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

Attention: Mr. Patrick Wruck, Commission Secretary

Dear Sirs/Mesdames:

Re: FortisBC Alternative Energy Services Inc. 2018/2019 Revenue Requirements and Cost of Service Rates Application for the Thermal Energy Service to Delta School District No. 37 ~ Project No.1598949

We enclose for filing in the above proceeding the Reply Submission of FortisBC Alternative Energy Services Inc., dated February 21, 2019.

Yours truly,

FASKEN MARTINEAU DuMOULIN LLP

[Original signed by]

Matthew Ghikas
Personal Law Corporation

MTG/gvm
Enclosure

BRITISH COLUMBIA UTILITIES COMMISSION

IN THE MATTER OF THE UTILITIES COMMISSION ACT (THE "ACT")

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

FortisBC Alternative Energy Services Inc.

Application for Approval to Charge the Cost of Service Rate to Delta School District No. 37

Reply Submission of FortisBC Alternative Energy Services Inc.

February 21, 2019

MATTHEW GHIKAS
FASKEN MARTINEAU DUMOULIN LLP
Legal Counsel to FAES

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PART ONE: INTRODUCTION

1. The Delta School District ("DSD") remains entrenched in a view of past events that cannot be reconciled with contradictory documents, the fundamentals of cost of service regulation, the BCUC's 2012 CPCN and Rates Decision ("2012 Decision")[1], the regulatory compact or commercial reason.

2. The DSD has modified its long-standing estoppel arguments in response to FAES's legal submissions, but its new legal theory is still flawed. The DSD's written argument ("DSD Submission") side-steps the fundamental legal impediments to its arguments. Those legal impediments include the requirement for terms and conditions of service (or any amendments) to be set out in a BCUC-approved written rate schedule, the Entire Agreement clause, and the absence from the approved rates any quantitative performance requirements for GHG savings, natural gas use or heat pump use.

3. The DSD is getting the service for which it contracted, and which the BCUC approved. The DSD has been, and will remain after the switch, much better off with this thermal energy service - in terms of budget impacts and GHG emissions - than it would have been in the absence of the Project (called "Business As Usual"). The DSD wants permanently subsidized service because it got used to it while on the transitional Market Rate ("MR"), which is an unreasonable expectation.

4. FAES' January 11, 2019 Submission ("Initial Submission") anticipated many of the arguments raised in the DSD Submission. FAES's Reply Submission avoids repeating the content of the Initial Submissions wherever possible. We have favoured an approach that focusses on the main points raised by the DSD, instead of a line by line rebuttal.[2] As requested by Order G-31-19, we have avoided referencing any of the DSD's new evidence that has been excluded from the record.

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[1] BCUC Order G-31-12 and Decision dated March 9, 2012.

[2] FAES disagrees with many discrete statements in the DSD Submission. Our silence on a particular point should not be construed as agreement.

5. FAES's Reply Submission is organized around the following points:

- **Part Two:** The DSD's portrayal of the facts sticks closely to Mr. Geyer's Affidavit. The DSD has left unreconciled its version of events with the contradictory documentation and evidence identified by FAES.

- **Part Three:** The DSD's characterization of the issues has changed. The DSD makes the notable concession that FAES has the right to apply to the BCUC to seek the switch from the MR to the COS Rate.

- **Part Four:** The DSD's revised estoppel argument, and its argument that there are implied detailed "objects" and discrete quantitative performance requirements, are incompatible with the UCA and public utility law.

- **Part Five:** On the question of whether the DSD should be switched from the MR to the Cost of Service ("COS") Rate at this time, the DSD concedes key facts highlighted in Part Three of FAES's Initial Submission. The DSD instead argues that these concessions are irrelevant, for reasons that are both conceptually and factually flawed.

- **Part Six:** The DSD's request for further process to assess the prudence of the Project capital costs should be rejected. The DSD has not rebutted the presumption of prudence in the face of ample evidence that the capital costs are within the expected cost range and the system is performing well.

6. Granting the approvals that FAES seeks (see Appendix D to the Application), upholds the agreed and BCUC-approved terms and conditions of service and serves the long-term interests of both Parties. It is the just and reasonable result.

PART TWO: THE DSD'S OUTLINE OF THE FACTS IS INCOMPLETE

7. The DSD spends a significant portion of its Submission outlining a chronology of events that sticks very closely to Messrs. Geyer and Poole's affidavits, except where that evidence turns out to have been unhelpful to the DSD. In other words:

- First, the DSD has omitted important facts in the pre-CPCN chronology that contradict the DSD's contention that it had been misled about the proposed Project and service.

- Second, the DSD is silent on the BCUC's findings in the 2012 Decision, which spelled out the implications of the RDA and contradicted the alleged pre-contractual representations.

- Third, although Mr. Geyer had been adamant that no one from the DSD had read the 2012 Decision – a key part of the DSD's theme that they had relied on FAES - the DSD now admits that Mr. Geyer had been mistaken.

- Fourth, the DSD's description of its system performance evidence has some notable shortcomings, including its reliance on Mr. Poole's old emails as evidence of system design problems, and not acknowledging MCW's and Mr. Cleveland's endorsement of aspects of the design approach that FortisBC and JCIC had used.

A. THE DSD'S DESCRIPTION OF THE EVENTS LEADING TO THE RDA OMITS IMPORTANT EVIDENCE

8. The DSD has spent approximately 10 pages of its Submission recounting events that occurred between 2008 and the filing of the CPCN Application in 2011. FAES's primary response to the DSD on this point is that, consistent with the UCA, the BCUC should have regard only to the approved terms of the RDA.[3] In the paragraphs that follow, we have put that point

[3] See FAES Initial Submission, paras. 13-17, 77-82.

aside and address the specific shortcomings in the DSD's presentation of the evidence. The notable failing is the DSD's unwillingness to reconcile its position with contradictory documentation.

9. FAES's Rebuttal Evidence detailed several instances where Mr. Geyer had singled out statements in documents without acknowledging contradictory language elsewhere in the documents or in related correspondence. FAES discussed some of these inconsistencies in the Initial Submission.[4] Yet, the DSD has made no attempt to address these inconsistencies in its Submission. The DSD's silence in this regard is telling. Its theme that it had been taken advantage of by FAES quickly falls apart with a more inclusive review of the documents.

10. Some notable facts that the DSD has elected to omit from its "Facts" section include:

- **There is an Entire Agreement clause:** The DSD has not explained why, with the benefit of legal advice, it had agreed to an Entire Agreement clause if it was intending to continue parsing email correspondence exchanged during fluid negotiations for guidance as to the implications of the RDA.

- **The DSD wanted a COS regime:** The DSD had wanted a cost of service regime, despite being aware that there were a variety of other alternatives available.[5] The fact that there are no quantitative performance requirements with respect to GHG emissions or heat pump output is no accident.[6] It is consistent with cost of service ratemaking, which focusses on recovery of prudent costs incurred to deliver a reasonable level of service.

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[4] See for instance, FAES Initial Submission, starting at para. 107.

[5] In the 2012 CPCN Proceedings, the DSD Responded to the BCUC IR 1.1.3 as follows: "Delta SD is aware that there are a variety of rate options that may exist, and that the role of the Commission is to review (level of detail at the discretion of the Commission) and approve the rate, whether cost-of-service or negotiated".

[6] 2012 CPCN Application, Exhibit C1-2, DSD Response to BCUC IR 1.13.6:

BCUC Question: "Under the terms of the Energy System Service Agreements and the Energy System Rate Development Agreement between FEI and SD, is FEI required to warrant that the thermal energy systems that are to be installed by FEI will deliver the approved Energy Savings Measures?

DSD Response: No, they are unrelated."

- **FAES negotiated a right to apply to switch to the COS Rate for this very scenario:** FortisBC had insisted upon having a right to apply to the BCUC to initiate a switch to the COS Rate in the event that the parties disagreed on the appropriate time to switch.[7]

- **Detailed design would follow the CPCN:** The DSD emphasizes specific performance outcomes based on alleged pre-contract representations, without acknowledging that the Parties well understood that detailed design had yet to occur.[8]

B. THE DSD HAS GLOSSED OVER THE BCUC'S 2012 FINDINGS, WHICH SPELL OUT THE IMPLICATIONS OF THE RDA

11. The 2012 Decision is an important answer to the DSD's theory of the case because it predated the final execution of the RDA. In it, the BCUC outlined the implications of the RDA in a manner that is consistent with FAES's position. The DSD Submission does acknowledge that the BCUC issued the order, but avoids any reference to the content. The DSD makes no attempt to reconcile its contention that it had been misled about the Project and the RDA with observations of the BCUC, including:

- The MR was "transitional"[9];

- The balance in the District Deferral Account ("DDA") "will be recovered in rates in subsequent years as part of the cost of service";[10]

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7 Exhibit B-7, FAES rebuttal Evidence, pp. 10 – 14.

8 2012 CPCN Application, p. 31: "FEI expects that the detailed design work carried out by JCLP, the use of contractor cost estimates to define geo-exchange costs, and the diligent project management techniques employed by JCLP will minimize variations from the package price." See also CPCN Decision, p. 30: "The initial analysis and investigation of alternatives focused on site specifics: heating system compatibility, site layout, local geological and hydro-geological conditions and system costs. The final analysis of technology alternatives will follow CPCN approval with site specific surveys, detailed design, installation, testing and commissioning. (Exhibit B-3, BCUC 1.35.4)"

9 There are a number of references to the Market Rate as being "transitional" in the 2012 Decision. See, for instance, p. 45; section 6.3.4, pp. 51-53.

10 2012 Decision, pp. 42-43. See also p. 80: "These deferred costs, resulting from the upfront discount, are shifted to the future years with carrying costs that reflects a weighted cost of debt and equity."

- Significant transfers to future years through the DDA would raise "issues of intergenerational equity";[11]

- "FEI expects a reasonable transition period is within 2 to 5 years";[12]

- The initial Project cost estimate was prepared at an AACE Class 3 level of accuracy. and that "final analysis of technology alternatives would follow CPCN approval."[13]

- "Given that GHG reductions are cited as a primary need, the Panel finds it unusual that there is no requirement for FEI to actually achieve the reductions.[14]

- "While Delta SD claims to be aware of clauses in the individual service contracts which hold FEI accountable for operational obligations, such as service reliability, guaranteed GHG reduction, or energy savings (Exhibit C1-2, BCUC 17.1), the BCUC was unable to locate these clauses after examining the Contracts."[15]

12. No one who read the 2012 Decision could reasonably have reached the conclusion that Mr. Geyer and the DSD reached about the terms and conditions of service. As described next, the DSD now concedes that it did review the 2012 Decision.

