BORALEX

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June 30, 2020

Sent by email (commission.secretary@bcuc.com)

Ms. Marija Tresoglavic
Acting Commission Secretary
British Columbia Utilities Commission
Suite 410, 900 Howe Street
Vancouver, BC V6Z 2N3

Re: British Columbia Utilities Commission
Boralex Ocean Falls Limited Partnership (Boralex LP)
Application for Rates and Terms and Conditions of Service to British Columbia Hydro and Power Authority
Project No. 1599046
Boralex LP Final Argument

Dear Ms. Tresoglavic,

In accordance with the updated regulatory timetable set out in Order G-142-20, enclosed is Boralex LP's Final Argument in this proceeding.

Yours truly,

Boralex Ocean Falls Limited Partnership

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Boralex Ocean Falls Limited Partnership

Application to the British Columbia Utilities Commission for Approval of Rates and Terms and Conditions of Service for Service to British Columbia Hydro and Power Authority July 1, 2019 to December 31, 2022 Project No. 159046

Final Argument of Boralex Ocean Falls Limited Partnership

June 30, 2020

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A. INTRODUCTION

1. The Ocean Falls Facilities on the central coast of British Columbia are used by Boralex Ocean Falls Limited Partnership LP (Boralex LP) to supply clean renewable electricity to British Columbia Hydro and Power Authority (BC Hydro) that in turn is used by BC Hydro to serve its customers in the communities of Bella Bella and Shearwater within BC Hydro's Bella Bella NIA. Boralex LP also supplies electricity directly to a small number of its own retail customers and two industrial customers in Ocean Falls.

2. Boralex LP has been a responsible and prudent owner and operator of the Ocean Falls Facilities since acquiring the facilities from Central Coast Power Corporation (CCPC) in 2009. Notwithstanding the isolated and remote location of the facilities and the harsh operating environment in this area of the Province, Boralex LP's service to BC Hydro has been extremely reliable over the years. In this regard, since acquiring the facilities Boralex has made significant investments in order to maintain the structural and operational integrity of the facilities (most of which are over 100 years old) to ensure that it is able to continue to provide safe, secure and reliable service to BC Hydro and its other utility customers over the long term.

3. Safe, secure and reliable service from Boralex LP is highly beneficial to BC Hydro, its ratepayers and the local communities. Receiving reliable electricity service from Boralex LP allows BC Hydro to avoid operating its expensive and environmentally undesirable back-up diesel generating station at Shearwater. This allows BC Hydro to defer, or avoid altogether, major capital upgrades and replacements of the diesel generating facility, it significantly reduces the risks associated with transporting diesel fuel by barge on the west coast to Shearwater, it prevents imposing continuous diesel exhaust emissions and noise impacts on local residents, and it significantly reduces the amount of greenhouse gas and other emissions associated with diesel electric generation.

4. Boralex LP had hoped that the rates for its service to BC Hydro could have been established through negotiations with BC Hydro, which is the basis on which BC Hydro rates have been set since service to BC Hydro commenced in 1986. However, given that Boralex LP and BC Hydro were unable despite their good faith efforts to reach agreement on rates and terms and conditions of service under a new EPA, it has become necessary for the Commission to fix the rates and terms and conditions of service.

5. Consequently, on June 27, 2019 the Commission issued Order G-143-19. Order G-143-19 modified the exemption granted to Boralex LP by Order G-26-10 to remove the exemption from certain sections of the Utilities Commission Act (UCA), including those related to rate setting, for Boralex LP's service to BC Hydro only. The Commission also approved interim and refundable/recoverable rates effective July 1, 2019 and interim terms and conditions for Boralex LP's service to BC Hydro.

6. Boralex LP subsequently filed its rate application (Application)[1] on September 30, 2019 pursuant to Orders G-143-19 and G-202-19, seeking Commission approval of the rates and terms and conditions for Boralex LP's service to BC Hydro.

7. The applied-for rates for Boralex LP's service to BC Hydro have been determined on a utility cost of service basis based on the historical depreciated cost of the Ocean Falls Facilities and Boralex LP's forecast revenue requirement for each of 2019 (six months actuals) and 2020, 2021 and 2022. The revenue requirement set out in Boralex LP's April 29, 2020 Application Update (Application Update)[2] is the revenue requirement on which the applied-for rates are based and reflects the costs necessary to enable Boralex LP to continue to provide safe, secure and reliable service and to earn a fair return on common equity.

8. The rates for Boralex LP's service to BC Hydro have been determined based on Boralex LP's gross forecast revenue requirement less the forecast revenue from its retail and industrial customers in Ocean Falls. As addressed in detail below, not only is it necessary to calculate the rates for service to BC Hydro on this basis in order to enable Boralex LP to recover its cost of providing service, including its allowed return on common equity, the ability of Boralex LP to provide service to retail and industrial customers is very beneficial to BC Hydro because this reduces the costs that would otherwise need to be recovered from BC Hydro.

9. Boralex LP is proposing to recover the net revenue requirement from BC Hydro through a two-tier declining block energy charge rate structure. As addressed in detail below, this rate structure is also very beneficial to BC Hydro because it imposes no fixed charge obligations on BC Hydro and therefore BC Hydro only pays for the electricity that it actually requires and that Boralex LP actually delivers. This also creates a very strong incentive for Boralex LP to continue to provide highly reliable service to both BC Hydro and its retail and industrial customers because Boralex LP will be directly responsible for any lost revenue from BC Hydro and its other customers if it fails or is unable to provide service.

10. Apart from the proposed First Nations relationship building deferral account, Boralex LP is not seeking Commission approval of any cost, load or revenue related deferral accounts.

11. The Application covers a three and one-half year period from July 1, 2019 to December 31, 2022. Boralex LP believes that this test period is appropriate and reasonable having regard for the desire to limit the frequency and cost of Boralex LP's rate applications to the Commission for its service to BC Hydro, particularly in light of the small size of Boralex LP, but recognizing the inherent greater uncertainty in forecasting Boralex LP's costs and revenues over a longer period of time. Boralex LP's intent is to file a subsequent rate application in 2022 to establish rates for a period beyond 2022.

12. As described in the Application, Boralex LP is seeking the following Commission approvals pursuant to Order G-143-19 and sections 59 to 61 of the UCA:

[1] Exhibit B-1.

[2] Exhibit B-11.

(a) approval on a final basis of the following rates for Boralex LP's service to BC Hydro for the period July 1, 2019 to December 31, 2022 as set out in the Application Update:

($/MWh)

	2019*	2020
Tier 1 (up to 13.10 GWh/year)	$270.81	$276.23
Tier 2 (greater than 13.1 GWh/ year)	$50.00	$51.00

($/MWh)

	2021	2022
Tier 1 (up to 11.63 GWh/year)	$281.75	$287.39
Tier 2 (greater than 11.63 GWh /year)	$52.02	$53.06

*July 1 to December 31 for rate and energy amount.

