risk Management Tool	Description	Degree to which Volatility is Mitigated	Limitations of Tool
Alternatives currently used or available to FEI and its customers			
<i>Physical Gas Contracting Tools</i>			
Contracting with multiple counterparties	FEI purchases supply from multiple producers or marketers.	No impact on mitigating market price or rate volatility if purchasing at market index prices.	Helps manage counterparty credit or supply risk only.
Receipt Point allocation	FEI purchases commodity supply at Station 2 and AECO/NIT (and in the past Huntingdon/Sumas) rather than a single hub.	Mitigates any market price disconnections that may occur at particular price hubs due to regional pipeline constraints or other market conditions.	Does not mitigate overall market price volatility as all market prices generally move together.
Allocation between monthly and daily index priced gas purchases	FEI currently purchases commodity supply at a mix of 60% monthly and 40% daily index prices.	Daily market price volatility is reduced by having monthly priced supply in the portfolio.	Does not mitigate monthly market price volatility.
Long term index price purchases	FEI purchases supply from producers or marketers at market index prices for terms up to ten years to provide security of supply.	Mitigates AECO/NIT-Station 2 basis volatility on an annual basis since the basis is determined and locked in each year.	Does not mitigate AECO/NIT market price volatility.
Use of storage	Under the Essential Services Model, FEI buys baseload gas every day of the year thus FEI injects gas in the summer, when market prices are typically lower, and withdraws it during winter, when market prices are typically higher.	Mitigates some market price volatility for a single winter period only, as most of the injected gas is used during the winter.	Mitigates price volatility for a single winter period. Sometimes, the summer injection price can be more than the winter market price.
Fixed AECO-Station 2 Basis Differential Contracts	FEI locks in the forward market price differential between AECO/NIT and Station 2 to capture the Station 2 discount.	Mitigates the volatility or changes in the price differential between AECO/NIT and Station 2.	Does not mitigate the AECO/NIT market price volatility.



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Price Risk Management Tool	Description	Degree to which Volatility is Mitigated	Limitations of Tool
Rate Setting Mechanisms			
<p>Quarterly rate setting (versus annual)</p>	<p>Pursuant to Commission Guidelines, each quarter FEI submits, for Commission review, a report on the actual incurred and forward market prices, and the actual and projected deferral account balances to determine if a commodity rate change is warranted.</p>	<p>Generally speaking, quarterly rate setting will result in more frequent yet smaller rate changes than annual rate setting.</p> <p>Quarterly rate setting allows FEI to manage the size of the deferral account while providing customers with a balance of rate stability and price transparency through a relatively simple and efficient process.</p> <p>Annual rate setting would reduce the frequency of rate changes but tend to increase the magnitude of the rate change required, would tend to provide less price transparency, and may be an obstacle to managing the deferral account balance within a reasonable range.</p>	<p>The quarterly rate setting mechanism addresses rate stability, price transparency, managing deferral account balances, and efficiency of process. However, the mechanism has to balance possibly conflicting objectives such as dealing with both the frequency and the size of rate changes which comprise rate stability. As well, amortization of deferral balances can affect price transparency by masking the price signal provided by the commodity rate. Does not affect underlying market prices and their impact on gas costs.</p>
<p>12 month amortization of CCRA deferral account balance</p>	<p>Consistent with the Commission Guidelines, FEI typically recovers from, or refunds to, customers any projected accumulated deferral account balance at the end of the current period over the next 12 months when setting commodity rates.</p>	<p>Generally, 12 months provides a reasonable amortization period for the variances (between the approved recovery rate, based on the forecast cost of gas, and the actual cost of gas incurred) captured in the deferral account.</p> <p>Shorter amortization periods would tend to increase the magnitude of the change in rates. Longer amortization periods would tend to have the opposite effect on rates but may impair the ability to manage deferral account balances within a reasonable range.</p>	<p>Amortization of the deferral balance can mask the price signal provided by the commodity rate.</p> <p>Size of deferral account, in conjunction with the amortization period, can impact customer behaviours.</p> <p>Does not affect underlying market prices and their impact on gas costs.</p>



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Price Risk Management Tool	Description	Degree to which Volatility is Mitigated	Limitations of Tool
0.95/1.05 cost-recovery ratio deadband	Consistent with Commission Guidelines, a commodity rate change is indicated if the ratio of the forecast 12 month gas cost recoveries at the existing rate compared to the sum of the forecast gas costs for the 12-month prospective period plus the projected CCRA deferral balance at the end of the current quarter is outside the +/- 5 percent deadband. A minimum rate change threshold of \$0.50/GJ was approved pursuant to L-40-11.	Supports rate stability, price transparency, managing deferral account balances, and efficiency of process. Provides a signal of when forward market prices, in conjunction with the deferral account balance, may drive the need to change the commodity rate.	<p>Provides a simple, easy to understand trigger mechanism however, taken on its own, it can indicate the need for minor, possibly unnecessary, changes in rates when in a low market price environment. Also, the trigger mechanism by itself excludes consideration of the full circumstances.</p> <p>Does not affect underlying market prices and their impact on gas costs.</p>
\$0.50/GJ minimum rate change threshold	Commission Guidelines were revised pursuant to L-40-11 to include a minimum rate change threshold of \$0.50/GJ.	The addition of the minimum rate change parameter prevents the 95%-105% deadband from becoming too narrow during periods when the price of natural gas remains low, thereby avoiding minor and possibly frequent commodity rate changes in low price environments.	<p>The minimum rate change threshold has a dampening effect on the volatility of rate changes which may mask the price signal provided by the commodity rate.</p> <p>Does not affect underlying market prices and their impact on gas costs.</p>
Consideration of full circumstances to vary from standard guidelines for commodity rate setting (e.g. 24 month amortization)	Consistent with Commission Guidelines, the full circumstances prevailing at the time when a quarterly report and cost recovery rates are under review will be considered. As well as the Commission Guideline trigger mechanism and rate methodology, consideration will be given to factors such as the current deferral balances and, based on the forecast costs, the appropriateness of any rate proposals over a 24-month timeframe.	Supports reduction of rate volatility, while still managing deferral account balances within a reasonable range, when there is a significant difference in the forward gas costs for the next twelve months compared to the subsequent twelve months. In some situations, setting the commodity rate over a 12-month timeframe can result in more rate volatility than if the commodity rate was set using a 24-month outlook.	<p>Opportunities for use of this tool are dependant upon the forward market prices at the time of the quarterly review.</p> <p>Does not affect underlying market prices and their impact on gas costs.</p>



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Price Risk Management Tool	Description	Degree to which Volatility is Mitigated	Limitations of Tool
<i>Optional Customer Bill and Rate Tools</i>			
Equal Payment Plan (EPP)	Customers can elect to sign up for a program that smooths out their monthly bill payments. Customers' consumption and commodity rates are forecast in order to average out the next twelve months' bills.	Some monthly bill payment smoothing will occur for customers during periods of relatively stable rates and when customers' actual consumption of gas is close to their expected consumption.	During periods of volatile rates and/or higher or lower expected consumption, periodic adjustments may be required within the twelve month period. This is to prevent large adjustments for EPP customers at the end of the twelve month term.
Customer Choice Program	Customers can elect to receive their commodity supply from a natural gas marketer rather than FEI and pay a fixed rate for terms up to five years.	Provides commodity rate stability for customers up to five years. Customers can benefit if market prices increase above their fixed rate.	Fixed rate dampens market price signals. Marketers' rates may include a profit margin. Customers do not benefit if market prices fall below their fixed rate.
Customer moving from sales to transportation service	Some customers can elect to receive their commodity supply from a natural gas marketer and use FEI transportation service to get their supply.	Customers can determine the degree of commodity rate volatility reduction they want through their arrangement with the marketer.	This option is only available to certain rate classes and is generally not available to low-volume residential and commercial customers.
<i>Financial Tools</i>			
Sumas AECO/NIT Swaps	FEI locks in the forward market price differential between AECO/NIT and Sumas to protect against Sumas price disconnections.	Mitigates the volatility or changes in the price differential between AECO/NIT and Sumas.	Does not mitigate the AECO/NIT market price volatility.
Approvals requested in the Application			
<i>Rate Setting Mechanisms</i>			
Capping quarterly rate changes at \$1.00/GJ	Implementing a rate cap for quarterly rate setting, plus or minus \$1.00/GJ that could be used for no more than 2 consecutive quarters when the rate changes subject to the cap have been in the same direction.	Reduces rate volatility during periods of short-term market volatility.	Only temporarily dampens the impact of a sustained market price decrease or increase, which is ultimately flowed through to the customer via rates.