C. MR. GEYER'S EVIDENCE THAT NO ONE REVIEWED THE 2012 CPCN DECISION TURNS OUT TO HAVE BEEN INCORRECT

13. An integral element of the estoppel doctrine, upon which the DSD's position is based, is reliance on the alleged misrepresentation. Thus, a critical facet of Mr. Geyer's Affidavit was that he and the DSD were relying on FAES throughout - to the extent that no one at the DSD even reviewed the 2012 Decision. However, that centrepiece of the Geyer Affidavit has now disappeared from the chronology in the DSD Submission. The only reference made in

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[11] 2012 Decision, pp. 59-60.

[12] 2012 Decision, p. 53.

[13] 2012 Decision, p. 29.

[14] 2012 Decision, p. 64.

[15] 2012 Decision, p. 42.

the "Facts" section of the DSD Submission to the period between the 2012 Decision and the approval of the RDA is in paragraph 42, which states: "On June 5, 2012, the BCUC issued Order No. G-71-12 approving the rate design and on June 25, 2012, the BCUC issued Order No. G-88-12 approving the rate."

14. The DSD's decision to downplay Mr. Geyer's evidence in this regard is not surprising, since contemporaneous correspondence directly contradicted his recollection. Although the DSD has only implicitly abandoned Mr. Geyer's evidence in the "Facts" section of its Submission, there is an explicit admission later on in paragraph 107:

> Throughout the course of the negotiation and execution of the RDA, the DSD was represented by legal counsel. However, the DSD was not represented by legal counsel during the CPCN Application proceedings and did not have the benefit of legal advice when reviewing the BCUC's March 9, 2012 decision regarding the CPCN Application. [Emphasis added.]

15. As indicated above, the DSD's admission on this point is a material one. The 2012 Decision, among other things, contradicts the DSD's view of the rate design, confirms the DSD's responsibility for the balance in the DDA, and dispels any notion that the BCUC was approving quantitiative performance requirements.

D. THE DSD'S SUMMARY OF ITS PROJECT DESIGN-RELATED EVIDENCE

16. The DSD summarizes its evidence on Project design starting at paragraph 65. We address the substance of the DSD's system design evidence (including Mr. Cleveland's and MCW's original reports) in Part Five below. At this juncture, we focus on the way in which the DSD Submission presents the DSD's Project design evidence in the "Facts" section.

(a) The DSD Is Now Presenting Mr. Poole's Affidavit as Expert Evidence, Despite Previously Advising to the Contrary

17. Mr. Poole's emails from 2013 are the very first evidence that the DSD cites in paragraph 65 to support of its contention that the system is improperly designed.[16] The DSD

[16] DSD Submission, para. 65.

also later characterizes the Affidavit of Mr. Poole as "corroborating" Mr. Cleveland's evidence.[17] The problems with the DSD's reliance on Mr. Poole are addressed in Part Six, Section C (d). In short, Mr. Poole's emails are (by the DSD's own admission) not expert evidence, and he had insufficient information to opine on the design in any event.

(b) The Description of MCW's Evidence Leaves Out its Endorsement of the Use of Energy Models and its Errors

18. MCW's endorsement of the use of energy modelling as "standard industry practice"[18], an approach which JCIC used when designing the system, is absent from paragraph 65. The DSD's summary of MCW's original report in the "Facts" section is also silent regarding the fact that MCW had based its analysis on the wrong information.[19] It is also silent regarding MCW's use of a methdology focussed exclusively on the system's peak capacity, when, by design, natural gas use would be at its highest.

(c) The DSD Has Overstated Mr. Cleveland's Thermal Energy Load Forecast Evidence

19. The DSD, in paragraph 65c, summarizes Mr. Cleveland's evidence on the load forecast variance. In doing so, it suggests that Mr. Cleveland had opined that the variance "can be attributed to two different errors", i.e., the DSD is implying that Mr. Cleveland definitively identified two errors. In fact, Mr. Cleveland was more equivocal. He identified two *possible* sources of the variance.[20]

- The first possible source was a mis-estimation of equipment efficiency due to data limitations understood by both parties. On this point, the DSD has omitted from its description Mr. Cleveland's concession that the approach used to

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[17] DSD Submission, paras. 133a, 135j.

[18] Exhibit C1-6, DSD Evidence, Report of MCW, pp. 5, 7.

[19] Exhibit B-7, FAES Rebuttal Evidence, pp. 32 – 33.

[20] Exhibit C1-6, Prepared Testimony of Will Cleveland, p. 10.

forecast load was "generally an appropriate approach for a project of this type".[21]

- Mr. Cleveland's second possible explanation for the variance involved the potential that the DSD has been supplying some of its own thermal energy. The DSD has omitted that this explanation, if it were correct (it is not), it would put the DSD in breach of contract.[22]

20. We address the flaws in Mr. Cleveland's analysis later.

(d) The DSD Presents "Project Cost" Evidence Only in Unit Costs

21. The DSD's description in paragraph 26 of the evidence on Project costs refers only to unit costs, not total dollars. This approach is convenient for the DSD in that the DSD can then avoid referencing the fact that the total Project cost was within the AACE Class 3 uncertainty parameters. However, FAES is unaware of any instance where the BCUC has used unit costs to compare a project completion cost to its initial estimate. The CPCN Guidelines require an AACE Class 3 estimate[23], which is presented in total dollars. The AACE Class 3 estimate is then the point of comparison for prudence reviews. This stands to reason because unit costs are influenced by load, and load changes have little to do with the reasonableness of project execution.[24]

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[21] Exhibit B-7, FAES Rebuttal Evidence, p. 24, quoting Mr. Cleveland: "This is generally an appropriate approach for a project of this type, but in my view FAES' accuracy is outside a reasonable range, and the magnitude of the errors suggest a reasonable participant could have made a more accurate forecast."

[22] RDA Section 3.2, Exclusivity.

[23] Exhibit B-3, FAES response to DSD IR 1.5.1.

[24] The Terasen Gas (Whistler) Inc. decision cited by the DSD in paragraph 127 is a good example of the exercise the BCUC goes through, comparing the cost in dollars to the estimate in dollars. There is no mention of unit costs anywhere in that decision, as one would expect.

PART THREE: THE DSD'S FRAMING OF THE ISSUES HAS CHANGED

22. The DSD's framing of the issues has changed from its position throughout the proceeding. One issue has been dropped, namely: "whether FAES is contractually permitted to apply to the Commission for approval to switch DSD from the MR to the COS Rate at this time."[25]

23. The DSD's original position had been, in effect, that FAES was estopped from even applying to the BCUC to switch to the COS Rate. It had characterized the RDA as having implied terms based on "certain representations", outlined in the evidence of Mr. Geyer, that preclude FAES from applying to the BCUC to switch to the COS Rate.[26] FAES pointed out the legal and factual flaws in that theory in the Initial Submission.[27] In its argument, the DSD now states that: "for the purposes of this proceeding, it acknowledges that the BCUC ultimately has the jurisdiction to determine whether to switch the DSD from the Market Rate to the COS Rate."[28] The DSD also states: "The RDA specifies the conditions that must be satisfied before FAES can apply to the BCUC for approval to switch the DSD to the COS Rate."[29]

24. FAES agrees with the DSD's formulation of the two issues in paragraph 72, except to the extent that the DSD intended the first issue to suggest that remaining on the MR indefinitely is an option. The issue is one of when, not if, the DSD should switch to the COS Rate.[30] A better formulation of the first issue would reflect more explicitly that the BCUC's inquiry is specific to "at this time". We address in Part Five why now is the time to switch to the COS Rate.

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[25] Exhibit C1-8, DSD Response to BCUC IR 1.1.4.

[26] Exhibit C1-8, DSD Response to BCUC IR 1.1.1.

[27] FAES Initial Submission, paras. 35 - 39.

[28] DSD Submission, para. 79.

[29] DSD Submission, para. 88.

[30] Exhibit B-1, p. 20, line 7.

PART FOUR:THE DSD'S POSITION ON BOTH ISSUES IS LEGALLY FLAWED

25. FAES relies on its Initial Submissions as to the applicable law, much of which was uncontradicted by the DSD.[31] In this Part, we focus on the inapplicability of (a) estoppel, and (b) implied quantitative performance targets, in the context of the UCA.

A. THE DSD'S ESTOPPEL ARGUMENT IS NOVEL AND UNTENABLE UNDER THE UCA

26. The DSD's case has, from the outset, relied on an estoppel argument; however, the nature of that argument has evolved. As we outlined in Part Three above, the DSD now appears to concede that FAES has met the conditions to bring an application to switch to the COS Rate. It argues, however, that the estoppel should prevail *in the BCUC's own analysis*:

> Accordingly, in the furtherance of its statutory mandate under ss.59-60 of the UCA, applied in light of the factual matrix in which the RDA was negotiated, executed, and approved, the BCUC should find <u>that FAES is estopped from obtaining an order</u> switching the DSD to COS Rate until the COS Rate is competitive with the Market Rate and provides benefits to the DSD in the form of low and/or less volatile rates, as the parties originally contemplated.[32] [Emphasis added.]

The DSD's revised estoppel argument is equally inapplicable in the context of the BCUC's role in setting public utility rates:

- First, the DSD has identified no legal or regulatory decision as authority for the proposition that estoppel is a proper consideration when the BCUC sets rates.

- Second, the DSD's apparent inability to identify supporting precedents in the public utility context is not at all surpising. The law of estoppel is superceded by

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[31] For example, FAES's Initial Submissions outlined the case law that makes the DSD's present budget constraints an invalid basis to deny recovery of costs or prevent FAES from being able to earn its BCUC-approved ROE. The DSD's Submission is silent on this point, never mentioning the *Hemlock Valley* case.

[32] DSD Submission, para. 82. See also para. 79, where the DSD "maintains that the BCUC should decline to grant such relief – in part, on the basis of the Representations – whether or not they constitute an implied term of the RDA. As set out below, the DSD maintains that, in any event, the Representations are relevant to the determination of whether the Proposed COS Rate is just and reasonable, and effectively operate as an estoppel that the BCUC should find collectively precludes FAES from being granted the relief that it seeks."

public utility legislation. Promissory estoppel is a legal principle that, by definition, exists outside of express contractual terms. The estoppel alleged by the DSD is collateral to the RDA. The notion of an estoppel is fundamentally at odds with requirements in the UCA that (i) rates must be in writing, (ii) rate schedules must be approved by the BCUC, and (ii) utilities must avoid the undue discrimination or preference that would result from departing from the approved terms.[33]

- Third, none of the cases cited by the DSD involved an agreement with Entire Agreement clause. The DSD has left unexplained why it would be reasonable for a sophisticated party with experienced legal counsel to rely on alleged prior representations after it had expressly agreed that any prior representations would not form part of the agreement.