(b) approval of the terms and conditions of Boralex LP's service to BC Hydro that are set out in Appendix B to the Application; and

(c) approval of the First Nations relationship building deferral account.

13. There is an extensive evidentiary record in this proceeding explaining, supporting and justifying the requested approvals. The record includes the Application itself filed by Boralex LP on September 30, 2019, the additional information requested by interveners filed by Boralex LP on December 13, 2019 [3], the supplemental information referred to in Directive 2 of Commission Order G-3-20 filed by Boralex LP on January 20, 2020 [4], the responses of Boralex LP to the two rounds of information requests from the Commission and interveners (approximately 615 information requests in total) filed by Boralex LP on February 24, 2020, March 9, 2020 and April 29, 2020, and the Application Update filed by Boralex LP on April 29, 2020. Boralex LP has endeavoured to provide full, complete and timely responses to all of the information requests and other additional information requested of it during this proceeding.

14. The Commission should approve the applied-for rates, terms and conditions of service and deferral account as just and reasonable.

B. THE OCEAN FALLS FACILITIES

15. An overview of the Ocean Falls Facilities is set out in paragraphs 40 to 67 of the Application and a map showing the location of the facilities is attached as Appendix A to the Application.

[3] Part of Exhibit B-4.

[4] Exhibit B-5.

16. In assessing the costs and risks associated with owning, operating and maintaining the Ocean Falls Facilities, Boralex LP asks the Commission to have particular regard for the age of the facilities and the fact that the facilities are in an isolated and remote location on the central coast of British Columbia, approximately 450 km northwest of Vancouver.

17. The operating environment in this area of the Province is harsh. Ocean Falls receives an average annual precipitation of 4.4 meters. There is no road access to Ocean Falls and the community is only accessible by boat or float plane. Air access can be constrained for extended periods by adverse weather, low cloud or fog, and therefore water access provides the only reliable year-round access. The nearest community to Ocean Falls is Bella Bella, which is approximately 40 km to the west on the east coast of Campbell Island. Any supplies and equipment required by Boralex LP for either operating and maintenance or construction purposes that cannot be flown into Bella Bella and barged to Ocean Falls have to be barged in from where the supplies and equipment can be delivered to tidewater, which is typically Vancouver Island or the Lower Mainland.[5]

18. The key events in the long history of the Ocean Falls Facilities are briefly summarized in paragraphs 15 to 23 of the Application. The history of the facilities is also summarized in BC Hydro's August 29, 2017 Application Requesting the Commission set a Rate for Boralex LP's Electricity Service to BC Hydro.[6]

19. Today the primary Ocean Falls Facilities consist of the dam, penstock, power generation facilities, substation and workshop/storage building in Ocean Falls, the distribution lines in the Ocean Falls town site and the nearby community of Martin Valley, the 45 km distribution voltage transmission line between Ocean Falls and Shearwater, and the Shearwater substation on Denny Island. Boralex LP's Shearwater substation is the point at which the electricity supplied by Boralex LP is metered and sold to BC Hydro and it is located adjacent to BC Hydro's back-up diesel generating station.

20. The dam, penstock and hydroelectric generation facilities that form part of the Ocean Falls Facilities were constructed over 100 years ago to serve the pulp and paper mill facilities at Ocean Fall that began operations in 1917. The 45 km transmission line, including the two subsea sections that cross Johnson Channel and Gunboat Passage, was built by CCPC in 1986 when it acquired the facilities from the Province. It was at this time BC Hydro and CCPC entered into the 1986 EPA for the purpose of supplying hydroelectricity from the Ocean Falls Facilities to meet the requirements of BC Hydro's customers in the Bella Bella NIA and allowing BC Hydro to displace diesel generation. Prior to this time BC Hydro served the Bella Bella NIA with its Shearwater diesel generation facility that was constructed in 1969.

21. Boralex LP's service to BC Hydro has been extremely reliable since it acquired the Ocean Falls Facilities from CCPC in 2009. Over BC Hydro fiscal periods

[5] Application paras. 15 and 16.

[6] Commission Project No. 1598947 (Exhibit B-1).

F2010 to F2017, Boralex LP has supplied on average approximately 99 percent of BC Hydro's electricity requirements for the Bella Bella NIA.[7]

22. As demonstrated by this high level of service reliability, the facilities have been well maintained and operated by Boralex LP since it acquired the facilities. Although the facilities are in generally in good operating condition, given the age of the main plant facilities it is not surprising that some components require replacement or rehabilitation.

23. There were a number of information requests regarding the operating configuration and level of redundancy of the four generating units within the Ocean Falls powerhouse. The current achievable capacities of Units G1 and G2 are 1,900 kW and the current achievable capacities of Units G3 and G4 are 4,200 kW.[8]

24. As explained in the responses to the information requests[9], although the unit dispatch configuration varies seasonally depending on expected demand, the typical operating configuration at Ocean Falls involves running at least two units at all times: one of the larger units (G3 or G4) in isochronous mode and one of the smaller units (G1 or G2) in frequency droop mode. The two larger units are sometimes run together during peak load periods to provide additional operating headroom.

25. Operating and dispatching the generating units in this manner provides a stable and reliable operational configuration of the units and enables Boralex LP to deliver power and all required ancillary system services to the Bella Bella NIA, including frequency control, voltage/reactive power control, spinning and non-spinning reserves, automatic generation control, adequate system inertia, black start capability and reliable operation of the protections on the transmission line between Ocean Falls and Shearwater. Should either spinning unit be forced out of service, there is normally an identical non-spinning unit available to be rapidly put into service, unless one of the offline units is undergoing maintenance or in situations when both of the larger units are being operated simultaneously (i.e., during high winter load periods).

26. This typical operating configuration has been utilized since the Ocean Falls plant first began serving BC Hydro's Bella Bella NIA in the mid-1980s. Operating the units in this manner is also very beneficial because it reduces electrical and mechanical loads on the individual units (all of which have been in service for over 100 years) and balances the total service hours between all four units, thereby extending machine service lives and increasing the interval between major maintenance activities.

27. As explained in Boralex LP's response to BCUC IR 1.2[10], this level of generator redundancy is the minimum level of redundancy necessary to enable Boralex LP to maintain historic levels of service reliability to BC Hydro and its customers at

[7] Boralex LP response to BCUC IR 1.6.2 (Exhibit B-6).

[8] Application para. 52.

[9] Boralex LP responses to BCUC IRs 1.1, 1.2 and 1.7 (Exhibit B-6).

