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British Columbia Utilities Commission
900 Howe Street, Box 250
Vancouver, BC, V6Z 2N3
Attn: Patrick Wruck, Commission Secretary
By Web Posting

Dear Mr. Wruck:

Re: FortisBC Energy Inc. 2016 Rate Design Application ~ Project No.3698899
BC Sustainable Energy Association and Sierra Club BC
Submissions on Cost of Service Allocation and Revenue to Cost Ratios

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These are BCSEA-SCBC's submissions in accordance with the timetable set out in the Commission's September 7, 2017 letter.[1]

This follows the streamlined review process proceeding on September 12, 2017 at which the issues were:

i. the Cost of Service Allocation (COSA) studies included in the Application;

ii. whether the revenue to cost (R:C) ratio; the margin to cost (M:C) ratio; or a combination of both R:C and M:C ratios should be used to guide rate design, and

iii. the corresponding range(s) of reasonableness of the selected ratio(s).

In summary, BCSEA-SCBC take the following positions:

1. BCSEA-SCBC have no objection to the COSA studies included in FEI's Application as modified by FEI following the evidence provided by Elenchus Research Associates, Inc. under contract for the Commission.
2. BCSEA-SCBC have a preference for adoption of the Margin to Cost (M:C) ratio over the Revenue to Cost (R:C) ratio, because the M:C ratio conveys the revenue to cost concept more directly. However, they acknowledge that the two measures are equivalent, except in terms of the size of the range of reasonableness, which is addressed in the next point.
3. BCSEA-SCBC believe that the range of reasonableness should be narrower than FEI's proposed 90% to 100% range for R:C ratios. BCSEA-SCBC believe that consideration of rate rebalancing should be triggered where R:C or M:C ratios vary from unity, noting that this does not mean that rate rebalancing to achieve R:C or M:C ratios of unity will necessarily be proposed or approved depending on the circumstances. In the alternative, BCSEA-SCBC support Commission approval of range of reasonableness of 95% to 105% for either M:C or R:C ratios.

Range of Reasonableness

These submissions focus on the range of reasonableness.

[1] Exhibit A-14

To begin, BCSEA-SCBC consider it desirable that rates be set so as to provide economically optimal price signals regarding the use of the commodity. Accordingly, BCSEA-SCBC believe that rate rebalancing should be considered where rates depart from economically optimal price signals.

FEI confirmed during the SRP that even though some rate class might fall outside the range of reasonableness that fact does not automatically trigger a requirement for the utility to propose rate rebalancing. FEI's consultant Gail Tabone said:

> MS. TABONE: Well, I think we have to go back, and I hate to bring up the Bonbright principles because everybody talks about them all the time. But the idea is you're trying to balance a lot of different things; you're trying to have fair and equitable rates. You're also trying to have rate stability and some other things. And so, when you put together a proposal, you look at the cost of service as one tool to see if you've got fair and equitable rates, and then you look at all of the other factors as well, and you come up with a whole package. And so while they may be asking for approval for a range of reasonableness, what they're really asking for is approval to rebalance. So, it's really the rebalancing numbers that they're requesting approval for and then further down the road the rates.[2]

In addition, FEI confirmed that where a rate class's cost of service ratio is outside the range of reasonableness the utility might propose a rate rebalancing that didn't bring the ratio all the way to the range of reasonableness. Ms. Tabone said:

> MS. TABONE: Right. And you could have rebalancing that is not exactly equal to the range of reasonableness as well. So, if you had somebody who was at a 50 percent revenue-to-cost ratio you may propose to rebalance them by 10 percent and not go all the way to the 90 percent revenue to cost ratio. So, you're looking at all those things. And you could have rebalancing that is not exactly equal to the range of reasonableness as well.[3]

FEI confirmed that in its view where a rate class's cost of service ratio is within the range of reasonableness cost of service is a "non-factor" in the utility's decision whether to propose rate rebalancing for a rate class. During the SRP, FEI was asked "What if [the rate class's] revenue-to-cost ratio was inside the range of reasonableness but either below or above unity. Does that become a non-factor or is it still one of the factors to be considered among many?" FEI's response was:

> MS. TABONE: We view it as a non-factor. And the reason is, when we look at any number between 90 to 110 we're saying if they're 92 percent they're meeting their cost of service. And so, we don't distinguish between 92 and 102, for example. We basically say if they're in that range that's as close as we can get to measuring whether they're paying their cost of service or not. And so, you have to take some kind of range at some point and break it off whether it's above and below and whether they're paying their fair share. But we don't think that the gradation between, you know, 92 percent and 93 percent is significant given all

[2] T5:490-491
[3] T5:491

> the uncertainty and the estimates and judgment in a cost of service study. So, we would say as long as they're in that range they're the same as each other.[4]

FEI confirmed during the SRP that changing the range of reasonableness from 90%-110% to 95%-105% would mean that where a rate class has a revenue-to-cost ratio between 90% and 95%, or between 105% and 110%, the utility would consider the possibility of rate rebalancing, whereas it would not do so in those circumstances if the range of reasonableness was 90% to 110%. The exchange was as follows:

> MR. ANDREWS: Okay. So, one of the consequences of changing from 90 to 110 to 95 to 105 would be that, in the event that a customer class has a revenue-to-cost ratio that was either between 90 and 95 or between 105 and 110, Fortis would consider that as a factor going towards whether there might be rebalancing among the other factors that would go into Fortis's decision, whether to actually propose rebalancing for that rate class.
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> MR. GOSSELIN: Right.
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> MS. TABONE: Exactly.[5]

BCSEA-SCBC explored the potential disadvantages of rebalancing rates during the SRP.[6] Narrowing the range of reasonableness would increase the number of situations in which the utility would <u>consider</u> whether or not to propose rate rebalancing. However, BCSEA-SCBC submit that this is not a bad thing. The utility has ample room to refrain from proposing rate rebalancing if it would not be warranted for whatever reason.