27. In paragraph 81, the DSD seeks to equate the role of the BCUC in determining just and reasonable rates to the role of the labour arbitrator in *M.A.H.C.P v. Nor-Man Regional Health Authority Inc.*[34] It has stretched that decision far beyond its breaking point. The decision stands for the proposition that labour arbitrators are not required to follow equitable and common law principles including estoppel - i.e., they not required to apply estoppel *at all,* let alone apply the principles in the same way. Moreover, the passage of the decision quoted in paragraph 81 of the DSD Submission is clear that the statutory scheme and established principles are critical to determining the proper exercise of jurisdiction. This is where the DSD's argument fails. The applicable statute in this case, the UCA, has provisions on how utility rates must be specified and changed that preclude estoppel arguments.

28. The statutory scheme applicable in this case also incorporates the regulatory compact. The DSD pays lip-service to this fundamental principle of public utility law.[35]

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[33] This is discussed further in FAES's Initial Submission, paras. 35-39.

[34] DSD Submission, para. 81.

[35] DSD Submission, para. 75: "…the DSD agrees that there are two sides to the regulatory compact, as set out in the authorities cited therein".

However, it asserts that, in light of the "factual matrix", the "regulatory compact requires that FAES be denied the relief that it seeks in this proceeding".[36] The DSD's argument is untenable. The legal precedents cited in FAES's Initial Submissions[37] included decisions of (i) the Supreme Court of Canada, (ii) the BC Court of Appeal and (iii) the BCUC, all of which stand for the proposition that the obligation to provide a utility an opportunity to earn its allowed return is absolute. The DSD has made no attempt to distinguish those decisions. Nor has the DSD disputed the self-evident fact that remaining on the MR would make it impossible for FAES to earn its BCUC-approved ROE[38], and would likely preclude recovery of its invested capital as well.[39]

B. THE ALLEGED IMPLIED PERFORMANCE REQUIREMENTS ARE PRECLUDED BY THE UCA

29. The same statutory provisions that thwarted the DSD's initial attempt to imply additional conditions on when FAES can apply to the BCUC to move to the COS Rate also preclude implying the quantitative performance requirements alleged by the DSD. The obligations of FAES under the RDA - the terms and conditions of service (rates) - are expressed in the RDA. One of those terms is the Entire Agreement clause, which provides that there are no implied terms or understandings. The BCUC's 2012 Decision had even noted the absence of quantitative performance metrics in the written agreements.[40] In any event, we address in Part Six, Section D the factual flaws in the DSD's implied "objects" and other performance terms.

30. The DSD relies on what it refers to as the "factual matrix" to imply quantitative performance terms, despite the Entire Agreement clause. The case it cites in support of this proposition[41], which involved a non-regulated commercial contract, would not support the DSD's arguments even in the absence of the UCA requirement for terms and conditions of service to be written. The court (and the decisions cited by the court) was clear that the

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[36] DSD Submission, para. 75.

[37] See FAES Initial Submission, paras. 21, 22, 25, 26, 27, 30 & 32.

[38] See FAES Initial Submission, paras. 28 – 29, 151.

[39] See FAES Initial Submission, para. 134. The MR does not cover variable costs of fuel and O&M, let alone depreciation. See Exhibit B1-1, Appendix A, Schedule 2.

[40] 2012 Decision, p. 32.

[41] *King v. Operating Engineers Training Institute of Manitoba,* 2011 MBCA 80 (Tab 2, DSD Book of Authorities).

exercise of examining the "factual matrix" is aimed at producing an objectively reasonable interpretation of a contract. Evidence of the subjective intent of a party, evidence of negotiations and evidence of subsequent conduct – all of which play a prominent role in the DSD's "factual matrix" - are not considered.[42] The commercial context in the present case was that the parties were developing a cost of service rate structure, with a transitional rate. The industry custom (and the law) is for a utility to recover its prudent costs incurred in delivering an appropriate level of service, plus a regulated rate of return. The custom is **not** for utilities to permanently subsidize customers.

31. The absence of performance metrics with accompanying penalties for non-performance is a fundamental feature of cost of service regulation, a regime in which a particular level of service comes with an obligation on the customer to pay the prudently incurred costs associated with that level of service. This point is spelled out in the decision of the Nova Scotia Utilities and Rates Board that the DSD has included in its Book of Authorities (Tab 5) for another purpose:

> 19. In short, rates charged to customers are based on costs incurred by the Utility in providing service. If the Board finds certain costs to be imprudent or unreasonable, it can (and has) disallowed such expenditures and reduced proposed rate increases accordingly. The Board cannot, however, make rate decisions based solely on reliability issues or current public opinion of the Utility. There are appropriate sanctions a regulator can impose should a Utility be found to have an inadequate or unreliable system. <u>In many cases, it is likely such sanctions would involve higher expenditures, rather than reductions in costs. However, the practical reality in a regulated utility environment is that sanctions for service-related issues generally do not include a moratorium on rate increases.</u> [Emphasis added.]

[42] *King*, supra, at paras. 70-73.

PART FIVE: IT IS JUST AND REASONABLE TO MOVE TO THE COS RATE AT THIS TIME

32. The DSD's Introduction articulates five reasons for why it should remain on the MR.[43] In this section, FAES augments the Initial Submissions to explain why those reasons are invalid. It is organized around the following points:

- First, key facts that FAES outlined in the Initial Submissions in support of the reasonableness of changing to the COS Rate at this time are undisputed.
- Second, despite the DSD's argument to the contrary, keeping the DSD on the MR for the entire term of the RDA would violate the regulatory compact.
- Third, the alleged pre-contractual representations about when the DSD would switch to the COS Rate did not occur as alleged. In any event, the DSD was also relying on its own legal counsel for advice about the RDA.
- Fourth, merits aside, the DSD's allegations about system performance are unrelated to the issue of whether or not the DSD should remain on a "transitional" rate. The allegations relate to the quantification of the COS Rate.
- Fifth, the size of the rate change is an invalid basis for remaining indefinitely on what was approved as a "transitional" rate, particularly when the magnitude of the rate change is caused by the extent to which the DSD has been obtaining service for well below cost for the past five years.

A. KEY FACTS SUPPORTING THE REASONABLENESS OF CHANGING NOW ARE UNDISPUTED

33. The DSD either expressly concedes, indicates it does not oppose, or tacitly accepts key facts that FAES identified in Part Three of the Initial Submission as supporting the reasonableness of moving to the COS Rate. The DSD's position is, in essence, that the facts are

[43] DSD Submission, para. 2.

not determinative of whether it should switch to the COS Rate. FAES submits that the DSD's reasoning is flawed. The facts are not only relevant, but compelling.

(a) The DSD Does Not Dispute that the MR Was Approved as a "Transitional" Rate

34. FAES observed in its Initial Submissions that the BCUC-approved RDA established a cost of service rate regime, with the MR being what the BCUC had called a "transitional rate". The DSD has now been on that "transitional" rate for five years.[44] The DSD neither (a) disputes the length of time that the DSD has spent on the MR, nor (b) denies that the 2012 Decision had both characterized the MR as "transitional" and referred to FortisBC's expectation of a two to five year period.

35. The DSD instead argues that there is no "natural transition period". It says that the two to five year transition period was "the period during which FEI projected that the COS Rate would drop below the Market Rate". Since the MR turned out to be below the COS Rate, the DSD maintains that the two to five year period discussed in the 2012 CPCN Application proceeding and the 2012 Decision can no longer be described as a "natural transition period".[45] There are three responses to this argument.

36. First, contrary to what the DSD suggests, FortisBC had never said in 2012 that the natural transition period was two to five years "because this was the period during which FEI projected that the COS Rate would drop below the Market Rate."[46] FortisBC's 2012 evidence had been that there were multiple factors that suggested a natural transition period of two to five years. The reasons had related as much to stability as they did to the rate level - in the words of FAES from the 2012 CPCN Application, "low and/or less volatile rates" (see full quote later in this section).[47] The factors that FAES had believed would affect the volatility of the cost of service (construction, tax impacts, expansion of the rate pool) would have stabilized and

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[44] FAES Initial Submission, para. 41.

[45] DSD Submission, paras. 86 and 87.

[46] DSD Submission para. 87.

[47] CPCN Application pp 44-45.

been known within a five year period.[48] Each of these factors is now known, and the cost of service[49] and thermal energy demand[50] have now stabilized.

37. Second, the DSD has side-stepped FAES's overarching point, which is that the MR was approved as a "transitional" rate. At some point a "transitional" rate stops looking "transitional". A "transitional" rate, by definition, implies that the MR has a finite life, and that the COS Rate is the default rate structure. On the DSD's interpretation, by contrast, the MR is the primary rate and the COS Rate is just an option available to the DSD that provides an opportunity for a potential windfall.

38. Third, the BCUC, in its 2012 Decision, had articulated concerns about the DSD remaining on the MR that apply equally to the present circumstances. The BCUC had envisioned only a limited role for transitional rates: "Unless the actual need for the transitional rate is to overcome budgetary difficulties within a specific number of budget cycles, the Panel believes that transitional rates should not be necessary."[51] [Emphasis added.] The BCUC had also expressed reservations about the DSD remaining on the MR for too long, citing the need to recover the DDA balance from the DSD and concern regarding intergenerational inequity.[52] On these points, the DSD Submission is silent.

39. Fourth, the 2012 Application (which had predated both BCUC approval and final execution of the RDA) had foreshadowed the potential for the MR to be both above and below the true cost of service. For instance:

> Although there is no set time by which the SD must switch from the transitional "market rate" to the cost of service rate, the variance between the "market rate" and the true cost of service will be captured in the SD37 Deferral Account, and either recovered from, or returned to, the customer. It is not likely to be in the

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[48] Exhibit B-4, FAES Response to BCUC IR 1.1.1.

[49] FAES Submission, para. 48.

[50] Exhibit B-8, FAES Response on Rebuttal Evidence to DSD IR 1.2.6.

[51] See FAES Initial Submission, paras. 41 and 42.

[52] 2012 Decision, p. 59.

> customer's interest to remain on the "market rate" if it means accumulating significant balances that must be recovered down the road.[53] [Emphasis Added]

40. Fifth, the DSD's argument (that the anticipated transition period no longer applies because the MR turned out to be lower than the COS Rate) is predicated on an assumption that the MR was a way for the DSD to speculate on how largely uncontrollable factors (e.g., natural gas prices) would unfold. The DSD and FAES both gave evidence in the 2012 proceeding that the MR was "intended to (sic) the transition, not provide a market speculation mechanism." In fact, the DSD had assured the BCUC that this intention had "been discussed during agreement negotiations and [was] well understood by Delta SD."[54] The DSD Submission is also silent on this point.