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Price Risk Management Tool	Description	Degree to which Volatility is Mitigated	Limitations of Tool
Established criteria for moving to 24 month amortization	Criteria provided for clarification of when consideration may be given for commodity rate proposals beyond the 12-month outlook in order to reduce rate volatility and manage deferral balances. Provides criteria for consideration of 24-month view during periods when 12-month gas costs are significantly different than following 12-month gas costs while maintaining the CCRA deferral account within a reasonable range over the full duration of the 24-month period.	Supports reduction of rate volatility, while still managing deferral account balances within a reasonable range, when there is a significant difference in the forward gas costs for the next twelve months compared to the subsequent twelve months. In some situations, setting the commodity rate over a 12-month timeframe can result in more rate volatility than if the commodity rate was set using a 24-month outlook.	<p>Opportunities for use of this tool are dependant upon the forward market prices at the time of the quarterly review.</p> <p>Does not affect underlying market prices and their impact on gas costs.</p>
Physical Contracting Tools			
Fixed price purchases	FEI purchases supply from producers or marketers at fixed prices for terms up to three years to mitigate market price volatility and provide security of supply.	Mitigates market price volatility for a portion of the supply portfolio for up to three years. Customers can benefit if market prices increase above the fixed price.	Limited counterparties may reduce the availability of this option. Partially dampens market price signals provided by the commodity rate. Customers do not benefit from market prices falling below the fixed hedge price.
Financial Tools			
Fixed price swaps	FEI enters into a financial swap transaction with a counterparty (such as a bank) and pays a fixed price while receiving an index price.	Mitigates market price volatility for a portion of the supply portfolio for up to three years. Customers can benefit if market prices increase above the fixed price.	Counterparty credit exposure must be monitored during periods of volatile market prices. Partially dampens market price signals provided by the commodity rate. Customers do not benefit from market prices falling below the fixed hedge price.
Potential Tools			
Optional Customer Rate Tools			
Alternate commodity rate offerings	FEI could provide the option to customers to purchase commodity supply from FEI at a fixed rate.	Provides commodity rate stability for customers. Customers can benefit if market prices increase above their fixed rate.	Additional commodity offerings may be confusing to customers. Fixed rate dampens market price signals. Customers do not benefit if market prices fall below their fixed rate.



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Price Risk Management Tool	Description	Degree to which Volatility is Mitigated	Limitations of Tool
<i>Physical Contracting Tools</i>			
Volumetric Production Payments (VPP)	The buyer pays an upfront lump sum payment to a gas producer in exchange for specific volumes delivered over the term of the agreement (up to twenty years). The buyer also receives a limited royalty interest in the production volumes which is returned to the seller once the volumes have been delivered.	Provides gas cost certainty for a portion of the commodity supply portfolio for a period up to twenty years. Provides long term security of supply. Customers can benefit if market prices increase above the VPP contract price.	Limited counterparties may reduce the availability of this option. Partially dampens market price signals provided by the commodity rate.
Investment in Reserves	The buyer enters into a joint venture with a gas producer for a term up to thirty years. The buyer would share in the cost of developing and producing the gas and earn the right to a portion of the production.	Provides gas cost certainty for a portion of the commodity supply portfolio for a period up to thirty years. Provides long term security of supply. Customers can benefit if market prices increase above the reserves costs.	Limited counterparties may reduce the availability of this option. Significant due diligence is required by the buyer to mitigate production variability and drilling and operating cost risks. Partially dampens market price signals provided by the commodity rate.
Long term fixed price purchases	FEI purchases supply from producers or marketers at a fixed price for terms up to ten years.	Mitigates market price volatility for a portion of the commodity supply portfolio. Provides long term security of supply.	Can result in higher than market costs if market prices move lower after locking in. Partially dampens market price signals provided by the commodity rate.
<i>Financial Tools</i>			
Call options	FEI enters into a financial transaction with a counterparty (such as a bank) where FEI will not pay more than a fixed cap price in exchange for FEI paying a call premium.	Limits market price volatility above the option cap price.	Buyer must pay a call option premium. Does not limit market price volatility below the option cap price. Partially dampens market price signals (above the cap price) provided by the commodity rate.
Costless collars	FEI enters into a financial transaction with a counterparty (such as a bank) where FEI will not pay more than a fixed cap price in exchange for FEI paying at least a fixed floor price.	Limits market price volatility above the option cap price and below the option floor price.	Buyer does not benefit if market prices fall below the floor price. Does not limit market price volatility in between the option cap and floor prices. Partially dampens market price signals (above the cap price and below the floor price) provided by the commodity rate.

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2
3 1.2 For those tools currently available to FEI and proposed by FEI in the Application,
4 please provide a discussion of the relative order in which these tools should be
5 layered in or applied.

6
7 **Response:**

8 FEI's gas supply and price risk management portfolios include numerous tools currently
9 available to FEI to meet the objectives stated on page 1 of the Application, providing cost-
10 effective and reliable supply to customers while mitigating market price volatility.

11 There are factors FEI must take into consideration to meet these objectives, including managing
12 supply risk, managing market price risk, managing deferral account balances, sending price
13 signals to customers and monitoring counterparties and credit exposure under different market
14 price conditions. FEI takes a comprehensive approach when considering various tools as no
15 single tool effectively addresses these factors and meets the objectives on its own.

16 At a high level, FEI needs to first make sure that physical tools are in place given that FEI has a
17 priority to deliver natural gas to its customers. These include tools such as contracting for
18 supply at multiple supply hubs with a variety of sound counterparties and using natural gas
19 storage to meet high customer demand periods. Once these physical tools are established, the
20 appropriate rate setting mechanisms, such as the quarterly rate setting and amortization of the
21 deferral account, need to be in place to ensure timely recovery or refund of gas costs through
22 rates from or to customers. Next, tools to mitigate market price volatility, such as rate change
23 thresholds and fixed price hedging, and optional offerings for customers (including the EPP) can
24 be applied.

25 Unlike the existing tools FEI uses, hedging can help with the objective of capturing market price
26 opportunities for customers' benefit. FEI thus believes that the requests within the Application
27 can add to its portfolio approach in meeting the price risk management objectives.

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31 1.2.1 Please also indicate which tools tend to increase the Commodity Cost
32 Reconciliation Account (CCRA) balance and which tools tend to
33 decrease the CCRA balance.

34
35 **Response:**

36 Please refer to the table below which indicates which tools tend to increase the Commodity Cost
37 Reconciliation Account (CCRA) balance and which tools tend to decrease the CCRA balance.
38 FEI has interpreted 'increase' or 'decrease' to mean increasing or decreasing the absolute dollar
39 amount range of the CCRA balance.