[10] Exhibit B-6.

the lowest operating cost. Together the two smaller units (G1 and G2) do not have sufficient capacity to serve even the Bella Bella NIA peak load, which together with line losses and plant/shop loads is forecast to be approximately 4,220 kW in 2022 (3,717 kW for the Bella Bella NIA with line losses and approximately 500 kW for plant/shop loads).[11] Although either of the two larger units (G3 and G4) would notionally be just able to serve the forecast Bella Bella NIA load (but not any higher than forecast Bella Bella NIA load and not the entire customer load), at least two units are required to meet the Bella Bella peak demand and provide all required system ancillary services, including frequency control, voltage/reactive power control, spinning and non-spinning reserves, automatic generation control, adequate system inertia, black start capability and reliable operation of the protections on the transmission line.

28. Without the availability of the back-up units, any extended outage to either of larger units (again, both of which have been in service for over 100 years) would require BC Hydro to operate its costly and environmentally undesirable backup diesel generating station at Shearwater. As discussed in Boralex LP's response to BCUC IR 7.1[12], unit G4 has been out of service since Q3 2019 due to replacement bearing issues identified during shaft and turbine maintenance work. Consequently, a forced outage to unit G3 during the G4 maintenance period would leave Boralex LP unable to serve peak Bella Bella NIA loads even with both units G1 and G2 available.

29. Moreover, the industrial customer loads in Ocean Falls, the revenue from which reduces the net revenue requirement to be recovered from BC Hydro by over $500,000 per year over the test period, cannot be reliably supported without maintaining all four existing units.[13]

30. Finally, the electricity prices that were payable by BC Hydro under the 1986 EPA between BC Hydro and Boralex LP that expired on June 30, 2019 were fixed and therefore Boralex LP (and CCPC before Boralex LP) had a direct financial incentive to reduce costs if and where possible during the term of the 1986 EPA. Also, Boralex LP (and CCPC) had no obligation under the 1986 EPA to maintain redundant generating capacity. Accordingly, Boralex LP would have stood to benefit financially during this period if it was able to reduce costs by idling generating capacity while at the same time maintaining service levels. However, Boralex LP did not idle any of the generating units because the operating practice and level of generator redundancy adopted and maintained by Boralex LP (which is the same as that adopted and maintained by CCPC between 1986 and 2009) is the best operating practice and the minimum level of redundancy necessary to allow Boralex LP to maintain very high levels of service reliability to BC Hydro at the lowest cost.[14]

[11] In its August 29, 2017 Application Requesting the Commission set a Rate for Boralex LP's Electricity Service to BC Hydro, BC Hydro indicates (at page 13) that the peak winter load in the Bella Bella NIA reaches 5 MW in the winter.

[12] Exhibit B-6.

[13] Boralex LP response to BCUC IR 1.1 to BCUC IR 1.2 (Exhibit B-6).

[14] Boralex LP responses to BCUC IR 1.1 (Exhibit B-6) and Zone IB Ratepayers Group IR 1.1 (Exhibit B-17).

C. COST OF SERVICE BASED RATES

31. Boralex LP has applied to the Commission to fix the rates for Boralex LP's service to BC Hydro on a traditional utility cost of service basis.

32. Boralex LP submits that cost of service based rates are appropriate in the case of the Ocean Falls Facilities and will result in just and reasonable rates for Boralex LP's service to BC Hydro. Establishing rates based on other rates setting methodologies (such as a rate pegged to a tariff of another utility or some form of benchmark rate plus inflation) would not be reflective of Boralex LP's cost of providing service, particularly in light of the capital expenditures required over the next few years to maintain the facilities.

33. BC Hydro has also taken the position, as initially expressed in its August 29, 2017 Application Requesting the Commission set a Rate for Boralex LP's Electricity Service to BC Hydro, that the rates for Boralex LP's service to BC Hydro should be established on a utility cost of service basis.

34. Neither BC Hydro nor the two other interveners questioned the appropriateness of cost of service rate setting either in the additional information they requested from Boralex LP at the commencement of this proceeding or in their information requests to Boralex LP.

D. NET REVENUE REQUIREMENT

35. Boralex LP has determined the applied-for rates for its service to BC Hydro based on Boralex LP's gross forecast revenue requirement less the forecast revenue from its retail and industrial customers in Ocean Falls.

36. In its letter dated June 5, 2020 [15], the Commission invited parties to make submissions on whether this methodology is just and reasonable. Boralex LP submits that the methodology is just and reasonable for the following reasons.

The Commission is Obligated to Fix Rates that Permit Boralex LP to Recover all of its Reasonable and Prudently Incurred Costs

37. Boralex LP is a public utility under the UCA that carries on the business of providing electrical service to BC Hydro and retail and industrial customers in Ocean Falls. Boralex LP is a single entity utility with one rate base and one cost of service.

38. Boralex LP's gross revenue requirement represents Boralex LP's cost of providing service, including a return on common equity. The gross revenue requirement is recovered from all of Boralex LP's customers through the rates charged to those customers. However, because the rates charged by Boralex LP to its non-BC Hydro customers have already been determined in accordance with prior Commission orders, the revenue that can be recovered from these customers is also already fixed. Therefore, in order for Boralex LP to recover its

[15] Exhibit A-12.

gross revenue requirement, including its allowed return on common equity, the net revenue requirement has to be recovered from BC Hydro through the rates charged to BC Hydro.

39. While the rates charged by Boralex LP to its retail and industrial customers are not being determined by the Commission in this proceeding, these rates are not "unregulated"; they have been established in accordance with prior Commission orders.

40. With regard to Boralex LP's retail customers, the rates that Boralex LP is permitted to charge these customers are regulated under the terms of Order G-26-10 (and as was confirmed by Order G-143-19), which requires that these rates be the same as the rates charged by BC Hydro in Rate Zone II (non-integrated areas). This has been the case since the Ocean Falls facilities were acquired by CCPC from the Provincial government in 1986 in accordance with Order G-40-86 dated July 4, 1986. In fact, it was a condition precedent to the completion of the acquisition that the Commission issue an exemption order that tied the rates CCPC was permitted to charge its retail customers to BC Hydro's Zone II rates.[16] This ensured that retail customers in Ocean Falls (a non-integrated area) paid the same rates as customers in BC Hydro's non-integrated areas. Boralex LP also understands that the BC Hydro Zone IB rates (Bella Bella NIA) are the same as the BC Hydro Zone II rates, with the exception that the Zone IB rates do not have the second tier inclining block rate which is part of the Zone II rates (i.e., the Zone IB rates are the same as the Zone II tier 1 rates). Consequently, with the exception of the inclining tier 2 rate paid by retail customers in Ocean Falls, retail customers in Ocean Falls pay the same rates as customers in the Bella Bella NIA. This stands to reason from a public policy perspective, and why the Province would have made it a condition of the original sale, because both customer groups are in a non-integrated area of the Province and receive their electricity from the very same Ocean Falls Facilities.

41. With regard to Boralex LP's industrial customers, under the terms of Order G-26-10 (and as was confirmed by Order G-143-19) the rates charged by Boralex LP to these customers are to be negotiated between the parties, provided that the industrial customer rates may not exceed the rates authorized for BC Hydro for similar service in Rate Zone II (which is Rate Schedule 1200 with the discounts set out in Rate Schedule 1211).[17] The negotiations are based on what the industrial customers are willing and able to pay for electricity having regard for the other costs of locating their operations in Ocean Falls, a remote and isolated location.