41. Sixth, as FAES observed in the Initial Submission, the DSD was still citing the two to five year transition period as late as 2015.[55] This was long after it became apparent that the MR was below the COS Rate. On this point, the DSD Submission was again silent.

(b) The DSD Concedes that FAES Has Met the Express Conditions to Trigger a Changeover

42. In paragraphs 44 to 47 of the Initial Submission, FAES explained that the BCUC-approved RDA expressly provides that FAES can apply to the BCUC to change from the MR to the COS Rate upon satisfying three conditions, which FAES has met. The DSD's original position had been that there is an additional "implied term" or "collateral representation" that FAES can only trigger the change if it is in the DSD's interest to move to the Cost of Service Rate.[56] However, the DSD now appears to have abandoned that argument. It states at paragraph 88:

> The RDA specifies the conditions that must be satisfied before FAES can apply to the BCUC for approval to switch the DSD to the COS Rate. However, the RDA is silent regarding the basis upon which the BCUC may grant such relief. Accordingly, it is not open to FAES to argue that FAES has met the express conditions to actually trigger a switch to the COS Rate. [Emphasis added.]

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[53] CPCN Application pp. 44-45, included in the Affidavit #1 of Frank Geyer.

[54] FAES Initial Submission, para. 92.

[55] FAES Initial Submission, para. 132.

[56] Exhibit C1-6, DSD Evidence, Affidavit #1 of Frank Geyer, paras. 27-32, 61, 69.

The BCUC should find as a fact that FAES has met the requirements of the RDA for requesting to move to the COS Rate.

43. We also note that the last sentence of the DSD's quote above mischaracterizes FAES's position. FAES's position has consistently been that it has met the conditions *to apply to the BCUC to seek a change to the COS Rate* - a point which the DSD now appears to have conceded. On application by FAES, the BCUC has discretion to consider a number of factors in determining whether switching to the COS Rate at this time is just and reasonable. The bounds of that discretion are defined by the cases included in FAES's Initial Submission, including those defining a utility's absolute right to an opportunity to earn the BCUC-approved return.

(c) The DSD "Takes No Position" on Stability of Operations, Certainty on Number of Schools, and Clarity on Tax Impacts

44. FAES made the point starting at paragraph 48 of its Initial Submissions that operations have stabilized, the final number of schools included is known, and tax impacts are understood. These factors mean that the total cost of service will be more predicable going forward. The DSD responds in paragraph 89 by saying: "The DSD takes no position on FAES' position that operations have stabilized, that the final number of schools served by the Project is known, or that the tax impacts of the Project are understood. However, it respectfully submits that these factors alone do not warrant a switch the Proposed COS Rate." While the DSD would prefer to "take no position" on these facts, it has not offered any basis to dispute them. The BCUC should find as a fact that the total cost of service will be more predictable going forwards as a result of these developments.

45. Why is this important? FAES had been clear in the 2012 proceeding that transitioning to the COS Rate was expected to provide benefits to the SD in the form of "low and/or less volatile rates".[57] The operations have now stabilized.[58] The only source of volatility at this time is the need to begin recovering the costs deferred to the DDA as a result of the DSD paying far less than the cost of service for the past five years. FAES submits that these facts

[57] CPCN Application page 45.

[58] FAES Argument para. 48.

should be given weight by the BCUC in determining whether now is the appropriate time to switch to the COS Rate. This is a particularly compelling point when, as described next, operations have stabilized at a lower cost of service than had originally been forecasted.[59]

(d) The DSD Concedes that Costs Have Been, and Remain, Below Original Forecasts

46. FAES pointed out in paragraph 49 of the Initial Submission that (1) FAES's costs have been $950 thousand less over the past five years than had originally been forecast in 2012, and (2) the cost of service in the 2018 rate year, before DDA amortization, remains lower than the original forecast. The DSD admits that the current total cost of service "is not significantly different from" the forecasted cost of service. However, the DSD makes a legal argument that this fact "should have no bearing on the BCUC's decision as to whether the DSD should be switched to the Proposed COS Rate".[60] This legal argument is untenable, for the reasons outlined below.

The Cost of Service is Relevant in Cost of Service Ratemaking

47. The DSD's legal argument is that the BCUC is charged under the UCA with regulating rates (which it seems to interpret as unit prices), not with determining whether the total cost of service is reasonable.[61] The first answer to the DSD's argument is that the definition of what constitutes a "rate" under the UCA is much broader than simply a unit price. For instance, the BCUC routinely relies on the rate setting sections (sections 59 to 61) as the authority for approval of deferral accounts / account amortization periods and depreciation rates for capital because they influence the amount recovered from customers.

48. Second, in seeking to draw a bright line distinction between total cost of service and rates, the DSD is overlooking the fact that the RDA is a cost of service rate regime. Not only is total cost of service "relevant" to cost of service ratemaking, it is the central focus of all cost of service rate setting (hence the term "*cost of service* ratemaking"). Under a cost of service rate regime, the rates that the regulator approves for the upcoming year flow from its

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[59] FAES Argument para. 49.

[60] DSD Argument, para. 90.

[61] DSD Submission, para. 91, footnote 82. See also paras. 90, 95 and 96.

determination of the total forecast costs required to provide an appropriate level of service to customers. That is why annual general rate applications, including this Application, are called "revenue requirements applications". The utility's total cost of service is the revenue requirements.

49. The DSD is fixated on unit prices (dollars per kW/h), and the impact of load on those unit prices. As FAES has explained, dividing the total revenue requirements into unit costs had no effect on the cost of service. The only practical impact that the load forecast variance has had (apart from reducing the MR and fuel costs to the benefit of the DSD for the past five years) was to change the timing of when the total revenue requirements is collected from the DSD within the year.

50. The issue of how a utility's total revenue requirements is collected, i.e., the billing determinants that determine when costs are collected and from whom, is a matter of rate design. A fundamental principle of rate design under cost of service regulation is that the full forecast revenue requirements - the forecast total (reasonable) cost of service - is recoverable from customers. The DSD has always been the only customer, and it is responsible under cost of service ratemaking for the full revenue requirements that the BCUC finds are reasonable for the nature of the service provided.

51. The BCUC had explicitly recognized the distinction between responsibility for costs and the setting of a pooled unit rate in the 2012 Decision.[62]

52. There is no evidence that the DSD has a problem with how the use of load as a billing determinant affects the distribution of billing throughout the year.[63]

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[62] 2012 Decision, p. 48: "The pooled rate is essentially an administrative or value-added project design service, which FEI has provided to Delta SD. The Delta SD, as it is responsible for budgeting across the district, could have made similar trade-offs between school sites within its standard budgetary practices."

[63] If it did have a concern, that was something that could potentially have been negotiated and submitted to the BCUC as an amendment to the RDA. However, it still would not have absolved the DSD from paying for the service it is receiving over the RDA term.

The Unit Costs Have No Practical Implications for the DSD's Budgeting

53. The DSD's focus on unit costs is convenient for them because it fits their narrative. However, the DSD has not provided any evidence that a difference in the unit rate poses any problem at all for its budgeting. The evidence is, in fact, to the contrary:

- Since the DSD is the only customer, the dollar per kW/h conversion for energy costs only affects the distribution of billing of the COS Rate throughout the year. The DSD's budget is set annually, not monthly.[64]
- The DSD's annual budget is expressed in dollars, not dollars per kW/h.
- In the pre-hearing conference in this proceeding, the DSD spoke of its budget challenges in total dollars, not dollars per kW/h.[65]
- The DSD is internally inconsistent on this point. When the DSD alleges (incorrectly) that FAES had promised specific savings annually and over the life of the RDA, it is claiming those representations were made with respect to absolute dollars, not based on unit costs measured in dollars per kW/h.[66]

The DSD's System Design Arguments Are Logically Unrelated to this Issue

54. The DSD's second argument in support of its contention that the comparison to the expected total cost of service is irrelevant is that there are system design problems. FAES addresses the substance of these design arguments, which are without merit, in Part Six,

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[64] 2012 Decision, pp. 51-52 refers to the DSD's "strict annual operating budget constraints".

[65] Transcript V.1 pp.27-29: "Thirdly, I would say that – and this is a fact which should inform and which colors this entire proceeding, it seems to me – should FAES be granted the relief that it's seeking, the impact on my client's financial position is going to be very significant. As you may be – as the panel may be aware, school boards are legislatively prohibited from running deficits year to year. So the estimated $1 million in additional costs that will result from a switch to the cost of service rate at this time is going to have to come out of the program budget by which the district operates its schools."

[66] DSD Submission, para. 99. One of the "objects" alleged is "reduce the DSD's annual operating and capital costs by $188,000", a sum expressed in dollars not dollars per kW/h. FAES discusses later in this Reply Submission how the DSD has misquoted a document.

Section C. System design issues are logically related to the determination of the COS Rate, not the question of whether the DSD should remain on the "transitional" rate.

Falling Gas Prices Are Only Part of the Reason for the Strong Cost Performance

55. The DSD also seems to suggest that the lower than expected cost of service is attributable to falling gas prices alone, which is incorrect.[67] The following table has been prepared entirely from data included in Mr. Cleveland's evidence. The table shows that, even excluding fuel costs, the cost of service has still been lower than expected since stable operation was achieved in April 2015.[68]

	2015/16	2016/17	2017/18	2018/19	EXHIBIT C1-6 ATTACHMENT 1
A - Original Projection – without DDA Amortization	1,139	1,267	1,320	1,491	Tab 1, Line 14 minus Tab 1, Line 11
B - Remove Original Gas Cost	-124	-132	-141	-148	Tab 1, Line 6
C - Remove Original Electric Cost	-234	-240	-247	-254	Tab 1, Line 7
D - Original Projection – without DDA Amortization and Fuel Costs	**826**	**895**	**932**	**1,089**	**SUM (A:C)**
E - Actuals – without **DDA Amortization**	1,097	1,153	1,071	1,114	Tab 2, Line 17
F - Remove Actual Gas Cost	-247	-235	-252	-244	Tab 2, Line 7
G - Remove Actual Electricity	-26	-33	-32	-31	Tab 2, Line 8
H - Actuals – without DDA Amortization and Fuel Costs	**824**	**885**	**787**	**839**	**SUM (E:F)**
I – Actual vs. Original Projection – without DDA Amortization	**92.6%**	**91.0%**	**81.2%**	**74.7%**	**E/A**
J – Actual vs. Original Projection – without DDA Amortization and Fuel Costs	**99.7%**	**98.9%**	**84.5%**	**77.1%**	**H/D**

The comparison is even more favourable when fuel cost savings are properly considered as shown in Line I above.

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[67] DSD Submission, paras 92-94. The DSD's third note in paragraph 98 is that "c. the price of natural gas has declined significantly relative to projected prices at the time of the CPCN Application proceedings. For example, 2019 prices are 41% lower than was forecast at the time of the CPCN Application proceedings."