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Price Risk Management Tool	Tend to Increase CCRA Balance	Tend to Decrease CCRA Balance	N/A	Notes
Alternatives currently used or available to FEI and its customers				
<i>Physical Contracting Tools</i>				
Contracting with multiple counterparties			X	Multiple counterparty contracting at index prices does not impact gas costs or CCRA deferral balances.
Receipt Point allocation		X		Using an average price from multiple Receipt Points may reduce price fluctuation and may contribute to some reduction in CCRA deferral balances.
Allocation between monthly and daily index priced gas purchases		X		Reduced volatility may contribute to some reduction in CCRA deferral balances.
Fixed AECO-Station 2 Basis Differential Contracts		X		Reduced volatility may contribute to some reduction in CCRA deferral balances.
<i>Rate Setting Mechanisms</i>				
Quarterly rate setting (versus annual)		X		Quarterly rate setting results in more frequent adjustment of rates and helps better manage CCRA deferral balances.
12 month amortization of CCRA deferral account balance		X		Amortization periods longer than 12-months would tend to increase balances but at the same time tend to reduce the amortization impact on rates. The 12-month amortization is consistent with Commission Guidelines.
0.95/1.05 cost-recovery ratio deadband	X	X		A narrower deadband, in the current lower gas price environment and disregarding the minimum rate change threshold, would tend to decrease balances. Conversely, a wider deadband, in a higher price gas environment would tend to increase balances. The 95%-105% deadband supports maintaining the CCRA balances within a reasonable range.
\$0.50/GJ minimum rate change threshold	X			The \$0.50/GJ threshold was added to avoid minor rate changes while market prices remained low. This has the effect of increasing the deferral balances but still within a reasonable range (hence why the \$0.50/GJ was selected).

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Price Risk Management Tool	Tend to Increase CCRA Balance	Tend to Decrease CCRA Balance	N/A	Notes
Consideration of full circumstances to vary from standard guidelines for commodity rate setting (e.g. 24 month amortization)	X	X		This may not correlate directly to either an increase or decrease in the deferral balances but provides more rate stability with the ever present requirement that any proposal would also provide that deferral balances are maintained within a reasonable range.
<i>Optional Customer Bill and Rate Tools</i>				
Equal Payment Plan			X	No impact on gas costs and therefore no impact on CCRA.
Customer Choice Program		X		CCRA could be lower if there was significant uptake in Customer Choice such that FEI's gas costs were significantly lower. The <u>relative</u> impact to the customers would be unchanged as there would be fewer remaining customers / volumes to allocate costs across.
Customer moving from sales to transportation service		X		CCRA could be lower if there was significant uptake in transportation service such that FEI's gas costs were significantly lower. There would be lower absolute value but basically the same unitized costs.
<i>Financial Tools</i>				
Sumas AECO/NIT Swaps		X		Reduced volatility may contribute to some reduction in CCRA deferral balances.
Approvals requested in the Application				
<i>Rate Setting Mechanisms</i>				
Capping quarterly rate changes at \$1.00/GJ	X			Would generally tend to attract larger deferral balance but FEI would only propose this provided the deferral balances are maintained within a reasonable range.
Established criteria for moving to 24 month amortization			X	The criteria for clarification provides an example of where the first 12-month market prices are moving in one direction and the second 12-month market prices are moving opposite. The 24-month view may not correlate directly to either an increase or decrease in the deferral balances but was driven more by rate stability with the ever present requirement that any proposal would also provide that deferral balances are maintained within a reasonable range.
<i>Physical Contracting Tools</i>				
Fixed price purchases		X		There would be less forward supply purchases estimated at forward prices.

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Price Risk Management Tool	Tend to Increase CCRA Balance	Tend to Decrease CCRA Balance	N/A	Notes
<i>Financial Tools</i>				
Fixed prices swaps		X		There would be less forward gas costs estimated at forward prices.
Potential tools				
<i>Optional Customer Rate Tools</i>				
Alternate rate offerings		X		Assuming this means fixed price offerings and supply was bought or hedged to match. Less purchases would be subject to forward price forecast.
Physical Contracting Tools				
Volumetric Production Payments		X		Less forward supply purchases estimated at forward prices.
Investment in Reserves		X		Less forward supply purchases estimated at forward prices.
Financial Tools				
Call options		X		During periods when market prices are above the strike price, less forward gas costs estimated at forward prices. During periods when market prices are below the strike price, these instruments have no impact on the CCRA deferral balance.
Costless collars		X		During periods when market prices are above the upper strike price or below the lower strike price, less forward gas costs estimated at forward prices. During periods when market prices are in between the strike prices, this instrument has no impact on the CCRA deferral balance.

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1 **2.0 Reference: REQUEST FOR COMMISSION APPROVAL**
2 **Commission Order G-120-11, Appendix A, p. 23;**
3 **Exhibit A2-2, FEI 2014 Price Risk Management Review Report, pp.**
4 **34–35**
5 **Sumas-AECO/NIT basis swaps**

6 In the British Columbia Utilities Commission’s (Commission) reasons for decision
7 attached as Appendix A to Order G-120-11 (2011 Decision) in regard to the FortisBC
8 Energy Inc./FortisBC Energy (Vancouver Island) Inc. (FEU) 2011-2014 Price Risk
9 Management Plan (2011-2014 PRMP), the Commission denied the 2011-2014 PRMP
10 with the exception of the request to enter into Sumas/AECO swaps.

11 In the FEI 2014 Price Risk Management Review Report (2014 PRM Review Report), FEI
12 describes on pages 34 and 35 how FEI made changes to the commodity portfolio
13 Receipt Point allocations effective November 1, 2013 to reduce exposure to Sumas
14 prices. The impact of this re-allocation was to reduce the commodity portfolio supply
15 allocation to zero at the Huntington Receipt Point. On page 35, FEI states that in the
16 past, FEI had used Sumas-AECO/NIT basis swaps to mitigate Sumas price risk. In the
17 footnote on page 35, FEI states that the “Total basis swaps cost for 2001 to 2013 was
18 \$4.7 million.”

19 2.1 Did FEI execute any Sumas-AECO/NIT basis swaps that were in place for the
20 period beyond November 1, 2013?
21

22 **Response:**

23 No, FEI did not execute any Sumas-AECO/NIT basis swaps that were in place for the period
24 beyond November 1, 2013 given that FEI removed its Sumas price exposure in the gas supply
25 portfolio effective November 1, 2013. FEI’s last Sumas-AECO/NIT basis swaps were
26 transacted in September 2012 for the November 2012 to March 2013 winter period.

27
28

29 2.1.1 If so, please provide the total cost of these basis swaps and please
30 comment on the need for these swaps given the Huntington Receipt
31 Point allocation was zero.
32

33 **Response:**

34 Please refer to the response to BCUC Scope A IR 1.2.1.
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1
2 2.2 Does FEI agree that the portfolio of price risk management alternatives available
3 to FEI at any given time needs to be considered from a holistic or comprehensive
4 perspective to ensure the strategies do not conflict or overlap unnecessarily?
5 Please discuss.