42. When Boralex LP and BC Hydro were unable to reach agreement on a new long-term EPA, the Commission issued Order G-143-19 on June 27, 2019 which revised Order G-26-10 to enable the Commission to fix Boralex LP's rates for its service to BC Hydro only. Accordingly, in issuing Order G-143-19 the Commission expressly left in place the basis on which Boralex LP's rates for

[16] See Section 5.01(d) of the Agreement dated March 27, 1986 between Ocean Falls Corporation and CCPC attached as Appendix II to Commission Order G-40-86 dated July 4, 1986.

[17] Boralex LP response to BCUC IR 53.1.1 (Exhibit B-13).

service to its retail and industrial customers are to be determined as established by Order G-26-10.

43. Consequently, although the gross revenue requirement is recovered from all of Boralex LP's customers, Boralex LP cannot change or adjust the rates that it charges its retail and industrial customers because those rates have already been established in accordance with the prior Commission orders. Therefore, the amount of Boralex LP's gross revenue requirement that can be recovered from the retail and industrial customers is also already fixed.

44. In Boralex LP's submission, there is a statutory obligation on the Commission under Sections 59 and 60 of the UCA to fix rates for Boralex LP's service to BC Hydro that will permit Boralex LP the opportunity to recover all of its costs of providing service, including the rate of return on common equity approved by the Commission for Boralex LP. Rates that are insufficient to enable a utility to recover its costs, including a fair and reasonable return, are unjust and unreasonable under the UCA. Because the rates for Boralex LP's service to its non-BC Hydro customers are already fixed, it will not be possible for Boralex LP to recover its cost of providing service unless the net revenue requirement is recovered from BC Hydro.

45. The leading authority addressing the Commission's obligation under Sections 59 and 60 of the UCA to set rates that are sufficient to enable a utility to recover its costs, including its allowed return on equity, is *Hemlock Valley Electrical Services Ltd. v. British Columbia (Utilities Commission)* (1992), 66 B.C.L.R. (2d) 1 (C.A.),[18] which in turn is based substantially on the Supreme Court of Canada's decision in *British Columbia Electric Railway Co. Ltd. v. Public Utilities Commission of BC*, [1960] S.C.R. 837.[19] These decisions focused on what are now substantially the following provisions in sections 59 and 60 of the UCA:

> **59** (1) A public utility must not make, demand or receive
>
> (a) an unjust, unreasonable, unduly discriminatory or unduly preferential rate for a service provided by it in British Columbia, or
>
> (b) (b) a rate that otherwise contravenes this Act, the regulations, orders of the commission or any other law.
>
> ...
>
> (4) It is a question of fact, of which the commission is the sole judge,
>
> (a) whether a rate is unjust or unreasonable,
>
> (b) whether, in any case, there is undue discrimination, preference, prejudice or disadvantage in respect of a rate or service, or

[18] Attachment A.

[19] Attachment B.

(c) whether a service is offered or provided under substantially similar circumstances and conditions.

(5) In this section, a rate is "unjust" or "unreasonable" if the rate is

(a) more than a fair and reasonable charge for service of the nature and quality provided by the utility,

(b) insufficient to yield a fair and reasonable compensation for the service provided by the utility, or a fair and reasonable return on the appraised value of its property, or

(c) unjust and unreasonable for any other reason.

60 (1) In setting a rate under this Act or the regulations

(a) the commission must consider all matters that it considers proper and relevant affecting the rate,

(b) the commission must have due regard to the setting of a rate that

(i) is not unjust or unreasonable within the meaning of section 59

….

46. In *Hemlock Valley* the Commission allowed a rate increase for the utility but declined to permit the full implementation of the increase, and instead directed that it be phased in over three years so as to avoid or lessen the "rate shock" of the increase on the utility's customers. Upon request, the Commission later reconsidered the matter and, purporting to distinguish *B.C. Electric,* concluding that having regard to the impact on customers, phasing in of the rate increase was "an integral part of the finding of just and reasonable rates".[20]

47. The Court of Appeal for British Columbia overturned the Commission's decision to phase in the rate increase, reasoning that to do so would preclude the utility from earning the rate of return found by the Commission to be the fair and reasonable return on equity. Relying on the Supreme Court of Canada's decision in *B.C. Electric*, the Court of Appeal found that the Commission, having found the fair rate of return on equity for the utility, was then *required* to set customer rates so as to allow the utility the opportunity to earn that return.

48. The Commission's obligation to set rates that are sufficient to enable a utility to recover its costs, including its allowed return on equity, has been addressed in a number of Commission decisions. For example, this issue was addressed by the Commission in its Reasons for Decision and Order G-99-06 dated August 21, 2006 in a case involving a 2006 rate application by Pacific Northern Gas Ltd.[21]

[20] B.C.L.R. page 11, para. 34.

[21] See also: Stage 1 Generic Cost of Capital Decision dated May 10, 2013 (pages 11 and 12); Decision and Order G-84-19 dated April 16, 2019 re FortisBC Alternative Energy Services Inc. Application for Approval of the Fiscal 2018/2019 Revenue Requirement and Cost of Service Rates for the Thermal Energy Services to Delta School

The issue in that proceeding was whether PNG should be permitted to recover the revenue deficiency created by the loss of its major industrial customer (Methanex) from its other remaining customers. The Commission concluded that it was obligated to do so under Sections 59 and 60, otherwise PNG would not be able to recover its reasonable and prudently incurred costs:

> "… although PNG is unique, it is and has been regulated by the Commission under the Act on a traditional cost of service basis. What this means is that this utility, which is a virtual monopoly provider of natural gas in its service area, is permitted under the Act to recover the reasonable and prudent costs of providing its services in exchange for the obligation to provide safe and reliable service. One of the regulator's tasks, therefore, is to balance the need for the Utility to recover its reasonable and prudent costs with the need to ensure that ratepayers are charged fair and reasonable rates. Rates charged to customers are based on costs incurred by the utility to provide service. If the Commission finds certain costs to be imprudent or unreasonable, it will disallow such expenditures and reduce proposed rates accordingly.
>
> The statutory obligation to approve rates which will afford a fair compensation for the services rendered and provide the utility with a fair and reasonable return was articulated by Mr. Justice Locke in *B.C. Electric*, (at pp. 846 and 848):
>
> > "In my opinion the true meaning of the relevant sections of the *Public Utilities Act* is that a utility is given a statutory right to the approval of rates which will afford to it fair compensation of the services rendered and that the quantum of that compensation is to be the fair and reasonable rate of return upon the appraised value of the property of the company referred to in s. 16(1)(b) [ss. 59(5)(a) and (b) and 60(1)(b)(i). …
> >
> > The obligation to approve rates which will provide the fair return to which the utility has been found entitled is, in my opinion, absolute, which does not mean that the obligation of the Commission to have due regard to the protection of the public, as required by s. 16(1)(b) [ss. 59(5)(a) and (b) and 60(1)(b)(i)], is not to be discharged. It is not a question of considering priorities between "the matters and things referred to in Clauses (a) and (b) of subsection (1) of s.16 [now ss. 59(5)(a) and (b)]. The Commission is directed by s. 16(1)(a) [now s. 60(1)(a)] to consider all matters which it deems proper as affecting the rate but that consideration is to be given in the light of the fact that the

District No. 37 (page 14); and Reasons for Decision and Order G-42-03 dated June 5, 2003 re Centra Gas British Columbia Inc. 2002 Rate Design Application (pages 25 and 26), which is the subject of the Court of Appeal for British Columbia decision discussed in paras. 49 and 50 below.