[68] Exhibit B-8 FAES Response to DSD IR 1.2.6 on FAES Rebuttal Evidence.

It is Harder to Absolve the DSD for its Budgeting Practices When the DSD Will Pay Less than It Expected to Pay

56. The comparison of forecast to current total cost of service demonstrates that the DSD will pay less than it had expected to pay as compared to when it entered into the RDA. The total cost of service is less than expected *despite the fact that FAES is carrying additional equipment costs for the DSD that are not included in the FAES service any more*.[69] This evidence is relevant to the question of when the DSD should switch.

57. The matter of what the DSD should have expected to budget for the service at this point in time had been identified in the 2012 CPCN Application proceeding as a factor that the DSD should consider before electing to switch.[70] The DSD has also argued in the current proceeding that changing to the COS Rate would cause it hardship.[71] The fact that the cost of service is below what was forecasted for this point in time speaks to the fact that the DSD must take responsibility for budgetary challenges it is now facing. The DSD has control over its own budgetary processes and possessed the information necessary to budget for this service.

(e) The DSD Concedes that Total Cost of Service Is Similar to What the DSD Would Have Paid in Heating Costs Under Business As Usual *Even Before* Considering the DSD's Avoided Capital Costs

58. FAES pointed out in paragraphs 52 to 57 of its Initial Submission that changing to the COS Rate still leaves the DSD considerably better off than it would have been without the service. The FAES service came with a new thermal energy system, which meant the DSD avoided investing significant capital. The cost of the FAES system provides an indication of the magnitude of the DSD's avoided investment. And yet, even without considering the DSD's avoided capital costs, the Annual Cost of Service is very close to the Business As Usual cost it had expected to pay at this time on an inflation-adjusted basis.[72] The DSD does not dispute

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[69] Exhibit B-7, p. 25.

[70] CPCN Application Exhibit C1-2, DSD Response to BCUC IR 1.20.1.

[71] Transcript V.1 pp. 27-29.

[72] Exhibit B-7, FAES Rebuttal Evidence, page 41.

these facts. Instead, the DSD argues that the facts are irrelevant, giving four reasons that we answer below.

The DSD's Legal and System Design Arguments Are Similarly Misguided in this Context

59. The DSD's primary relevance argument[73] is that the focus should be on unit costs, which are higher than anticipated by virtue of lower than anticipated load.[74] It argues, once again, that the BCUC is required to look at unit rates under the UCA, not costs of service. We have addressed the fallacy of that legal argument in Section A (d) above.

60. The DSD also repeats the same system design and gas price arguments that it makes in arguing that the lower than expected total cost of service is irrelevant.[75] FAES addresses the substance of these design arguments, which are without merit, in Part Six, Section C.

The DSD Is Incorrectly Paraphrasing the Total Savings Discussion

61. The DSD's third and final argument is set out in full below, because it is incorrectly portraying FortisBC's pre-contractual statements. The error is underlined:

> Finally, the DSD agreed to undertake the Project on the understanding that, as promised by FEI, the Project would reduce the BAU Total Cost of Service by $188,000 during <u>each year of the Project, such that the DSD would save $3,760,000 over the life of the Project ($1,860,000 or 97.89% more than FAES is now saying the DSD will save over the life of the Project)</u>. The fact that the Project is performing poorly with respect to the original forecasts, and will save the DSD far less than FEI promised it would, militates against switching DSD to the Proposed COS Rate.[76] [Emphasis added.]

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[73] DSD Submission, para. 97.

[74] DSD Submission, paras. 97, 98.

[75] DSD Submission, paras 97-99.

[76] DSD Submission, para. 99.

FortisBC never stated that it "would reduce the BAU Total Cost of Service by $188,000 during each year of the Project, such that the DSD would save $3,760,000 over the life of the Project." [Emphasis Added]

62. The DSD cites the "Revised Feasibility Assessment" from around October 10, 2010 as support for this claim.[77] However, the document actually says:

> "Calculated annual energy savings of over $180,000 in the first year after completion"

There is no reference in the document at all to projected total savings over the 20 year term. The DSD has calculated that amount by extrapolation from an estimate that is explicitly only relevant to the first year. The document is also explicit that all figures presented in it are "estimates only" (it predated the detailed design).

(f) The DSD Concedes that, if a Switch Must Occur, it is in the DSD's Best Interest for the Switch to Occur Now

63. FAES's evidence is that delaying the changeover by three, five or even 10 years would result in the DSD paying a much higher Annual Cost of Service (i.e., revenue requirement), experiencing a more significant increase in total thermal energy costs in the year of the changeover, and paying more in total over the RDA term.[78] The DSD admits that delaying the switch would not be in its interests:

> The DSD does not dispute that, assuming the DSD is switched to the Proposed COS Rate, delaying the switch to the COS Rate by three, five or ten years will cause the DSD to pay a higher COS Rate and that doing so would not be in the DSD's best interests.[79]

In other words, the DSD's case rests on the BCUC accepting the premise that the DSD should never have to switch to the COS Rate at all. This argument is addressed next.

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[77] The reference to Mr. Geyer's affidavit is further referenced to the actual "revised Feasibility Assessment" report that Mr. Geyer included as "Exhibit D" to his affidavit from Exhibit C1-6 of this proceeding.

[78] Exhibit B-7, FAES Rebuttal Evidence, p. 42.

[79] DSD Submission, para. 100. See also para. 105.

B. KEEPING THE DSD ON THE MR FOR THE ENTIRE TERM WOULD VIOLATE THE REGULATORY COMPACT

64. The DSD argues, starting at paragraph 100, that the regulatory compact is respected if the DSD remains on the transitional MR permanently because "the RDA contemplates a scenario where the DSD is switched to the COS Rate after 10 years, and FAES cannot recover the full balance in the DDA from the DSD."[80] Reaching that conclusion requires a long leap in logic, and overlooking the fact that the parties agreed to, and the BCUC approved, a cost of service regime.

(a) Legitimate Shareholder Risk Under COS Regulation Excludes the Risk that the Regulator Will Actively Work to Deny Prudent Cost Recovery

65. Shareholders bear residual risk in all cost of service ratemaking - the risk of stranded assets, including regulatory account balances, when the utility winds-up. This RDA framework, as designed, operates the same way. There is a finite term of 20 years, with the potential for a wind-up. At that point, the shareholder is at risk for stranding of the physical assets and the DDA balance, subject to the Expiry provisions of the RDA that give the DSD an opportunity to buy those assets rather than install new assets. The shareholder's residual risk under cost of service regulation generally, or the RDA specifically, would be an invalid reason under public utility law for a regulator to set rates at a level that is below what is necessary to permit full recovery of prudent costs plus the allowed ROE.

66. The DSD's argument is no different in its spirit and effect from a hypothetical argument that the regulator should set depreciation rates so low (i.e., a depreciation period so long) that a utility is likely to go out of business before ever being able to collect. The regulatory compact requires that rates include reasonable amortization of regulatory account balances, just as it requires the rates to include reasonable depreciation expense on capital assets. Put simply, the regulatory compact requires that rates be set to allow an opportunity to earn both a return <u>on</u> utility investment, and the return <u>of</u> the original book value investment through inclusion of amortization and depreciation expense in rates.

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[80] DSD Submission, para. 101.

(b) There Were Scenarios Where a Switch Could Have Occured Late in the Term and Still Have Met the Regulatory Compact - this Is Not One of Them

67. Standing in the shoes of the Parties in 2011 and 2012, there were scenarios where a switch to the COS Rate could have occurred late in the RDA term and still have respected the regulatory compact. In particular, new customers might have been added. This circumstance is different.

68. The DSD does not dispute FAES's evidence regarding the size and growth rate of the deferral account balance.[81] It also does not appear to dispute that, given the gas price forecasts, and the thermal energy demand[82], the transitional MR will now remain below the COS Rate for the remainder of the initial term.[83] In other words, we now know that, unless the DSD is moved to the COS Rate in short order, (a) the DDA balance will grow, (b) millions of dollars will remain unrecovered, and (c) the DSD will enjoy subsidized service for the duration of the term. With this knowledge, it would be contrary to the regulatory compact to keep the DSD on the transitional MR into the latter half of the RDA term.[84] And, if the switch must occur, the DSD concedes that it is in its best interests to switch now.[85]

C. RESPONSE TO THE PRE-2012 "FACTUAL MATRIX" AND EMAIL "REPRESENTATIONS"

69. The DSD argues that the BCUC's decision as to whether to move the DSD from the MR to the COS Rate at this time should turn on the "factual matrix" prior to the 2012 CPCN Application[86], rather than the circumstances that exist today. The DSD's "factual matrix" argument is premised in large part on three alleged "representations" in emails exchanged during negotiations in 2011. It characterized the alleged representations as follows in paragraph 77:

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[81] FAES Initial Submission, para. 60.

[82] Application, p. 16: "Further, given that the forecast variance in thermal demand is embedded into the initial MR and is not adjusted in subsequent calcualtions of the MR, it becomes a systemic bias towards lower revenues when the DSD is paying the MR."

[83] FAES Initial Submission, para. 59.

[84] FAES Initial Submission, paras. 67 and 69.

[85] DSD Submission, para. 105.

[86] DSD Submission, para. 76.

> 77. Taken together, the evidence adduced by DSD in paragraphs 31 to 33 of these submissions [i.e., the email correspondence] confirms that between May and September of 2011, FEI/FAES represented to the DSD that:
>
> a. FEI expected the COS Rate to be lower than the Market Rate and to provide benefits to the DSD in the form of low and/or less volatile rates;
>
> b. the rate structure in the RDA would give the DSD the opportunity to ensure that the COS Rate was "in line with expectations" before the DSD would be switched to the COS Rate; and
>
> c. BCUC approval would be required to switch the DSD from the Market Rate to the COS Rate and FEI would need to present a compelling argument that switching the DSD to the COS Rate was in the DSD's interests before the DSD would be switched;
>
> (collectively, the "Representations").

70. FAES has already addressed in the Initial Submission and in Part Four above, the legal shortcomings of the DSD's estoppel argument. We respond to the factual substance of these three alleged representations below.