6

7 **Response:**

8 Yes. Please also refer to the response to BCUC Scope A IR 1.1.2.

9

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1 **3.0 Reference: REQUEST FOR COMMISSION APPROVAL**

2 **Exhibit B-1, p. ES-1;**

3 **Exhibit B-1, Appendix A, Price Risk Management Workshop**
4 **Summary Report, p. 19**

5 **Enhancements to the rate setting mechanism**

6 FEI states on page ES-1 of its Application that:

7 The workshop process also revealed that stakeholders and FEI agree that the
8 current FEI quarterly rate setting and deferral account mechanism is working as
9 intended. However, there was also some agreement that **enhancements could**
10 **be made to the rate setting mechanism** that would meet the price risk
11 management objectives and benefit customers, particularly during periods of
12 **significant market price volatility**. Maintaining commodity deferral account
13 balances **within a reasonable range** is also an important consideration when
14 setting commodity rates. The proposed enhancements **include** implementing a
15 commodity rate change cap and establishing criteria to assist in determining
16 when consideration should be given to rate proposals beyond the standard 12-
17 month timeframe. [Emphasis added]

18 In the Price Risk Management Workshop Summary Report in Appendix A of the
19 Application, FEI stated:

20 FEI noted that if gas market price conditions were to change significantly from
21 where they are today and revert back to a pre-shale gas price range of \$6-\$7/GJ,
22 then the rate setting criteria proposed here **may have to** be revisited and
23 adjusted. It is difficult to come up with rate setting rules and criteria that are
24 applicable in all circumstances. [Emphasis added]

25 3.1 Please expand on reasons why the rate setting criteria proposed may have to be
26 revisited and adjusted if the price of natural gas returned to the \$6-\$7/GJ price
27 range.

28
29 **Response:**

30 The reference above should have read “Participant comments from the workshops were that if
31 gas market price conditions were to change significantly from where they are today and revert
32 back to a pre-shale gas price range of \$6-\$7/GJ, then the rate setting criteria proposed here
33 **may have to** be revisited and adjusted. It is difficult to come up with rate setting rules and
34 criteria that are applicable in all circumstance.” It was not FEI that made the above comment.

35 However, FEI believes that the current rate setting criteria have worked in different market
36 conditions including those in the past where market prices were considerably higher (e.g. in the
37 \$6-\$7 price range). However, if there are market conditions that affect FEI’s ability to balance
38 managing deferral accounts with mitigating rate volatility and providing price signals to

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1 customers, then FEI could review and revisit the rate setting criteria including any approved
2 enhancements. At this point in time, FEI has no plans to do so.

3
4

5

6 3.2 Please explain what would constitute a reasonable range for Commodity Cost
7 Reconciliation Account (CCRA) deferral account balances if the price of natural
8 gas moves to the \$6-\$7/GJ price range.

9

10 **Response:**

11 The range for the CCRA deferral account balance does not change with different market prices.
12 Thus a reasonable range for the CCRA deferral account balance if the price of natural gas is
13 within the \$6-\$7/GJ price range remains at the current \$50-\$60 million.

14 FEI believes the rate setting mechanism has worked well, and continues to work well, in higher
15 gas price environments. The basic mechanism was put in place in 2001 and worked well
16 through a high price market. Only as a result of the low price environment did FEI propose the
17 \$0.50/GJ minimum threshold in 2011 to reduce the frequency of rate changes for minor
18 amounts which otherwise would have occurred based solely on the 95%-105% deadband.

19

20

21

22 3.3 Please explain the limitations and costs of growing deferral accounts during
23 volatile periods to smooth out commodity rates.

24

25 **Response:**

26 The limitations and costs of growing deferral accounts during volatile periods as a means to
27 smooth out commodity rates depend on factors such as the nature of the market circumstances,
28 duration of the market event, and the level of the CCRA account before the event. In general,
29 the limitation is that the CCRA deferral account should not exceed a reasonable range.

30 Prior to 1999, gas cost recovery rates for FEI's predecessor company, BC Gas Utility Ltd. (BC
31 Gas), were set once per year effective January 1. During 1999 and 2000, natural gas prices
32 increased dramatically and mid-year rate changes were required. The approved gas cost
33 recovery rates, however, continued to under-recover the gas costs incurred and the balance in
34 the gas cost deferral account grew to a deficit of approximately \$180 million by the end of 2000.
35 Commission staff prepared a report on the method of establishing gas cost recovery rates for
36 BC Gas and amortizing the deferral balance, which was circulated to BC Gas and other parties
37 on November 7, 2000. The Commission, based on its review of the staff report and
38 submissions made by BC Gas and other parties, established the Guidelines for Setting Gas

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1 Cost Recovery Rates and Managing the Gas Cost Reconciliation Balance by Letter L-5-01. The
2 quarterly rate review and rate setting guidelines as set forth by the Commission in 2001, and
3 followed by FEI, provide a mechanism to manage the recovery of gas costs through rates and
4 the gas cost deferral account balances.

5 Increasing the CCRA deferral balance by lengthening the rate setting intervals may mask price
6 signals, or lead to the Company holding more customer money for a longer period of time.

7
8
9

10 3.4 Please explain what impact the proposal to limit rate changes to the range
11 between the existing minimum rate change of \$0.50/GJ and the proposed
12 maximum rate change of \$1.00/GJ will have on FEI's ability to maintain the
13 CCRA deferral account balances within a reasonable range.

14

15 **Response:**

16 The proposed maximum commodity rate change cap of \$1.00/GJ, applicable to rate increases
17 or decreases, would be implemented only if the deferral account balance is maintained within a
18 reasonable range. In other words, the proposed maximum rate change of \$1.00/GJ should have
19 no impact on FEI's ability to maintain the CCRA deferral account balances within a reasonable
20 range.

21

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1 **4.0 Reference: DEFERRAL ACCOUNTS**

2 **Commission letter L-5-01, Appendices II and III;**

3 **Exhibit B-1, Appendix A, 2014 Price Risk Management Workshop**
4 **Review Report, p. 27;**

5 **Exhibit A2-1, March 2011 Report on the Commodity Cost**
6 **Reconciliation Account (CCRA) and Midstream Cost Reconciliation**
7 **Account (MCRA) Deferral Accounts and Rate Setting Mechanisms,**
8 **Appendix D**

9 **Historical GCRA and CCRA deferral account size**

10 Appendix II of Commission letter L-5-01 states:

11 Size of Deferral Account

12 In general, a mechanism that results in relatively small deferral account balances
13 would be preferred to a mechanism that results in relatively large deferral
14 account balances because large deferral accounts can mask underlying
15 commodity price changes and alter the competitive position of the utility relative
16 to smaller gas marketers. Large deferral accounts can also create issues related
17 to **the applicability of GCRA rate riders to new customers or customers**
18 **switching to transportation service** that might be avoidable or less important
19 with smaller deferral account balances. [Emphasis added]

20 4.1 Please explain if the two conditions of large deferral accounts referenced above,
21 the applicability of GCRA (now CCRA) rate riders to new customers and/or
22 customers switching to transportation service, are issues today at FEI, and if they
23 are, exactly how they are dependent on the size of the CCRA deferral account
24 and what cost impact this has on FEI and on ratepayers.

25
26 **Response:**

27 FEI has no evidence, and does not believe, that there is presently an issue with new customers
28 making decisions about gas service, and/or customers switching between the FEI standard
29 commodity sales rate offering and gas marketers, via either the Customer Choice Program or
30 the transportation service rate offerings, as a result of the CCRA deferral account balances. FEI
31 believes that as long as the CCRA deferral account balances are maintained within a
32 reasonable range, the economic value of any particular CCRA surplus or deficit will amount to a
33 very minor component of a customer's overall decision.

34

35

36

37

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1 Appendix III of Commission letter L-5-01 states:

2 BC Gas provided initial comments in a letter dated **December 13, 2000**. BC Gas
3 indicated that it supports the implementation of a formula-based monthly review
4 process. Rates would be changed at the end of a month if the projected cost of
5 gas for the next 12 months less expected rate revenue for the same period plus
6 the GCRA balance (excluding the initial GCRA balance) **exceeds (or is lower**
7 **than) by \$50 million (approximately \$65 per customer, or 4.4 percent)**. ... BC
8 Gas also provided information related to the current status of the GCRA including
9 the possibility that the previous estimate of the GCRA balance as at December
10 31, 2000 (\$159 million) may be too low by as much as \$20 million. [Emphasis
11 added]

12 4.2 Please provide the dollar amount per customer represented by a \$50 million
13 deferral account today, and what percentage of the average annual residential
14 customer billing that would represent.