During the SRP, FEI acknowledged that the size of the range of reasonableness does not affect whether the utility will recover its cost of service.[7]

FEI's rationale for maintaining the 90%-110% R:C range of reasonableness is that this range was approved by the Commission in the past and the accuracy of FEI's revenue to cost analysis has stayed the same since then. Mr. Perttula said:

> MR. PERTTULA: It was in fact the Commission's judgment that that level was appropriate. So as far as I know there wasn't sort of numerical calculations or anything like that, but that may have gone on at the Commission rather than in any way that we would be aware of it.[8]

Further:

> MR. ANDREWS: Okay. So the main rationale – tell me again if I'm correct – that Fortis has for keeping the 90-110 is that that was what was recited in the past and that the accuracy of Fortis's revenue cost methodology has not -- has stayed the same since the time that 90-110 was approved.

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[4] T5:491-492
[5] T5:492
[6] T5:493-494
[7] T5:494-495
[8] T5:495-596

> MS. TABONE: Yeah, that's correct.[9]

The research presented by Elenchus indicates that other jurisdictions use a range of reasonableness that is more narrow than FEI's proposed 90%-110%: some use 95%-105%, others seek to be close to unity. FEI acknowledged in the SRP that it is not making the argument that its proposed 90%-110% range is warranted because its own revenue cost analysis is less accurate than the analysis used by the other utilities.

> MR. ANDREWS: And to be clear, Fortis is not arguing that it actually has evidence that its cost analysis or -- sorry, a revenue/cost analysis based on the cost of service analysis is either less accurate or more accurate than the revenue/cost methodology that's used in these other specific jurisdictions?
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> MS. TABONE: Right. We didn't look specifically at the other jurisdictions, but we don't have any evidence that would show we're any more precise than anybody else or any less precise.

While one of FEI's reasons for the concept of a range of reasonableness is that there are different, valid methodologies for determining revenue to cost ratios, FEI acknowledged during the SRP that the method it has chosen to implement is the best method for FEI to use under all of the circumstances.[10] BCSEA-SCBC submit that if the Commission agrees and approves FEI's revenue to cost methodology then it follows that the R:C (or M:C) ratios are the best estimate of the extent to which each rate class is paying its share of its costs.

This is the essence of BCSEA-SCBC's disagreement with the assertion by Mr. Todd of Elenchus that there is absolutely no useful information provided where a rate class's R:C ratio is different from unity but within an arbitrarily defined range of reasonableness.

In BCSEA-SCBC's view, the farther away a rate class's R:C ratio is from unity the stronger the weight of evidence that the class is paying more, or less, than its share of costs. Mr. Todd acknowledged during the SRP that for R:C ratios that are outside the range of reasonableness there is directionality: the farther from unity the more, or less, the share of costs is being paid. Asked about a hypothetical situation where rate classes have R:C ratios of 5% and 89% (with a 90%-110% range of reasonableness) Mr. Todd said that the former would require more adjustment than the latter:

> MR. ANDREWS: Would you agree that -- sorry. Would you agree with me that if one customer class had a range at a revenue cost ratio of 89 and another had a revenue cost ratio of 5, that the inference is that the one with 5 is more out of balance with its revenue to cost than the one with 89? They're both outside the range of reasonableness so we're not saying they're automatically identical. But would you agree that there is some directionality there to the number?
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> MR. TODD: Yes, they both need adjustment. One would require more adjustment than the other, I agree.[11]

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[9] T5:496
[10] T5:502.
[11] T5:515-516

BCSEA-SCBC submit that the same directionality applies to R:C ratios that are within the range of reasonableness. Where the range of reasonableness is 90%-110% and one rate class has a R:C ratio of 99% and another has a R:C ratio of 110%, 20 percentage points higher, the weight of evidence is that the first rate class is paying less of its share than the second rate class. This is why BCSEA-SCBC take the position that consideration of rate rebalancing should be triggered where R:C or M:C ratios vary from unity, noting that this does not mean that rate rebalancing to achieve R:C or M:C ratios of unity will necessarily be proposed or approved depending on the circumstances.

In any event, Mr. Todd's evidence is that both a 90%-110% range of reasonableness and a 95%-105% range of reasonableness would be reasonable for the Commission to approve:

> MR. ANDREWS: And I think you've said that in terms of the size, 90 to 110 percent is a reasonable range? Is that correct?
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> MR. TODD: Yes, that's correct.
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> MR. ANDREWS: And that 95 to 105 would also be a reasonable range?
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> MR. TODD: If that is what the Commission decided, yes, that would be a reasonable range.[12]

In conclusion regarding the range of reasonableness, BCSEA-SCBC support a Commission determination that FEI should consider rate rebalancing where R:C or M:C ratios vary from unity, noting that this does not mean that rate rebalancing will automatically be required. In the alternative, BCSEA-SCBC support Commission approval of a range of reasonableness of 95% to 105% for either M:C or R:C ratios.

All the above is respectfully submitted.

Yours truly,

William J. Andrews

Barrister & Solicitor

[12] T5:505-506