(a) Alleged Representation 1: FAES Expected that the COS Rate Would Be Lower than the MR

71. There are three problems with the DSD's first alleged "representation".[87]

The Evidence in the 2012 CPCN Process Contemplated the Potential for the MR to Be Both Higher and Lower than the COS Rate

72. We have addressed this point in Part Five, Section A (a) above.

The MR Was Dependent on Gas Prices, Which Were Beyond Anyone's Control

73. The second problem is that, even on the DSD's own argument, FAES was only ever expressing an "expectation" about future events over which no one had control. The relative position of the MR and the COS Rate was determined, in part, by natural gas prices. (The MR was tied to gas prices, and declined when gas prices fell.) In regulatory processes,

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[87] DSD Submission, para. 77.

utilities are regularly called upon to provide forecasts of, or their opinion about, uncertain future outcomes. The idea that a utility should be held responsible to customers for failing to accurately predict future commodity prices is a novel one. The DSD would have been, or at least certainly ought to have been, aware that FortisBC had no control over natural gas markets. This logical failing is only compounded by the fact that the DSD in this case wants to punish FAES for the fact that falling gas prices have resulted in the DSD paying <u>much less</u> for service than anticipated.

The COS Rate Will Deliver Lower Volatility

74. It will be noted that, even as phrased by the DSD, the alleged representation is "low and/**or** <u>less volatile</u> rates" – "or", not "and".[88] FortisBC's evidence in 2012, which the BCUC had noted in the 2012 Decision, had been that it expected the initial cost of service to be volatile and artificially low due to expected temporary effects of construction, tax treatments and expansion efforts.[89] These issues are resolved.[90]

(b) Alleged Representation 2: Remain on MR Until the COS Rate Was in Line With Expectations

75. The second alleged representation is as follows: "b. the rate structure in the RDA would give the DSD the opportunity to ensure that the COS Rate was 'in line with expectations' before the DSD would be switched to the COS Rate".[91] This alleged representation never occurred.

76. The DSD has not footnoted its reference to "in line with expectations", but to FAES's knowledge that phrase only appeared once in the documentary record. The phrase did not, as the DSD suggests, relate to the "COS Rate", but rather the "costs". The statement that FortisBC had actually made was:

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[88] This language is from the CPCN evidence that is quoted in Part Four, Section A above.

[89] Exhibit B-4, FAES Response to BCUC IR 1.1.1; 2012 Decision, p. 53.

[90] Exhibit B-4, FAES Response to BCUC IR 1.1.1.

[91] DSD Final Argument p. 37, para. 77(b)

> As of now, we all want to get to Cost of Service, but you need proof that it will be beneficial, which is what the market rate gives you so that you can get some comfort that COS is going to be reasonable before switching. We would go straight to COS, but this way, with the market rate, you have the chance to watch and ensure that **the costs** are in line with expectations first. [Underlining and bold added.][92]

The evidence is that the costs are in line with the original forecast costs. In fact, Mr. Cleveland has confirmed that the costs are actually well below the original projections.[93]

77. The context of the above correspondence was that FortisBC had been expecting the construction and commissioning period, tax implications and potential expansion of the pool to impact costs in the short-term. These factors are what drove FortisBC to anticipate a two to five year transition.[94] FortisBC's expectations turned out to be correct; all of these issues did resolve within five years and the costs are stable now.

(c) Alleged Representation 3: Best Interests / BCUC Approval Necessary

78. The DSD's third alleged representation was: "BCUC approval would be required to switch the DSD from the Market Rate to the COS Rate and FEI would need to present a compelling argument that switching the DSD to the COS Rate was in the DSD's interests before the DSD would be switched."[95] The answer to this argument is:

- BCUC approval is necessary if FAES applied to the BCUC to switch to the COS Rate.
- The just and reasonable standard does require an examination of the customer's interests, among other things.
- The DSD is interpreting "best interests" in a way that is divorced from context. FortisBC had stated in the 2012 CPCN Application, to the knowledge of the DSD,

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92 Exhibit B-7, p. 13.

93 FAES Argument para. 155 and Table 2 (Restated) Cost of Service: Original Projections vs. Actuals.

94 Exhibit B-4, FAES Response to BCUC IR 1.1.1; 2012 Decision, p. 53.

95 DSD Submission, para. 77.

that "It is not likely to be in the customer's interest to remain on the 'market rate' if it means accumulating significant balances that must be recovered down the road."[96] FortisBC had repeated this point in its 2012 Final Submission: "It is in the interests of the DSD to switch to the cost of service rate as soon as possible because it is ultimately less expensive for the customer."[97] These statements are fundamentally incompatible with the DSD's theory that they would only have to switch if there was a credit balance in the DDA to be flowed back to them to offset the total cost of service.

- The BCUC, like FAES, had the long-term best interests of the DSD in mind. The 2012 Decision said: "The Panel has serious concerns about the possible deferred cost implications for future Delta School Boards."[98] And: "Significant transfers to future years through the DDA would raise "issues of intergenerational equity".[99]

- FAES's current Application and evidence makes a compelling case that switching to the COS Rate is in the best interests of the DSD, when "best interests" is interpreted in a reasonable manner consistent with the context. As noted above, even the DSD does not dispute that, if the DSD must switch, then a delay is not in their "best interests".[100]

79. In short, the current circumstances are exactly what FAES, the DSD and the BCUC had envisioned in 2012 as being a circumstance where the switch should occur.

(d) The 2015 Email Regarding the COS Rate "Dropping at or Below the MR"

80. In paragraph 78, the DSD extends the "best interests" argument one step further to something more concrete: "that it would not be switched to the COS Rate unless or until the

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[96] CPCN Application, p. 44.

[97] CPCN Application, FAES Final Argument, para. 67.

[98] 2012 Decision, p. 53.

[99] 2012 Decision, pp. 59-60.

[100] DSD Argument para. 100.

COS Rate dropped at or below the Market Rate". There is a factual problem and a legal problem with this argument.

The DSD's Factual Problem

81. First, the factual problem: The email referenced by the DSD from May 2015 does not say "that [the DSD] would not be switched to the COS Rate unless or until the COS Rate dropped at or below the Market Rate". Here is the email exchange (unedited):

> **Geyer (DSD):** "I re-read the RDA and am still under the belief that as long as we stay on the market rate (indexed), the deferral account will not be a factor to to [sic] the District. Once the COS rate drops at or below the Market Rate and we elect to change, only then would the deferral account affect the District (as part of the COS rate in the form of an amount necessary to amortize the deferral account balance).
>
> Please tell me that I'm correct and that I didn't get duped…"
>
> **Beirlmeier (FortisBC)**: "Your understanding is absolutely correct Frank. You pay the market rate until you elect to switch to the COS rate exactly as you describe below."

82. A close examination of this exchange shows Mr. Geyer presenting a scenario, in which "the COS rate drops at or below the Market Rate and we [the DSD] elect to change". In Mr. Geyer's scenario, Mr. Beirlmeier's confirmation was correct; the DSD would "pay the market rate until you elect to switch to the COS rate". One problem with the DSD's argument is that there was nothing in Mr. Geyer's email to prompt Mr. Beirlmeier to identify every other conceivable scenario that might result in the switch to the COS Rate occurring. FAES had a right to apply for the switch too. Moreover, in every scenario, it would only be once the transition to the COS Rate occurs that the deferral account would "affect the District (as part of the COS rate in the form of an amount necessary to amortize the deferral account balance)".

83. In any event, it would have required unreasonable tunnel vision for the DSD to conclude that it was immune from the DDA balance unless it decided it wanted to pay, given the surrounding circumstances and other contemporaneous documents. FAES has identified in

paragraphs 130-143 of the Initial Submissions a variety of documents that contradict the inference that the DSD is now trying to draw from the above email exchange. The mere fact that FAES had insisted on a unilateral right to apply to switch to the COS Rate speaks volumes - FAES would not have needed the right to apply if the COS Rate remained below the MR because, in that case, the DSD would have initiated the switch on its own.[101]

The DSD's Legal Problem

84. The legal flaw in the DSD's argument is that it is based on an email from three years after the RDA was signed. It could not have had any impact on the DSD's decision to enter into the RDA. The DSD has not identified any instance where FortisBC had stated, prior to entering into the RDA, "that [the DSD] would not be switched to the COS Rate unless or until the COS Rate dropped at or below the Market Rate". Had the Parties intended to limit FAES' ability to switch to the COS Rate unless the COS Rate dropped at or below the MR, they could have instructed their respective lawyers to draft the RDA that way.

(e) Reliance, Let Alone Reasonable Reliance, Is Absent in Any Event

85. Let's assume, just for the sake of argument, that the estoppel doctrine is a legally valid consideration in rate-setting and FortisBC had made representations. The DSD would still have to demontrate that it relied on the alleged representation. The DSD seeks to demonstrate reliance by portraying itself as an unsophisticated party without legal counsel, and by pointing to its requests for FAES to assist it during the CPCN proceeding. The problem with the DSD's reliance argument is that it is an exercise in revisionism, and any reliance would have been unreasonable in any event.

86. The DSD does not dispute that it had legal counsel when negotiating the RDA.[102] Rather, the DSD focuses on the fact that it did not retain legal counsel during the 2012 CPCN Application proceeding, or to review the 2012 CPCN Decision. It makes this argument

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[101] Exhibit C1-6, page 164, September 12, 2011 8:53 AM email from G. Bierlmeier. to F. Geyer. Mr. Bierlmeier pointed this out to Mr. Geyer in email correspondence, which Mr. Geyer acknowledged.

[102] DSD Submission, para. 107.

repeatedly.[103] The logical flaw in the DSD's focus on legal representation during the CPCN process and after the 2012 CPCN Decision is that these events occurred after the RDA had been negotiated by the DSD with the involvement of legal counsel. The provisions about which the DSD complains were determined before the CPCN process, not during or after the CPCN process. It was during those negotiations that the DSD, among other things, determined that it wanted a cost of service rate structure, agreed to an Entire Agreement clause, and forewent quantitative performance targets on GHGs or heat pump use.

87. The BCUC, in its 2012 CPCN Decision, had highlighted the cost of service rate structure and the absence of quantitative peformance metrics. The DSD read the 2012 Decision before agreeing to proceed.[104]

88. FAES never discouraged the DSD from obtaining legal advice. In fact, the opposite is true. The DSD did seek FortisBC's advice during the 2012 CPCN Application proceeding, i.e., only after the RDA was negotiated, about whether it needed a lawyer for the proceeding. In both instances, FortisBC sent the DSD away to make its own decisions.

89. The 2012 proceeding record was full of evidence about how the RDA worked, all of which was consistent with what FAES is saying today.[105] The BCUC's 2012 Decision, which the DSD read, then gave the DSD a second opportunity to consider the rate design. The 2012 Decision encouraged the DSD to reconsider some aspects of the Agreement. The fact that, after reading the 2012 Decision, it did not call its lawyer and seek to renegoatiate any aspect of the RDA speaks volumes as to its level of comfort with the RDA as written.

90. The DSD, at a minimum, demonstrated it had the understanding and sophistication to know that legal advice was available. At some point, the DSD has to take responsibility for its own decisions.

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[103] DSD Submission, paras. 107, 108 and 27.

[104] DSD Submission, para. 107.