15
16 **Response:**

17 FEI interprets this question to ask about the proportion of a residential customer's annual bill in
18 dollars and percentage that would result from the amortization of a \$50 million deferral account
19 balance. FEI uses its current rates to illustrate the response.

20 On November 25, 2015, FEI filed its 2015 Fourth Quarter Gas Cost Report on the Commodity
21 Cost Reconciliation Account (CCRA) and Midstream Cost Reconciliation Account (MCRA)
22 Deferral Accounts. The projected December 31, 2015 CCRA balance as indicated in this report
23 was approximately \$49 million pre-tax surplus (comparable to the \$50 million pre-tax deferral
24 account change referenced in the preamble to the question). The deferral surplus of \$49 million
25 represented approximately \$38 or 5% of the annual bill for a typical Mainland Rate Schedule 1
26 residential customer with an average annual consumption of 90 GJ.

27
28

29
30

31 In Exhibit A2-1, the March 2011 Report on the Commodity Cost Reconciliation Account
32 (CCRA) and Midstream Cost Reconciliation Account (MCRA) Deferral Accounts and
33 Rate Setting Mechanisms, in Appendix D: Historical Actual Monthly Deferral Account
34 Balances shows a graph of the deferral account after-tax balances from January 1998 to
35 January 2011 including the large Gas Cost Reconciliation Account (GCRA) balance
36 around January 2001.

37 On page 27 of the 2014 PRM Review Report (Appendix A of the Application), FEI stated:

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1 The CCRA became effective April 1, 2004 and since that time deferral account
2 balances, on a net of tax basis, have **generally been within a reasonable ± \$50**
3 **million range**. The quarterly review and opportunity to adjust deferral account
4 balances provides **timely management of these balances to an appropriate**
5 **amount**. This is in the best interests of customers, **in terms of rate volatility**
6 **mitigation**, price transparency and reduced intergenerational inequities and
7 allows for prudent financial management by FEI. [Emphasis added]

8 4.3 Did FEI receive a credit rating downgrade or ratings watch notice as a result of
9 the large GCRA balance in January 2001? Please elaborate.

10

11 **Response:**

12 FEI does not appear to have been downgraded at any point in 2001. During this year, FEI was
13 rated by DBRS, S&P, and Moody's. 2001 was the first year that Moody's rated FEI and their
14 initial rating was A2 for FEI's unsecured debentures. In Moody's rating announcement they do
15 not specifically refer to the GCRA balance. In 2000, S&P acquired CBRS, and as a result took
16 over the rating of FEI, which was previously rated by CBRS. As part of this process, S&P
17 harmonized all ratings of companies that were rated by CBRS, to ensure the ratings reflect its
18 own methodology. As a result, S&P's rating for FEI changed to BBB+, however this rating
19 change did not constitute a downgrade for worsening creditworthiness. The S&P report also
20 does not specifically reference the GCRA balance for this year. Lastly, DBRS's rating remained
21 at A during this year. The DBRS report for this year highlights the fact that it was expected for
22 outstanding balances in the GCRA deferral account to be recovered before 2002.

23

24

25

26 4.4 Please provide a chart showing the GCRA/CCRA+MCRA deferral account
27 balances on a quarterly basis from January 1, 2000 to January 2016. Please
28 provide the chart and data in working Excel format.

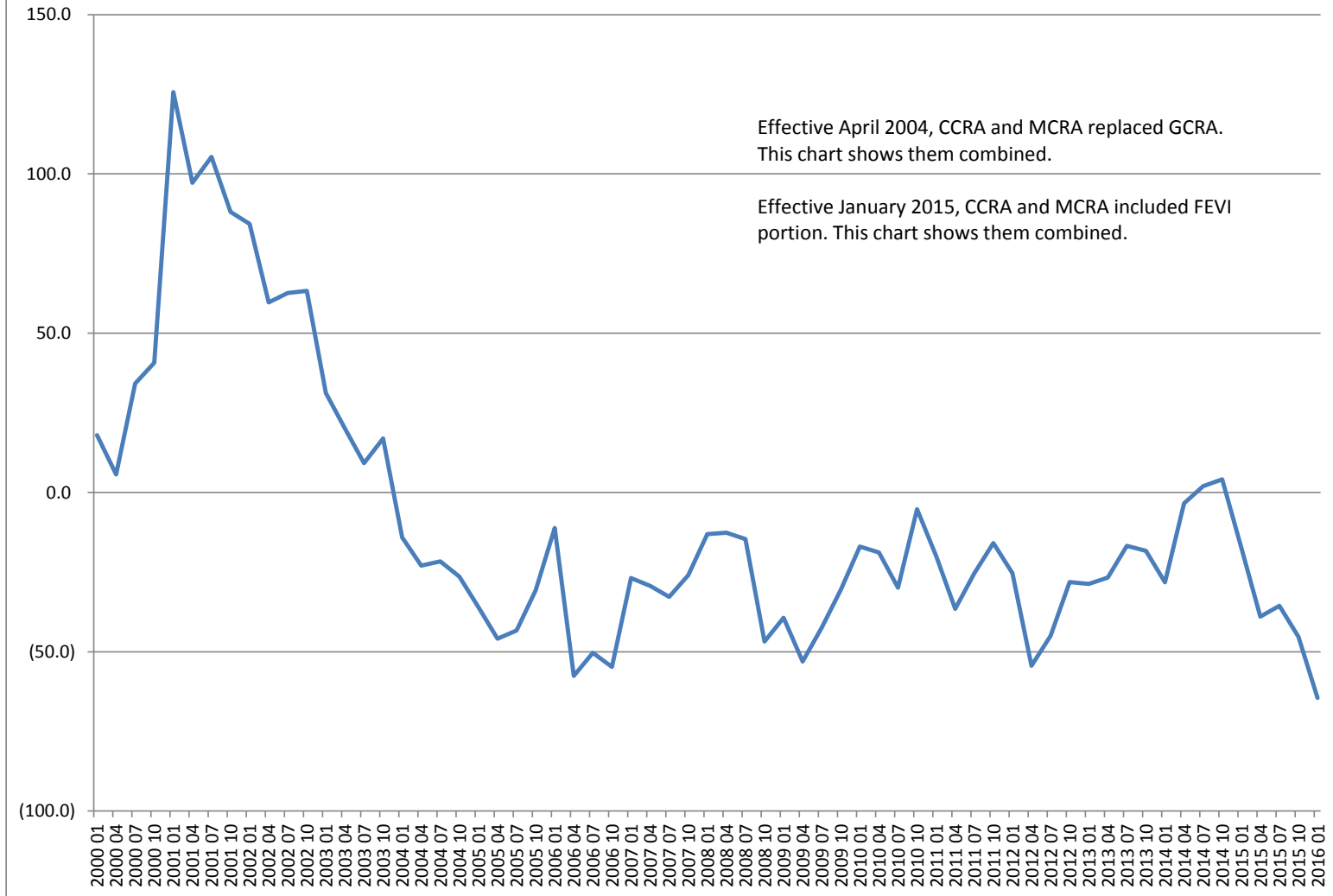
29

30 **Response:**

31 Please refer to the graph below, and refer to Attachment 4.4 for the fully functional Excel file.

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FEI Deferral Balance Net of Tax in \$ Millions



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1 4.4.1 Please calculate the following as a percentage of rate base: (i) the
 2 highest net-of-tax GCRA actual balance around January 2001 divided
 3 by the average net rate base of the utility in 2001; and (ii) \$50 million by
 4 the FEI ending net rate base for December 31, 2015. Show the
 5 calculations.
 6

7 **Response:**

8 The summary below shows the requested information for 2001 and 2015.

	Rate Base (millions)	Deferral Balance (millions)	Deferral Balance as a % of Rate Base
2001	\$2,209	\$126	5.7%
2015	\$3,661	\$50	1.4%

9

10

11

12

13 4.4.2 Using the January 2001 percentage calculated above, please multiply
 14 by the December 31, 2015 FEI net rate base. Would FEI consider this
 15 calculated figure for December 2015 to be relatively proportional to the
 16 January 2001 deferral account balance when adjusted for growth in the
 17 utility's rate base? Please elaborate.
 18

19 **Response:**

20 Using the January 2001 calculated percentage of 5.7%, multiplied by the 2015 rate base results
 21 in a calculated value of \$209 million. Based on the growth in rate base only, \$209 million would
 22 seem relatively proportional to the 2001 highest deferral balance of \$126 million, with the
 23 following caveats.