> obligation to approve rates which will give a fair and reasonable return is absolute." [emphasis added]
>
> The Commission Panel considers, therefore, that it is required, by virtue of sections 59 and 60 of the Act to allow the utility to recover its reasonable and prudent cost of service, to be determined on the basis of its 2006 RRA and the evidence adduced in this proceeding."[22]

49. *Hemlock Valley* was applied by the Court of Appeal for British Columbia in *BC Hydro and Power Authority v. Terasen Gas (Vancouver Island) Inc.,* 2004 BCCA 346.[23] The issue in *Terasen Gas* was the correctness of a Commission decision to include in the transportation rates paid by BC Hydro for service on the transmission system of Centra Gas British Columbia Inc. (which at the time of the Court's decision had been renamed Terasen Gas (Vancouver Island Inc.)) a contribution to the amortization of an accumulated shortfall between Centra's revenues and costs that arose on Centra's Vancouver Island distribution system.[24] While Centra's facilities comprised a transmission pipeline to deliver gas from the Lower Mainland to Vancouver Island and a distribution system on Vancouver Island, it was nonetheless one entity with one rate base and one cost of service. The rates paid by the distribution customers were subject to a "soft cap" because competition from alternative energy sources imposed a pragmatic limit on the revenue that could be obtained from those customers. The rates for Centra's transmission customers other than BC Hydro (the Vancouver Island Joint Venture and Squamish Gas) were also already fixed by agreement under the terms of their transportation service agreements with Centra, which had been approved under a Special Direction issued to the Commission by the Lieutenant Governor in Council under the Vancouver Island Pipeline Act, and the Special Direction precluded the recovery of the revenue deficiency from these customers.

50. Because Centra's distribution customer rates were subject to the "soft cap" and the rates for the non-BC Hydro transportation customers were already fixed under the transportation service agreements with those customers, a substantial portion of the revenue deficiency had to be recovered from the rates charged to BC Hydro if the revenue deficiency was going to be recovered by Centra over a reasonable period of time and before royalty credits available to Centra expired. BC Hydro argued that as a transportation service customer the Commission did not have the jurisdiction under the Special Direction or the UCA to require BC Hydro to make a contribution to the accumulated revenue deficiency that arose on the distribution system. Applying *Hemlock Valley*, the Court of Appeal rejected BC Hydro's arguments and upheld the Commission's decision:

> "[35] The ability of Centra to earn a fair return on its utility rate base is an imperative of the Special Direction and the regulatory scheme.

[22] Reasons for Decision and Order G-99-06 dated August 21, 2006, pages 23 and 24.

[23] Attachment C.

[24] Reasons for Decision and Order G-42-03 dated June 5, 2003 re Centra Gas British Columbia Inc. 2002 Rate Design Application.

> General regulatory principles require the Commission to grant a utility the opportunity to earn a fair return: *Hemlock Valley Electrical Services Ltd. v. British Columbia (Utilities Commission*) (1992), 66 B.C.L.R. (2d) 1, 12 B.C.A.C. 1 ¶57. The "soft cap" on rates paid by Distribution System customers because of the competition from alternative energy sources imposed a pragmatic limit on the revenue that could be obtained from those customers. The rates for the Joint Venture and Squamish Gas were fixed by formulas in their transportation service agreements and confirmed by the Special Direction. While the rates set for Distribution System customers are projected to make some contribution to the amortization of the accumulated revenue deficiency, they will still leave a substantial portion outstanding in 2011, when the royalty credits will end, with a corresponding increase in the cost of service. The alternatives facing the Commission were to set rates for BC Hydro that provided for a contribution to the amortization or defer substantial recovery to an uncertain future after 2011. The submission of Mr. Quail, on behalf of the Consumers' Association of Canada (BC Branch) and other residential consumer groups, emphasized the continued financial vulnerability of the utility if amortization of the Deficiency Account were deferred to an indefinite, uncertain future. The Special Direction instructs the Commission to set rates that will amortize the Deficiency Account balance "over the shortest period reasonably possible" (s. 2.10(j)). The legislative scheme, the Special Direction and economic exigencies of the single entity utility all look to BC Hydro (and any new transportation service contracts) to contribute substantially to the amortization of the accumulated deficiency."[25]

51. In this case, Boralex LP is a single entity utility with one rate base and one cost of service. The rates for Boralex LP's retail and industrial customers are already established in accordance with prior Commission orders that remain in effect today. Similar to the situation in *Terasen Gas*, if the rates for Boralex LP's service to BC Hydro are not based on Boralex LP's forecast gross revenue requirement less the forecast revenue from the retail and industrial customers, Boralex LP will not be able to recover its cost of providing service, including the return on common equity allowed by the Commission in this proceeding, contrary to Sections 59 and 60 of the UCA. Determining the rates for Boralex LP's service to BC Hydro based on the forecast net revenue requirement will provide Boralex LP with the opportunity to recover its cost of providing service, including its allowed return on common equity.

[25] The Commission reached the same substantive conclusion in its July 31, 2002 Decision regarding PNG's 2002 Revenue Requirements Application discussed in Boralex LP's response to BCUC IR 43.1 (Exhibit B-13), where the Commission directed that the revenue deficiency resulting from a load retention rate negotiated between PNG and Methanex (prior to when Methanex left the system altogether, which is the subject of the Commission Decision in para. 48 above) be recovered from PNG's other customers.