[105] See FAES Initial Submission, paras. 94 - 99

(f) The Objective Unreasonableness of the DSD's Interpretation of the RDA Makes its Position All the More Unreasonable

91. The DSD has provided no plausible explanation for why FAES would have entered into an Agreement as one-sided as the DSD is alleging.

D. SYSTEM PERFORMANCE IS UNRELATED TO WHETHER THE DSD SHOULD REMAIN ON THE MR

92. Two of the DSD's five reasons for why it should remain on the MR relate to system performance.[106] FAES submits that the evidence does not support these two allegations. In any event, allegations related to system performance would relate to the determination of the COS Rate, not the question of whether the DSD should remain on the MR. The MR is a "transitional rate" that is tied to commodity prices. It is, by design, delinked from costs. The DSD has made no attempt to correlate the amount of the MR with the cost associated with the system performance issues it alleges. FAES has thus responded to the DSD's system performance arguments in Part Six of this Reply Submission.

93. The DSD's attempt to justify remaining on the MR by referencing system performance allegations fails to heed the commentary in the Nova Scotia Utility and Rates Board decision cited by the DSD that "in a regulated utility environment…sanctions for service-related issues generally do not include a moratorium on rate increases."

E. THE DSD'S "RATE SHOCK" ARGUMENT IS PERVERSE AND CONTRARY TO LAW

94. In paragraph 66e, the DSD argues that changing to the COS Rate "will result in the very 'rate shock' that the Project was intended to avoid." The fact that the cost of service is now in line with expectations that were set out at least as far back as 2011, precludes the change from being a "shock" to the DSD. It would be a perverse result indeed if the fact that the DSD was paying artificially low rates and got used to it were to be used as a justification for

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[106] See DSD Submission, para. 2. Specifically, the DSD maintains that the Project is delivering less thermal energy than it says FAES had promised, and the capital intensive heat pump components are of the Project in particular are delivering less thermal energy "than FEI promised they would". It also argues that the Project has lowered the DSD's GHG emissions by less than "FEI promised".

harming the future DSD boards and taxpayers or requiring FAES to subsidize its service indefinitely.

95. It would also be an unlawful approach. The *Hemlock Valley* case, to which the DSD made no reference, holds that the solution to address the magnitude of rate changes is to transition the rate change. The B.C. Court of Appeal was unequivocal that denying cost recovery - in this case by keeping the the DSD on the MR for the whole term - is not a lawful option.[107]

[107] See FAES Initial Submission, para. 30.

PART SIX: FAES'S PROPOSED COST OF SERVICE RATE IS JUST AND REASONABLE

96. Part Five of this Reply Submission addresses the DSD's arguments about the quantification of the COS Rate, and its request for a prudence review of capital costs. It is organized around the following points:

- First, significant components of the total cost of service are undisputed, with the DSD's focus being on capital costs.
- Second, a capital cost variance that is well within the estimating margin specified by the BCUC's CPCN Guidelines is insufficient evidence for the DSD to rebut the presumption of prudence in this case.
- Third, the DSD's arguments about the Project design are conceptually and factually flawed.

A. A SIGNIFICANT PORTION OF THE REVENUE REQUIREMENTS IS UNDISPUTED

97. In paragraph 117 of the DSD Submission, the DSD makes admissions regarding significant components of the revenue requirements: operating costs, overhead and financing costs. It states:

> The DSD does not dispute that, based on the facts known at the present time, and the limited information provided by FAES in this proceeding:
>
> a. the operating costs of the Project are being managed appropriately by FAES;
>
> b. the overhead costs of the Project do not include some indirect costs; and
>
> c. FAES has incurred costs to provide service and has had to finance those costs with both debt and equity in anticipation of future recovery.

The DSD does not appear to object to the recovery of fuel costs either.

98. We offer one further comment on the DSD's proviso "based on the facts known at the present time and the limited information provided by FAES". The BCUC should reject the

DSD's attempt to diminish the import of these admissions. FAES has provided ample evidence to support the reasonableness of these costs.[108]

B. THE PROJECT CAPITAL COSTS WERE REASONABLE

99. The DSD argues that the BCUC should undertake a prudence review of the capital costs.[109] However, under the test in *Enbridge Gas Distribution Inc. v. Ontario (Energy Board)*[110], which the Parties agree is applicable to BCUC prudence reviews[111], there is a presumption of prudence that the DSD must rebut with some tangible evidence. The DSD, for the reasons described below, has not met that burden when it comes to the capital cost.

100. When prudence reviews are undertaken, they are generally prompted by large overruns that might cause one to wonder if the project was well-managed. That is absent here. The DSD has not acknowledged that the BCUC requires CPCN project estimates to meet AACE Class 3 standards, which has an accuracy range of -20%/+30%. The actual cost of $8,099 thousand was well within the AACE Class 3 parameters.[112]

101. The DSD has referenced[113] a BCUC decision related to the Terasen Gas (Whistler) Inc. conversion project, describing it as an instance where the BCUC had triggered a prudence review. That case involved a very different set of facts. The Whistler project had experienced a 100% overrun, with costs exceeding the $6.01 million BCUC-ordered CPCN cost cap by approximately $6 million (to $11.87 million). The presumption of prudence was rebutted in

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[108] See, for instance, FAES Initial Submissions, paras. 162 and 167.

[109] DSD Submission, para. 138.

[110] [2006] O.J. No. 1355, 210 O.A.C. 4, included in the DSD's Book of Authorities.

[111] DSD Submission, para. 126.

[112] Exhibit B-3 FAES Response to DSD IR 1.5.1 provides a detailed breakdown of the costs, the reference to the CPCN Guidelines and the AACE Class 3 definitions. The $8,099 is 18.5% more than the CPCN cost estimate of $6,826. The DSD has quoted 24% as the variance, but this is after application of the CIAC; it is illogical to measure FortisBC's performance on this basis.

[113] DSD Submission, para. 127.

that case because the company had exceeded the cost-cap that had been imposed as a condition of the CPCN.[114]

C. THE DSD'S ARGUMENTS ABOUT THE PROJECT DESIGN ARE CONCEPTUALLY AND SUBSTANTIVELY FLAWED

102. The DSD suggests[115] that FAES breached its contractual obligations under 2.1b of the Service Agreement to design and construct the Project "in accordance with sound and currently accepted industry codes of practice normally employed, at the time and place of performance, in projects of a similar nature." Its position is based on three factors: (a) the lower than foreast thermal energy demand, (b) natural gas savings, and (c) the amount of thermal energy provided via heat pumps.[116] These system design arguments are untenable for the reasons described below. The system was designed properly by experts (JCCLP), and is performing properly.

(a) The Evidence is that FAES Hired Experts in System Design and Analysis Was Performed

103. FAES provided evidence that the design was performed by experts (JCCLP) in accordance with sound and currently accepted industry standards and codes of practice.[117] FAES even provided JCCLP's detailed energy modeling performed for Neilson Grove[118] to prove that JCCLP, in fact, performed the type of modelling that the DSD's expert MCW characterizes as "standard industry practice".[119]

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[114] We also note that the DSD-referenced $80 thousand disallowance represented approximately 0.5% of the project cost, with the remaining over $11.07 million recoverable because the BCUC had found it had been prudently incurred notwithstanding the overrun. This speaks to the allocation of risk under cost of service regulation, which is frequently overlooked in the DSD Submission.

[115] DSD Submission, para. 128.

[116] DSD Submission, paras. 128- 134. These same three arguments are repeated throughout the DSD Submission, both in the context of the request for a cost disallowance and in the context of arguing that it should not have to switch from the transitional MR. See, for instance, paras. 93 and 98.

[117] Exhibit B-7, FAES Rebuttal Evidence, p. 29.

[118] Exhibit B-8, FAES Response to DSD IR 1.7.1 on Rebuttal Evidence.

[119] Exhibit C1-6, DSD Evidence, Report of MCW, pp. 5, 7.

(b) The Load Forecast Variance Had No Impact on System Sizing; It Is Sized to Provide the Amount of Energy Demanded

104. The DSD's first design-related argument is based on the thermal demand variance:

> More specifically, FAES and/or JCLP failed to undertake reasonable efforts to obtain an accurate understanding of the actual thermal energy demands of the Project Buildings prior to undertaking the Project. This is demonstrated by the significant difference between the forecasted annual thermal energy demands of the Project Buildings (10,605 MWh) and the actual annual thermal energy demand for the Project Buildings in the year preceding the COS Rate Application (6,504 MWh).[120]

The DSD has failed to provide the necessary evidence to rebut the presumption of prudence. There is neither evidence of unreasonable action on the part of FAES in forecasting thermal energy demand, nor evidence that that the load forecast variance has resulted in the customer paying too much for service.

The Forecasting Approach Was Appropriate

105. Paragraph 172 of FAES's Initial Submissions addressed the evidence that demonstrated the load forecasting process was appropriate in the circumstances. That evidence included Mr. Cleveland's concession that the approach used to forecast load was "generally an appropriate approach for a project of this type".[121] Mr. Cleveland also conceded: "There was also very limited meter data available before the Project was set up. The only information available was on fuel consumption. This potential source of forecast error has contributed to the above described gas reimbursement issue, and also makes it challenging to confirm equipment output and efficiencies."[122]

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[120] DSD Submission, para. 129. See also DSD Submission, paras. 92-93, 97-98.

[121] Exhibit B-7, FAES Rebuttal Evidence, page 24, quoting Mr. Cleveland: "This is generally an appropriate approach for a project of this type, but in my view FAES' accuracy is outside a reasonable range, and the magnitude of the errors suggest a reasonable participant could have made a more accurate forecast."

[122] Exhibit C1-6 DSD Evidence, Prepared Testimony of Mr. Will Cleveland p. 4.

The System Cost Was Unaffected by the Annual Load Forecast

106. Energy systems are sized for the peak, not with reference to annual consumption. In other words, the FAES system is designed to meet peak demand on the coldest design day. This concept was discussed in the CPCN Application[123] and was also explained in FAES' Rebuttal Evidence.[124] As such, the capital costs were unaffected by the annual load forecast.[125]

107. There is similarly no evidence that the system is undersized. Undersized equipment would create a performance issue on the peak (coldest) days. FAES's thermal energy system is meeting thermal energy demand throughout the year. Apart from implying that DSD-owned make-up air circulation equipment in schools might be contributing some thermal energy, the DSD does not appear to be suggesting that FAES is unable to meet the DSD's peak thermal energy requirements. There is no evidence to support the theory that the FAES system is being materially supplemented by other thermal sources.[126] Were that the case, the DSD would be breaching its contract with FAES.[127]

108. The annual load, while not used when selecting and sizing equipment, was used when developing billing determinants. However, as explained in paragraph 173 of the Initial Submission, the load variance only served to reduce the MR. In arguing for a cost disallowance the DSD is, in essence, arguing that FAES should be penalized because the DSD is saving money.