- 24 1. The GCRA was split into the CCRA and MCRA in 2004, so the CCRA (\$50 million) only
 25 represents one of the gas cost deferrals (sometimes the CCRA and MCRA balances can
 26 have an offsetting effect on overall customer rates, but sometimes they have a
 27 cumulative effect).
- 28 2. The actual impact to customer rates is based on the deferral balances being grossed up
 29 to pre-tax amounts and the tax rates in 2001 were higher than current.
- 30 3. There is a change in customer count since 2001, along with a change in average use
 31 rate.
 32

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1 However, FEI does not believe that the deferral account balance should be allowed to grow
2 proportionately with the size of rate base. The average annual bill of a residential customer is
3 lower today relative to what it was in 2001; therefore the impact of the recovery of a \$50 million
4 deferral balance on a customer's bill is greater today than it was in 2001.

5
6

7

8 4.5 Please explain further the "timely management of these balances to an
9 appropriate amount" and how that appropriate amount relates to the +/- \$50
10 million.

11

12 **Response:**

13 Timely management of these balances to an appropriate amount refers to the quarterly review
14 of deferral balances and recovery rates under the current Commission Guidelines. More
15 specifically, the mechanisms currently in place have correlated with managing the CCRA
16 deferral account balances within a band of approximately +/- \$50 million while supporting rate
17 stability and price transparency through an efficient process.

18

19

20

21 4.6 Please explain the linkage between the +/- \$50 million range for CCRA deferral
22 account balances and rate volatility mitigation, and if there is any difference if the
23 threshold is higher.

24

25 **Response:**

26 The linkage between the +/- \$50 million range for CCRA deferral account balances and rate
27 volatility mitigation is the need to balance the frequency and the magnitude of the rate changes
28 to maintain rate stability. The wider the dollar range for the CCRA deferral balance (affected by
29 the Commission Guidelines +/- percentage or +/- dollar amount), the greater the level of rate
30 volatility mitigation (reducing the frequency of changes); the narrower the range for the CCRA
31 deferral balance, the lower the level of rate volatility mitigation. A larger deferral balance from a
32 wider range will reduce the frequency (volatility) of rate changes but the resultant rate changes
33 will tend to be larger \$/GJ amounts.

34

35

36

37 4.7 Theoretically, if FEI had the ability to have no ceiling on CCRA deferral account
38 balances and its balance did not affect FEI's credit rating, solvency and debt

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1 covenants, could the commodity deferral account balance be managed in a
2 manner to mitigate rate volatility to the full extent necessary in times of temporary
3 market uncertainty? Please elaborate.
4

5 **Response:**

6 In the theoretical scenario where the size of the CCRA deferral account balances were not a
7 concern, it may be possible to reduce the number of commodity rate changes that would
8 otherwise be indicated in response to volatile market conditions. For example, the CCRA rate
9 could be held constant permanently (no commodity rate volatility) capturing all differences
10 between the actual incurred costs and the recoveries from rates in the CCRA deferral account.
11 With no boundary on the CCRA deferral account balance, it could grow as a deficit or surplus to
12 any level. The CCRA balance is included in rate base and depending on the balance could have
13 a material impact on earned return, taxes, and ultimately delivery rates.

14 However, this theoretical scenario would not provide the appropriate balance of managing
15 deferral account balances, including the timely recovery or refunding of deferral account
16 balances from/to customers, mitigating rate volatility, and providing customers with appropriate
17 price signals.

18

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1 **5.0 Reference: DEFERRAL ACCOUNTS**
2 **Commission letter L-5-01, Appendix III, p. 1;**
3 **Exhibit A2-2, FEI 2014 Price Risk Management Review Report, p. 39;**
4 **Exhibit B-1, pp. 3–4**
5 **Impact of CCRA deferral account size on FEI’s cost of capital**

6 Appendix III of Commission letter L-5-01 states:

7 BC Gas provided initial comments in a letter dated December 13, 2000. ... BC
8 Gas also indicates that slow recovery of large deferral account balances may be
9 perceived by financial markets as increasing the risk of the utility. Such a
10 perception could increase the cost of capital to the utility, thereby increasing
11 rates to customers.

12 On page 39 of the 2014 PRM Review Report (Exhibit A2-2), FEI states:

13 In addition, deferral accounts, if significant in value, can impact the utility’s
14 borrowing capacity, thereby harming cash flow and credit rating. Aether
15 comments: ‘The use of deferral accounts provides utilities and their investors with
16 a degree of comfort that potentially uncertain commodity costs will be recovered.
17 However, **an accumulation of large deferral balances can create credit and**
18 **liquidity concerns.** For instance, credit rating agencies tend to view very large
19 deferral balances negatively out of concern that subsequent recovery may not
20 fully occur.’ [Emphasis added]

21 FEI has grown significantly, both since 2000 and through amalgamation, so the historical
22 deferral account sizes and the relative impact on the FEI organization would presumably
23 not be the same absolute amount now.

24 5.1 Please explain if there are any recent, post-amalgamation, credit rating agency
25 reports which highlight credit and liquidity concerns due to the current total dollar
26 amount in deferral accounts at FEI, and if so, quantify the cost to FEI and to
27 ratepayers as a result. If there have been no post-amalgamation credit rating
28 agency reports, please explain if FEI has concerns about the size of the CCRA,
29 MCRA, or any other deferral accounts with respect to the impact on the cost of
30 capital.

31
32 **Response:**

33 Moody’s produced a credit ratings report in July 2015, which was based on post-amalgamation
34 figures. In this report Moody’s notes that FEI’s liquidity is adequate, however its financial metrics
35 are weak, and will remain weak over the next few years during the construction of several major
36 capital projects. Previous Moody’s ratings reports for FEI have stated that the deferral balances
37 have a near term impact on cash flows, as these balances are not collected until future periods.

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1 Should these balances increase to a material level, this near term cash flow impact would be
2 amplified, which could weigh negatively on FEI's credit rating, although it is not known what that
3 materiality level would be.

4 DBRS released ratings reports for FEI in January 2015 and 2016 both indicating no concerns
5 over FEI's post-amalgamation liquidity, and both viewing FEI's minimal deferral balances as a
6 credit positive factor. DBRS has also stated in past reports that amounts recorded in the CCRA
7 account are expected to be fully recovered within the next year, exposing FEI to a recovery lag.
8 They also make note of the fact that quarterly price adjustments help to mitigate the impact of
9 this recovery lag. Material changes to these mechanisms may likely cause DBRS to adjust their
10 views around this issue.

11
12

13

14 5.2 Please explain how CCRA deferral account balances of \$50 million to \$200
15 million are or would be perceived by financial markets today, explain the impact a
16 \$50 million and a \$200 million deferral account has on the cost of capital to FEI in
17 today's markets, and delineate the resulting dollar impact on customer rates.