The Recovery of the Net Revenue Requirement from BC Hydro Represents a Fair, Reasonable and Appropriate Allocation of Costs

52. The primary and predominant purpose of the Ocean Falls Facilities is to provide electric service to BC Hydro and the Bella Bella NIA. The facilities would not have been acquired (and upgraded) by CCPC from the Province of British Columbia in 1986 without the Bella Bella load and the sale of electricity to BC Hydro to serve the load under the 1986 EPA that was entered into at the time of the acquisition of the facilities. There were no industrial customers at that time (Mowi Canada West did not become a customer of CCPC until 2002 and Ocean Falls Blockchain only became a customer of Boralex LP in 2018) and the retail load in Ocean Falls was (and remains) far too small to support the acquisition, maintenance and operation of the facilities. Accordingly, without the Bella Bella load there would have been no Ocean Falls utility in the first place.[26]

53. Virtually all of Boralex LP's capital and operating costs are required to provide service to BC Hydro and the Bella Bella NIA. If Boralex LP had no retail or industrial customers, the only costs that Boralex LP would be able to avoid are the relatively minor costs associated with the distribution lines in the Ocean Falls town site and Martin Valley.[27] Similarly, all the capital improvements being undertaken by Boralex LP over the test period are required to maintain safe, secure and reliable service to BC Hydro and the Bella Bella NIA.[28]

54. With regard to the two industrial customers specifically, Boralex LP has not undertaken any capital improvements since its acquisition of the Ocean Falls facilities to accommodate the load from its two industrial customers.[29] Mowi Canada West was an existing customer when Boralex LP acquired the facilities, and is connected to the system by a 900 meter distribution line that forms part of Boralex LP's distribution facilities in Ocean Falls. Ocean Falls Blockchain began taking power in July 2018 and paid all the costs required to connect its operations to the Ocean Falls Facilities, and none of these interconnection facilities are included in Boralex LP's rate base.

55. Moreover, neither the timeline nor scope of any forecast capital improvements has been affected by the load from Boralex LP's industrial customers. The capital improvements over the test period are driven by asset condition and BC Hydro interconnection requirements and are necessary in order to maintain safe and reliable service to BC Hydro and the Bella Bella NIA.[30]

56. As demonstrated in Boralex LP's response to BCUC IR 32.2 [31], if each of the asset categories that make up the Ocean Falls Facilities was categorized based

[26] Boralex LP response to BCUC IR 30.1 (Exhibit B-13).

[27] Boralex LP response to BCUC IR 2.3.2 (Exhibit B-6).

[28] Boralex LP response to Zone IB Ratepayers Group IR 6.1 (Exhibit B-17).

[29] Boralex LP response to BCUC IR 4.1 (Exhibit B-6).

[30] Boralex LP response to BCUC IR 7.5 (Exhibit B-6).

[31] Exhibit B-13.

on whether they are required to provide service to all customers, for the sole or predominant purpose of servicing BC Hydro, or for the sole or predominant purpose of serving BC Hydro and all customers, and the gross revenue requirement was then allocated based on that categorization using either a percentage of load or a peak demand methodology, BC Hydro would be required to pay a *greater* amount of the gross revenue requirement than the amount being proposed by Boralex LP (i.e., the gross revenue requirement less the forecast revenue from the retail and industrial customers). Conversely, the amount of the gross revenue requirement allocated to the retail and industrial customers using either methodology would be *less* than the revenue generated by the prevailing rates charged by Boralex LP to these customers.

57. Accordingly, determining the rates for Boralex LP's service to BC Hydro based on the forecast net revenue requirement results in a fair, reasonable and appropriate allocation of costs to BC Hydro.

The Methodology is Beneficial to BC Hydro

58. As discussed above and in Boralex LP's responses to BCUC IRs 2.3.2 and 30.1[32], Boralex LP does not incur any significant costs in providing service to its retail and industrial customers in Ocean Falls. The cost to provide service to these customers is very low and indeed lower than the revenue generated by the rates charged to these customers.

59. Accordingly, the revenue that Boralex LP is able to generate from the sale of electricity to its retail and industrial customers makes a significant net positive contribution to Boralex LP's cost of providing service and enables Boralex LP to reduce its rates for service to BC Hydro. As shown in the Application Update, the forecast revenue from the retail and industrial customers is approximately $600,000 per year over the test period. Without this revenue contribution, this amount would need to be recovered from BC Hydro.

E. BC HYDRO LOAD FORECAST

60. Based on the Application Update, Boralex LP's forecast deliveries to BC Hydro are now as follows:

BC Hydro Electricity Delivery Forecast (MWh)

	2019 Actual	2020	2021	2022
BC Hydro	12,953	13,100	11,816	12,005

[32] Exhibits B-6 and B-13, respectively.

61. The 2020 forecast is based on the average energy sales to BC Hydro from 2014 to 2018 of 13,072 MWh (Application, Table 1), rounded to 13,100 MWh. As shown in Table 1 in response to Boralex LP's response to BCOAPO IR 5.1, with the inclusion of actual deliveries for 2019 of 12,953 MWh the average deliveries to BC Hydro over the six year period from 2014 to 2019 were 13,052 MWh and the average deliveries over the five year period from 2015 to 2019 were 13,086 MWh. Accordingly, even with the inclusion of actual deliveries for 2019, Boralex LP believes that it is still reasonable to round either the six year or five year averages to 13,100 MWh for forecasting purposes.

62. For 2021 and 2022, the 2020 forecast deliveries of 13,100 MWh were increased by 1.6% per year. The forecast deliveries for these two years was then reduced to account for the six-week plant outage from mid-April to the end of May each year to accommodate the outage required for the Penstock 2 rehabilitation work. The reduced amount is based on an average of the energy sales to BC Hydro from mid-April to the end of May over the 2014 to 2018 period.[33]

63. Boralex LP does not directly serve customers in the Bella Bella NIA and did not undertake an independent forecast of the Bella Bella NIA electricity load. However, the 1.6% escalator is based on Boralex LP's understanding, based on its discussions with BC Hydro, of what BC Hydro believes is a reasonable annual growth rate for the load in the Bella Bella NIA.[34] Boralex LP submits that the forecast is reasonable and does not in any way underestimate the expected load. In this regard, Boralex LP notes that the BC Hydro actual load has exceeded 13,100 MWh per year only once (in 2017) in the last six years.[35]

64. Boralex LP also notes that under the proposed two-tier declining block rate structure and Tier 1/Tier 2 threshold, Boralex LP is exposed to asymmetrical risk/benefit impacts should the Bella Bella NIA load grow at a different rate than forecast by Boralex LP. As discussed below, the threshold has been set at 13,100 MWh for 2020 and 11,630 MWh for 2021 and 2022 (the 2020 level adjusted downward for the penstock rehabilitation work). Lower than forecast growth reduces Boralex LP's revenues by the product of the lower than forecast energy sales by the higher Tier 1 rate, whereas higher than forecast growth will increase Boralex LP's revenues by the product of the higher than forecast growth by the much lower Tier 2 rate. In other words, if for any reason the actual load is less than the Tier 1/Tier 2 threshold Boralex LP will lose significantly more revenue (all at the Tier 1 rate) than it would gain if the actual load is greater than the threshold (all at the lower Tier 2 rate).[36]

65. This impact is shown in the sensitivity analysis provided by Boralex LP in its response to BCUC IR 51.3, which shows the revenue deficiency/sufficiency if the BC Hydro load is either 10% greater than forecast or 10% less than forecast. As shown in the response, over the three year period 2020 to 2022 the revenue

[33] Application para.152.