109. The Terasen Gas (Whistler) Inc. decision cited by the DSD at paragraph 127 is informative in this context. The decision demonstrates that a mis-estimatation, in and of itself, is not a basis for disallowance under cost of service regulation. The primary cause of the overrun in the Whistler case was flawed budgeting, not flawed design or execution (p. 20). The BCUC allowed recovery of all but $80 thousand of the $11.87 million cost because it found that

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[123] 2012 CPCN and Rates Application, Exhibit B-1, p. 17.

[124] Exhibit B-7, FAES Rebuttal Evidence, section 4.3, p. 32.

[125] 2012 CPCN Application, Exhibit B-9, FAES Response to BCUC Confidential IR 2.3.3.

[126] Exhibit B-8, FAES Response to DSD Information Request on Rebuttal Evidence, IR 2.2.1.1.

[127] RDA Section 3.2, Exclusivity.

most costs were prudently incurred. In other words, there was a budgeting error but customers were no worse off as a result because the project was generally executed well and delivering service to customers. In short, the Whistler decision highlights the legal shortcomings of the DSD's reliance on a load forecast variance as a basis to deny cost recovery. Irrespective of whether or not the load forecast was prepared prudently (it was), the capital costs were unaffected because they were driven by peak-day capacity requirements. The Whistler decision says those costs are recoverable.

(c) There Was Never a Requirement to Achieve 93% "Gas Savings"

110. The DSD's second performance-related argument is:

> Furthermore, FAES and/or JCLP failed to undertake the work necessary to conclude with any reasonable certainty that the Project could achieve the 93% natural gas savings (and resulting GHG emission reductions) that FEI originally promised the DSD that the Project could achieve and which were the "primary driver of the Project".[128]

111. There are flaws with this argument.

112. First, the RDA contains no performance requirements relating to natural gas savings.

113. Second, FAES never promised 93% natural gas savings. The 93% natural gas savings figure referenced by the DSD appears to have been extracted from a table filed in the CPCN Proceeding that quoted from the JCLP contract with FAES.[129] The data extracted by the DSD is for only three schools, and even then had been prepared before the detailed design had been completed. The DSD had been, or ought to have been, well aware that the 93% figure was not representative of the overall targeted natural gas savings across the entire Project.

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[128] DSD Submission, para. 129.

[129] Exhibit C1-6, DSD Evidence, Expert Witness Report of MCW, p. 3.

(d) Heat Pump Utilization Was Not a Performance Requirement and the DSD's Calculations Are Unsubstantiated

114. The DSD advocates a further prudence review based on an analysis of heat pump usage and heat pump unit costs prepared by Mr. Cleveland. It maintains that the heat pumps have not delivered a promised level of thermal energy, with the result that the heat pump unit cost is "exhorbitant".[130] However, the calculations performed by Mr. Cleveland's are flawed. The DSD is also overlooking the fact that it had contracted for (and the BCUC approved) an overall pooled service, not for a particular heat pump unit rate.

Mr. Cleveland Is Making Significant Assumptions in His Calculations

115. As FAES indicated in its responses to information requests, the analysis that Mr. Cleveland has attempted was impossible to perform because of the absence of metering on individual pieces of equipment. Metering individual components was superfluous to the Project because the DSD was paying for a thermal energy service based on the combination of all equipment and all schools. For this reason, FAES similarly never provided estimates about the amount of thermal energy that the heat pumps would deliver.[131] Mr. Cleveland had acknowledged this challenge in his initial report:

> "**Limited Meter Data**. The above issue highlights a general challenge in evaluating the Project, which is that there is a limited amount of metered data. Figure 1 illustrates the flow of fuel and thermal energy, and the meter locations for a typical Project site with heat pump-based Systems. The only things actually being metered are: electricity consumption by the FAES Equipment, total natural gas consumption (including, without any sub-metering, FAES Equipment and DSD Equipment), and thermal energy delivered by the FAES Equipment. <u>There is no information available on sub-metered gas consumption, no metered breakdown of how much thermal energy is provided by the FAES heat pumps vs by the FAES boilers, and no meter data on how much thermal energy is being provided by the DSD Equipment.</u> There was also very limited meter data available before the Project was set up. The only information available was on fuel consumption. This potential source of forecast error has contributed to the above described gas

[130] DSD Submission, para. 132.

[131] FAES Argument para. 182.

> reimbursement issue, and also makes it challenging to confirm equipment output and efficiencies."[132] [Emphasis added.]

116. In order to arrive at a percentage, Mr. Cleveland had to use numerous unsubstantiated assumptions.[133]

Mr. Poole and Amaresco Offer Dubious "Corroboration"

117. The DSD maintains that Mr. Cleveland's analysis is "corroborated by the evidence of a person who had direct involvement in the design of the Project (Don Poole) and by the evidence of a third party with no direct involvement in the design of the Project (Amaresco)".[134] In response:

- Contrast the DSD's reliance on Mr. Poole in its Submission with its response to BCUC-DSD IR 1.2.1, in which the DSD had confirmed that it was tendering Mr. Poole's affidavit as lay (i.e., non-expert) evidence.[135] It is self-evident that the DSD wants the BCUC to accept the content of Mr. Poole's emails as true and probative as to the design of the FAES system. FAES explained in its Rebuttal Evidence, which was also discussed in paragraphs 208 and 209 of the Initial Submissions, how Mr. Poole had no visibility into the system design work being undertaken by JCCLP. The issues he was raising were "neither novel nor overlooked."[136] They had already been considered by JCCLP, the experts retained for the job.[137]

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[132] Exhibit C1-6 DSD Evidence, Prepared Testimony of Mr. Will Cleveland p. 4.

[133] Exhibit B-7, FAES Rebuttal Evidence, p. 28.

[134] DSD Submission, para. 133a.

[135] Exhibit C1-8, DSD Response to BCUC IR 1.2.1. "DSD prefaces its response by noting that it has adduced evidence from Mr. Poole in his capacity as a lay witness who has direct knowledge of certain material facts relating to the design of the thermal energy system installed in DSD schools that are the subject of these proceedings."

[136] Exhibit B-7, FAES Rebuttal Evidence, p. 38.

[137] See FAES Initial Submissions, para. 210.

- Amaresco had even less visibility regarding the Project than Mr. Poole. It was also a competitor of FAES that was locked in a dispute with FAES at that time in the BCUC's AES Inquiry. Amaresco is hardly a reliable source.

D. THE ENTIRE AGREEMENT CLAUSE PRECLUDES IMPLYING THE ALLEGED DETAILED PERFORMANCE REQUIREMENTS OR "OBJECTS" IN A FEASIBILITY STUDY

118. The DSD's argument about Project design is premised on alleged performance metrics and "objects set out in the Revised Feasibility Assessment"[138], none of which are stated in the RDA. As discussed in Part Four above, the obligations of FAES under the RDA - the terms and conditions of service (rates) - are expressed in the RDA, and the RDA includes an Entire Agreement clause. The unstated metrics and "objects" are not terms and conditions of service.

119. The following table summarizes FAES's answer on the substance of the alleged "objects stated in the Revised Feasibility Study". We observe that some of these "objects" are absent from the referenced Revised Feasibility Study.

Alleged "objects stated in the Revised Feasibility Study"	FAES's Answer
"reduce the DSD's annual operating and capital costs by $188,000"	This does not appear in the referenced document. Rather, the document refers to calculated annual energy savings of over $180,000 in the first year after completion.
"reduce the DSD's future replacement costs"	This does not appear in the referenced document. However, the service avoided the acknowledged need for the DSD to replace its existing systems.[139] FAES is responsible for all capital costs associated with the service for as long as the DSD continues to renew the service.

[138] DSD Submission, para. 27.

[139] 2012 Decision, p. 3.

Alleged "objects stated in the Revised Feasibility Study"	FAES's Answer
"reduce the DSD's GHG emissions by 69%"	The DSD compares that percentage to an actual reduction in GHG emissions of 44%. However, this is a comparison of two different systems as the final design and configuration of the system changed.[140] To illustrate the impact, the project emitted 1,357 tCO_2e in 2015/16[141] including the two schools that were traded for the 50 roof-top heat pumps. Those two schools emitted 117 tCO_2e in the same year[142]. Subtracting this difference, 2015/16 emissions were 1,240 tCO_2e as originally configured representing a 57.5% reduction over the 2,915 tCO_2e base.[143] Furthermore, the BCUC specifically pointed out in its 2012 CPCN and Rates Decision that this was not a performance requirement.[144]
"increase the efficiency of the DSD's energy systems"	Total annual system efficiency has exceeded 75 percent and the efficiency of the system replaced by the Project had likely been significnatly lower than the 60 percent originally estimated.[145]
"protect the DSD against energy price volatility"	The document also refers to "Stability when it comes to annual budgeting for utilities pertaining to thermal energy". It will be noted that the document is addressing the DSD's annual budgeting (in dollars), not the unit rate. Operations and Cost of Service have stabilized and the contract year aligns with DSD annual budget dates.[146]
"deliver a better and healthier indoor environment to DSD facility occupants"	This does not appear in the document.

E. DSD'S "SPECIFIC RESPONSES" TO FAES'S SUBMISSIONS

120. In paragraph 135, the DSD provides specific responses to FAES' submissions. Our Initial Submissions and the submissions provided above answer the DSD's arguments.

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[140] Exhibit B-7, FAES rebuttal Evidence, p. 22.

[141] Exhibit B-3, FAES Response to DSD IR 1.2.1.

[142] Exhibit B-3, FAES Response to DSD IR 1.2.4

[143] FAES Response to DSD IR 1.2.1 and 1.2.4. [1-((1,357-117)/2915)]/100=57.5%

[144] 2012 Decision, p. 32.

[145] FAES Rebuttal Evidence p. 27.

[146] FAES Initial Submission, paras. 48, 49; 2012 CPCN and Rates Application, p. 39.

PART SEVEN: CONCLUSION AND ORDER SOUGHT

121. The DSD has made a number of important concessions in its Submission, and has offered unpersuasive excuses rather than compelling arguments. The evidence demonstrates that it is just and reasonable for the DSD to be switched from transitional MR to the COS Rate. The COS Rate itself is just and reasonable, reflecting the prudently incurred cost of service and the anticipated amortization of the unrecovered costs from prior years.

ALL OF WHICH IS RESPECTFULLY SUBMITTED.

Dated: February 21, 2019 ***[original signed by Matthew Ghikas]***

Matthew Ghikas

FASKEN MARTINEAU DUMOULIN LLP

Counsel for FortisBC Alternative Energy Services Inc.