18

19 **Response:**

20 From a financial markets perspective, deferral accounts can represent a form of implied
21 financing for utilities, and as such, would be looked upon similarly as a conventional form of
22 financing obligation. The perception of this by the financial markets as well as any impact on the
23 cost of capital of FEI would depend on the relative amount of the deferral account balance
24 compared to the size of the entity, and the recovery mechanism. A deferral account balance of
25 up to \$200 million would not be expected to appreciably impact the cost of capital of FEI in the
26 absence of other factors, but if allowed to accumulate along with the expected growth of the
27 other financial obligations of FEI, there may be an impact to FEI's marginal cost of capital, the
28 extent of which would be dependent on the capital market's view of FEI's financial risk.

29

30

31

32 On page 4 of its Application, FEI states:

33 In terms of the rate setting mechanism enhancements, FEI currently considers a
34 band of approximately **+/- \$50-60 million** a reasonable range for the commodity
35 deferral account. Deviations falling materially outside of this range can pose
36 challenges for FEI **in terms of the timing of refunding or recovering**
37 **significant dollar amounts from customers** and can **impact FEI's balance**
38 **sheet and potentially its credit rating and borrowing capacity.** [Emphasis
39 added]

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1 5.3 Please explain the proposed +/- \$10 million increase the CCRA, including how
2 the increase above +/- \$50 million was derived.

3

4 **Response:**

5 The increase from +/- \$50 million to a range of +/- \$50 to \$60 million is to account for the
6 inclusion of Vancouver Island baseload volumes, and other volume adjustments which include
7 customers returning from the Customer Choice program to FEI's standard commodity rate
8 offering. There is no precise calculation, but with the Guideline percentages and dollar
9 thresholds with the additional Vancouver Island and other volumes, the range has expanded.
10 There has been no change to FEI's quarterly rate setting process, the Commission Guidelines,
11 or the calculations as a result of the addition of Vancouver Island and other volumes to the
12 CCRA portfolio, nor is there any need for any changes as a result of the increased commodity
13 volume in the CCRA portfolio as the rate change mechanism appropriately handles changes in
14 the baseload volumes.

15

16

17

18 5.4 Please quantify the magnitude of deviation which can pose challenges for FEI in
19 terms of the timing of refunding or recovering significant dollar amounts from
20 customers.

21

22 **Response:**

23 It is difficult to quantify the magnitude of deviation which could pose challenges for FEI as it
24 would depend on a number of factors as discussed in the responses to BCUC Scope A IRs
25 1.5.1 and 1.5.2. However, the fact that FEI has been able to manage the CCRA deferral
26 balance within a band of approximately +/- \$50 million under the quarterly rate setting
27 mechanism has provided greater certainty that FEI will be able to recover its costs from, or
28 refund surpluses to, customers in a timely fashion.

29

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1 **6.0 Reference: REQUEST FOR COMMISSION APPROVAL**

2 **Exhibit B-1, pp. 3–4**

3 **Enhancements to the rate setting mechanism**

4 FEI states on page 4 of its Application that:

5 FEI notes that it is **not proposing any changes to the Commission guidelines**
6 for setting gas cost recovery rates and managing the gas cost reconciliation
7 balances as set out in Letters L-5-01 and L-40-11 (the Guidelines) with respect to
8 the consideration of the full circumstances. It is merely proposing some criteria to
9 provide further clarification of when consideration be given to the
10 appropriateness of commodity rate proposals for timeframes beyond the 12-
11 month outlook since the guidelines currently do not include any specific metrics
12 or criteria in this regard. [Emphasis added]

13 6.1 Please confirm, or otherwise explain, that, in item 2(a) of the requested approvals
14 listed on page 3 of the Application, FEI is proposing a change to the Commission
15 guidelines for setting gas cost recovery rates and managing the gas cost
16 reconciliation balances as set out in Commission letters L-5-01 and L-40-11, with
17 proposed changes to the commodity rate change cap and to the number of
18 consecutive times the cap would be used.

19
20 **Response:**

21 Confirmed, with the following clarification.

22 In Letter L-40-11, the Commission stated that:

23 ...the Guidelines should be applied in a flexible manner, considering the full
24 circumstances prevailing at the time when a quarterly report is under review. The
25 Commission intends to consider the full circumstances and other criteria in the review of
26 the commodity and midstream cost recovery rates. As well as the Guideline trigger
27 mechanism and rate methodology, consideration will be given to factors such as the
28 current deferral balances and, based on the forecast costs, the appropriateness of any
29 rate proposals over a 24-month timeframe.

30
31 FEI is proposing changes that will not change the Commission’s approach stated above, i.e.,
32 consideration of full circumstances at the time of the quarterly report review. Nor will the
33 proposals change the other main components for the commodity rate setting mechanism. The
34 other main components include the following:

- 35
36 • a review and potential adjustment of rates on a quarterly basis;
- 37 • a rate change trigger mechanism of +/- 5%;



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- 1 • a minimum rate change threshold of +/- \$0.50/GJ; and
- 2 • typically, a 12-month prospective period for rate setting.
- 3 The proposed changes, i.e., implementation of a commodity rate change cap and the number of
- 4 consecutive times the cap would be used provided the deferral balance is maintained within a
- 5 reasonable range, provides another component, to work together with other existing
- 6 components.
- 7 The proposed criteria summarized on pages 3-4 of the Application are intended to provide
- 8 further clarification as to when consideration should be given to the appropriateness of
- 9 commodity rate proposals for timeframes beyond the 12-month outlook.

10

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1 **7.0 Reference: RATE SETTING ENHANCEMENTS APPLICATIONS TO OTHER**
 2 **UTILITIES**

3 **Exhibit B-1, Section 3.2.3, p. 23**

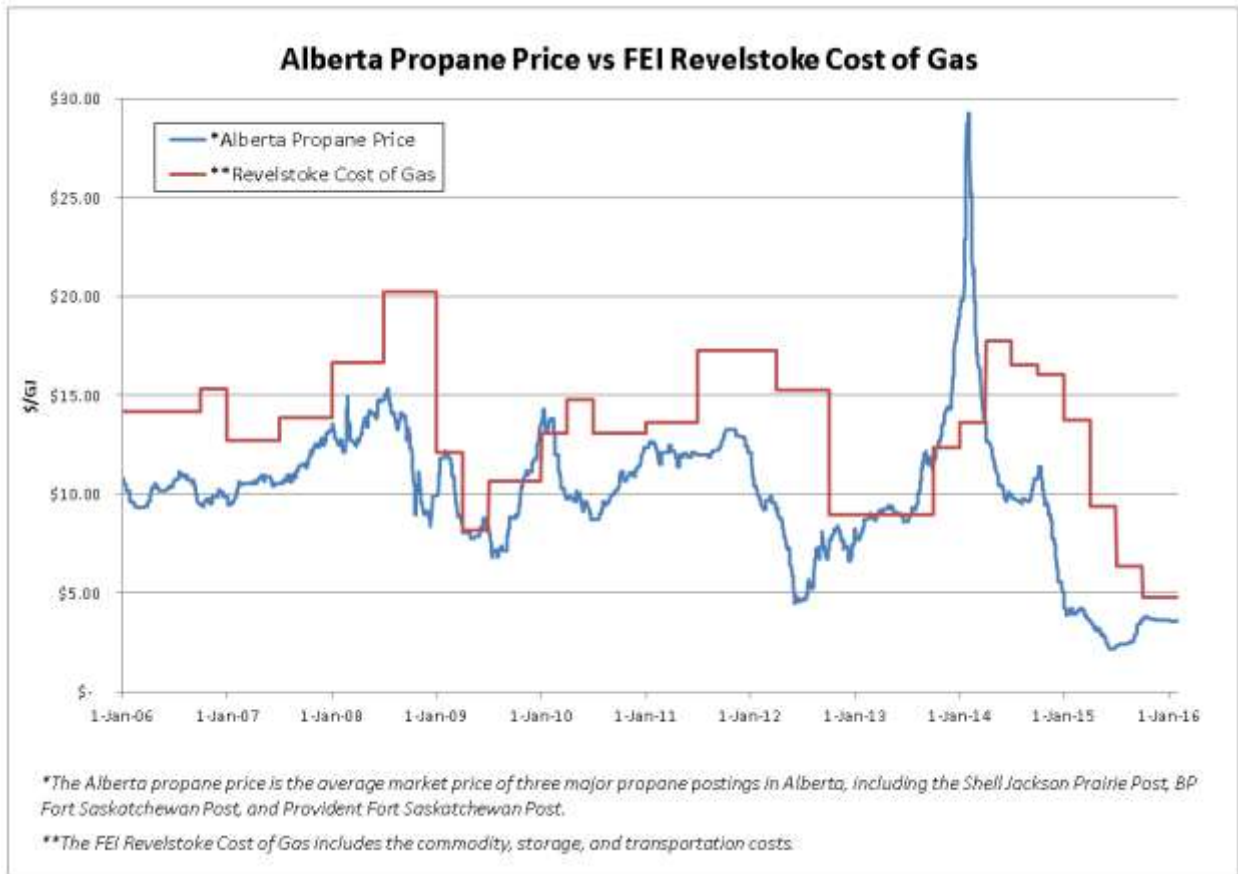
4 **Applicability to propane utilities**