[34] Boralex LP response to BCUC IR 21.2 (Exhibit B-6).

[35] Boralex LP response to BCOAPO IR 5.1 (Exhibit B-8).

[36] Boralex LP responses to BCUC IRs 21.4 and 21.6 (Exhibit B-6).

deficiency will be -$909,158 if the BC Hydro load is 10% less than forecast but only $266,947 higher if the BC Hydro load is 10% greater than forecast.

66. Finally, Boralex LP also notes that the load forecast for 2021 and 2022 assumes a fixed six week shutdown period for the Penstock 2 rehabilitation work in each of these years. This imposes a very strong incentive on Boralex LP to limit the outage time and complete the work within the six week period because, if the shutdown extends beyond six weeks, Boralex LP will lose revenue from both BC Hydro and its two industrial customers in Ocean Falls. Minimizing the shutdown period is beneficial to both Boralex LP and its customers.

F. NON-BC HYDRO REVENUE FORECAST

67. Based on the Application Update, Boralex LP's forecast revenue from its retail and industrial customers in Ocean Falls is now as follows:

Non-BC Hydro Revenue Forecast ($000)	**2019 (Q3-Q4) Actual**	**2020**	**2021**	**2022**
Ocean Falls Retail Customer Revenue	$50	$94	$96	$98
Ocean Falls Industrial Customer Revenue	$304	$533	$503	$512
Total	**$354**	**$627**	**$599**	**$610**

68. As noted in the Application Update, the forecast revenue from the two industrial customers has been updated from the original Application to reflect the delay in the commencement of the Penstock 2 rehabilitation work from 2020 to 2021. There is no change in the forecast revenue from sales to Boralex LP's retail customers in Ocean Falls as a result of the delay because sales to these customers are unaffected by the penstock related shutdowns.

69. Boralex LP's forecast revenue from its retail customers is based on average historical revenue from these customers over the period 2014 to 2018 and an assumed 2% annual increase. The number of retail customer accounts and the retail customer load has been stable over the years and weather changes are the primary reason for the yearly variations in the retail customer load.[37]

70. Boralex LP believes that the forecast revenue from its retail customers is reasonable and has not proposed any mechanisms to account for either differences in retail rates or load because, given the small number of retail customers, any differences will not have any material impact on Boralex LP's operations or the revenue credit to the gross revenue requirement. As indicated

[37] Boralex LP responses to BCUC IRs 22.1 (Exhibit B-6) and 52.2 (Exhibit B-13).

in Boralex LP's response to BCUC IR 52.4.1[38], a variance of even 20% in the forecast annual revenue from the retail customers (either as a result of higher or lower rates or higher or lower loads, or a combination of both) would be approximately $19,000, representing only about 0.05% of the net revenue requirement used to fix the BC Hydro rates. As shown in Boralex LP's response to BCUC IR 52.1.10, since 2011 the residential the load has never varied by as much as 20%, with the highest variation being -16.8% between 2012 and 2013.

71. The forecast revenue from Mowi Canada West and Ocean Falls Blockchain is based on the forecast load from these customers and the rates negotiated with each customer. The forecast revenue also includes the forecast lease payments from Ocean Falls Blockchain for its leased space in Boralex LP's workshop/storage building.[39]

72. The two industrial customers have not informed Boralex LP that they intend to expand their operations or to increase their electric loads over the forecast period.[40]

73. Boralex LP is also not engaged in talks with any potential new customers who might take service during the test period.[41] Boralex LP see little or no prospect that it will be able to attract any new industrial customers to Ocean Falls over the test period.

74. With regard to Mowi Canada West, this customer has historically had a stable load and Boralex LP has assumed that this will continue in the test period. Given the nature of Mowi Canada West's operations in Ocean Falls, there is little likelihood that this load will be higher than forecast. Rather, given the political/environmental issues facing the fish farming industry in British Columbia, Boralex LP believes that there is greater risk that this load will be lower than higher over the test period.[42]

75. With regard to Ocean Falls Blockchain, this is a much higher risk load as the ongoing viability of the facility depends on volatile cryptocurrency prices in the international market and the efficiency and effectiveness of the servers installed by Ocean Falls Blockchain. Based on its discussions with Ocean Falls Blockchain, Boralex LP believes that there is very little likelihood that Ocean Falls Blockchain will expand its cryptocurrency facility or increase its load over the test period.[43] Rather, there is a significant risk that this load, and the associated revenue, will be far less than forecast.

76. The electricity purchase agreements between Boralex LP and the two industrial customers have energy charge rate structures with no minimum consumption, fixed charge, take-or-pay or similar obligations on the part of the customer. Consequently, since all the forecast revenue from Boralex LP's sales to the two

[38] Exhibit B-13.

[39] Application paras. 155 and 159.

[40] Boralex LP response to BCUC 22.3 (Exhibit B-6).

[41] Boralex LP response to BCUC IR 22.8 (Exhibit B-6).

[42] Boralex LP response to BCUC IR 22.1 (Exhibit B-6).

[43] Ibid.

industrial customers has been credited to the revenue requirement to reduce BC Hydro's rates over the test period, Boralex LP is at risk if this revenue does not materialize either because of reduced customer load, loss of the customer altogether, or the inability or failure of Boralex LP to deliver electricity to the customers.

77. Boralex LP has not proposed a deferral account or similar mechanism to manage the non-BC Hydro load and revenue because this would have the effect of transferring all the revenue risk associated with these customers to BC Hydro. Boralex LP believes that it is reasonable that Boralex LP should be responsible for managing this risk. These are direct customers of Boralex LP and Boralex LP believes that it is appropriate that it have a direct incentive to continue to provide highly reliable service to these customers and to do what it can to retain these customers and, although there are very limited opportunities to do so at least over the test period, grow its non-BC Hydro load and revenue over the long term.[44]

78. The assumption of this risk by Boralex LP is, in Boralex LP's submission, another favourable aspect from BC Hydro's perspective of the applied-for rates for Boralex LP's service to BC Hydro. As indicated above, there is a much greater risk that the revenue from the non-BC Hydro load will be lower over the test period, rather than higher.

G. BC HYDRO RATE STRUCTURE

79. Boralex LP is seeking approval of a two-tier declining block energy charge rate structure for its service to BC Hydro. The proposed Tier 1/Tier 2 threshold is equal to the average annual amount of electricity delivered by Boralex LP to BC Hydro over the last five years of 13.1 GWh, adjusted downward in 2021 and 2020 to account for the scheduled plant outages to undertake the Penstock 2 rehabilitation work. Consequently, the Tier 1/Tier 2 threshold is 13.1 GWh in 2019 (six months) and 2020 and 11.63 GWh in 2021 and 2022.