5 On page 23 of the Application, FEI states that “propane utilities will typically have higher
 6 and more volatile underlying commodity costs than those of gas utilities given the nature
 7 of the crude and propane markets. This means that rate change thresholds or rate
 8 change caps that apply to regional gas utilities may not be appropriate for propane
 9 utilities.”

10 7.1 Please provide a graph showing the market price of propane and the per
 11 gigajoule Cost of Gas for FEI’s Revelstoke customers for the period from January
 12 2006 to January 2016.

13
 14 **Response:**

15 The following figure illustrates Alberta’s market price of propane and the Cost of Gas for FEI’s
 16 Revelstoke (i.e. propane) customers for the period from January 2006 to January 2016.



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1 It should be noted that the Alberta market propane price does not include the same components
2 as the Revelstoke Cost of Gas which includes commodity, storage, and transportation costs.
3 This is why the Cost of Gas is generally higher than the market prices. However, the cost of
4 gas still exhibits significant volatility like the market prices.

5
6

7

8 7.2 Please describe whether FEI considers that Revelstoke customers have
9 concerns regarding the volatility of propane commodity rates and, if so, what FEI
10 considers to be the average Revelstoke customer's tolerance for commodity rate
11 volatility. Please describe the nature of the customer feedback used to determine
12 this tolerance.

13

14 **Response:**

15 FEI has not conducted any surveys to determine an average Revelstoke customer's tolerance
16 level for commodity rate volatility. However, FEI received general feedback at a meeting with
17 Revelstoke's City Council members about their concerns over high and fluctuating propane
18 rates in the past number of years, especially after the cold winter of 2013/14.

19

20

21

22 7.3 Please describe the price risk management strategies FEI employs for managing
23 the cost of propane for its Revelstoke customers.

24

25 **Response:**

26 The price risk management strategies FEI employs for managing the cost of propane for its
27 Revelstoke customers include fixed price physical purchases, propane storage, purchasing
28 supply from multiple locations in Alberta, and the use of a propane cost deferral account. For
29 winter 2015/2016, propane storage and supply from multiple locations in Alberta, as well as the
30 propane cost deferral account were used.

31

32

33

34 7.4 Please confirm that FEI applies the 12 month amortization and +/- 0.95 to 1.05
35 cost/recovery ratio deadband as set out in the rate setting guidelines in
36 Commission letters L-40-11 and L 5 01.

37

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1 **Response:**

2 Confirmed.

3

4

5

6 7.4.1 In the past ten years, has FEI proposed extending the amortization
7 period beyond 12 months or otherwise modifying the application of the
8 guidelines in order to reduce the impact of rate volatility on Revelstoke
9 customers? If not, why not?

10

11 **Response:**

12 In the past ten years, FEI has proposed extending the amortization period beyond 12 months
13 only once for Revelstoke customers, which was a proposal to extend to 15 months in the 2012
14 Third Quarter Gas Cost Report for Revelstoke (2012 Q3 Report).

15 In the 2012 Q3 Report FEI provided 3 sets of forward prices (based on NYMEX WTI light sweet
16 crude oil prices, Mt. Belvieu swaps and a 50/50 blend of the two). Based on the three forecasts,
17 the rate change trigger mechanism was calculated to be in the range of 187.4 to 187.6
18 percentage that fell outside the dead band of 95 to 105 percent, indicating that current cost
19 recovery rates and a propane decrease was required effective October 1, 2012. The resulting
20 change in reference price equated to a rate decrease of \$7.384/GJ. However, the 2012 Q3
21 Report also indicated that an increase of \$1.171/GJ would be triggered effective January 1,
22 2013. FEI recommended an alternative scenario for Commission review whereby rates were
23 calculated over a 15 month period. The alternate scenario was consistent with Commission
24 Letter L-40-11 which allows for the consideration of full circumstances. The Commission
25 approved rates effective October 1, 2012 based on the 15 month timeframe by Order G-117-12.

26 In addition to extending the amortization period as discussed above, even though the rate
27 change trigger mechanism indicated a rate change, FEI proposed to leave rates unchanged in
28 both the 2011 First Quarter Gas Cost Report for Revelstoke (2011 Q1 Report) and the 2012
29 Second Quarter Gas Cost Report for Revelstoke (2012 Q2 Report), in order to reduce the
30 impact of rate volatility on Revelstoke customers.

31 In the 2011 Q1 Report all three sets of forward prices indicated an under recovery over the next
32 12 months that fell outside the deadband, FEI proposed leaving rates unchanged at April 1,
33 2011 consistent with Commission Letter L-40-11 which allows for the consideration of full
34 circumstances. The circumstances included high price volatility, and the current heating season
35 was coming to an end where consumption volumes would be reduced and remaining at the
36 current recovery rates was forecast to result in only a modest change in the deferral balance
37 over the next quarter. The Commission approved leaving the rates unchanged at April 1, 2011
38 by Letter L-15-11.

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1 In the 2012 Q2 Report all three sets of forward prices indicated over recoveries over the next 12
2 months that fell outside the deadband, FEI proposed leaving rates unchanged at July 1, 2012
3 consistent with Commission Letter L-40-11 which allows for the consideration of full
4 circumstances. The circumstances included high price volatility, consumption volumes were low
5 in the summer, and FEI suggested it would be preferable to reset the propane cost recovery
6 rates next quarter at the beginning of the 2012/2013 heating season and when propane prices
7 may be less volatile. The Commission approved leaving the rates unchanged at July 1, 2012 by
8 Letter L-33-12.

9
10

11
12 7.5 Please discuss whether FEI considers that rate change thresholds and/or rate
13 caps should be applicable for Revelstoke and other propane utilities.

14
15 **Response:**

16 FEI understands this question to be asking if changes to the rate setting guidelines that are
17 being proposed in this Application should also apply to Revelstoke or other propane utilities.
18 FEI would have to do further assessment regarding rate setting for Revelstoke and other
19 propane utilities and the appropriate level of deferral account balances before determining if the
20 proposed changes are applicable.

21

Attachment 4.4

REFER TO LIVE SPREADSHEET MODEL

Provided in electronic format only

(accessible by opening the Attachments Tab in Adobe)