80. In Boralex LP's submission, the proposed rate structure is appropriate and indeed very beneficial to BC Hydro. It does not impose any minimum take or fixed charge obligations on BC Hydro and therefore BC Hydro only pays for the electricity that it requires and Boralex LP actually delivers to BC Hydro. Conversely, this means that under this rate structure Boralex LP loses revenue anytime it fails or is unable to provide service to BC Hydro. This provides a very strong incentive for Boralex LP to continue to provide highly reliable service to BC Hydro.

81. In addition, the marginal cost to produce electricity at Ocean Falls is extremely low. Therefore, anything that Boralex LP can do to promote greater electricity production from the facilities reduces the average cost of production and BC Hydro's average cost of energy. Boralex LP believes that the significantly lower Tier 2 rate (starting at $50.00/MWh in 2019) should give BC Hydro an incentive

[44] Boralex LP response to BCUC 22.2 (Exhibit B-6).

to encourage greater use of electricity in Bella Bella since the proposed Tier 2 rate is lower than BC Hydro's Zone IB rates in the Bella Bella NIA (pursuant to Commission Order G-45-19, the interim approved energy charge for Zone IB is 11.32 cents/kWh, or $113.20/MWh).[45]

82. This would, for example, enable BC Hydro to implement a program to incentivize the conversion of oil-fired or propane-fired space heaters to air electric heat pumps in the Bella Bella NIA at a lower incremental costs, which would be beneficial to all stakeholders. The lower incremental energy cost might also facilitate economic development initiatives in the Bella Bella NIA by minimizing both the energy cost and environmental impacts associated with providing the electricity required for such developments.[46]

83. Boralex LP summarized and expanded on the rate design objectives for this rate design in its response to BCUC IR 54.1:

1. Recovery of Boralex LP's revenue requirement: The BC Hydro rates have been designed to recover the forecast net revenue requirement (i.e., Boralex LP's forecast gross revenue requirement less that portion of the gross revenue requirement forecast to be recovered from Boralex LP's retail and industrial customers in Ocean Falls).

2. Consistency: The BC Hydro rates are designed to be consistent with the two tier declining block energy charge rate structure that has been in place since service to BC Hydro commenced under the 1986 EPA.

3. Customer understanding and acceptance: The two-tier rate structure for BC Hydro is well understood, practical and cost effective to implement. Boralex LP believes that BC Hydro is supportive of the two-tier energy charge rate structure. The rate structure does not impose any fixed charge obligation on BC Hydro (i.e., no payment in circumstances where Boralex LP fails or is unable to provide service to BC Hydro) and the significantly lower Tier 2 rate allows BC Hydro to reduce its average cost of energy when its consumption exceeds the Tier 1/Tier 2 threshold.

4. Simplicity and freedom from controversies as to proper interpretation: The two-tier energy charge rate structure is not complex and Boralex LP does not believe there should be any controversies as to its interpretation or application. The rate structure can be adopted without the need to make rate-related modifications to the proposed terms and conditions of service for Boralex LP's service to BC Hydro, which are based on the terms and conditions of service set out in the 1986 EPA. Other rate methodologies, such as minimum take or fixed charge methodologies, would require revisions to terms and conditions of service including, for example, to address the circumstances, if any, where BC Hydro would be relieved of the minimum take or fixed charge obligation.

[45] Boralex LP response to BCUC IR 24.6 (Exhibit B-6).

[46] Application para. 157.

5. Incent high level of service reliability: Under the energy charge rate structure Boralex LP only receives payment for electricity that is actually delivered to BC Hydro. Accordingly, Boralex LP has a very strong incentive to continue to provide highly reliable service to BC Hydro in order to recover its annual revenue requirement, including its allowed return on common equity.

6. No curtailment of service to BC Hydro: Similarly, under the energy charge rate structure Boralex LP has a very strong incentive to not curtail service to BC Hydro. This is beneficial to BC Hydro and the local communities in Bella Bella and Shearwater because it enable BC Hydro to avoid operating its expensive and environmentally undesirable diesel generating station in Shearwater.

7. Encourage load growth through fuel conversion in the Bella Bella NIA: The lower Tier 2 energy charge rate should give BC Hydro an incentive to encourage the greater use of electricity in the Bella Bella NIA (e.g., through the conversion of oil-fired or propane-fired space heaters to air electric heat pumps) because, as noted in Boralex LP's response to BCUC IR 24.6, the Tier 2 rate is lower than the Zone IB rates charged by BC Hydro in the Bella Bella NIA.

8. Reduce BC Hydro's average cost of energy: Because the Tier 2 rate is significantly lower than the Tier 1 rate, BC Hydro can, unlike in the case of single energy charge or two tier inclining block energy charge rate structures, reduce its average cost of energy when its consumption exceeds the Tier 1/Tier 2 threshold.

84. To this list, Boralex LP would add rate stability. The two-tier rate structure will result in rate stability for BC Hydro because both tiers will be fixed until the end of 2022 with no deferral mechanisms operating within this period to cause an adjustment to the rates.[47]

85. As explained in the Application, the starting point under the proposed rate structure in order to establish the level of the Tier 1 and Tier 2 rates is to first fix the level of the Tier 2 rate. The Tier 2 revenue is then deducted from the net revenue requirement to determine the amount of revenue that needs to be recovered from the Tier 1 rate.

86. Although the Tier 2 rate can be set higher or lower, Boralex LP is proposing a Tier 2 rate of $50 MWh starting in 2019 and escalating at 2% per year thereafter. Fixing the Tier 2 rate at this level supports the rate design objectives above, and Boralex LP believes that BC Hydro is supportive of fixing the Tier 2 rate at this level.[48]

87. Also, Boralex LP is proposing to use a constant energy threshold between Tier 1 and Tier 2, namely 13.1 GWh for 2019 and 2020 and 11.63 GWh for 2021 and 2022 (without the penstock related outage in 2021 and 2022, the threshold would

[47] Boralex LP response to BCUC IR 3.1 (Exhibit B-6).

[48] Application para. 159.

be 13.1 GWh in 2021 and 2022). Alternatively, the Tier 1/Tier 2 threshold could be designed to match the load forecast in the Bella Bella NIA. However, this would mean that the BC Hydro load in 2021 and 2022 would need to reach the full load forecast in each of these years (i.e., 11.816 GWh in 2021 and 12.005 GWh in 2022) before BC Hydro is able to take advantage of the significantly lower Tier 2 rate.[49]

88. Boralex LP has also structured the Tier 1 rate to avoid year over year fluctuations by "levelizing" the rate. The levelized Tier 1 rate is calculated to generate the same net present value of the required Tier 1 revenue over the test period (Q3 2019 through 2022) as would be the case if unlevelized Tier 1 rates were used. The steps in the calculation are set out in paragraph 164 of the Application and is further explained in Boralex LP's response to BCUC IRs 26.2 and 55.1.[50]

H. REVENUE REQUIREMENT

89. Boralex LP's revenue requirement for the test period is set out in Table 3 to the Application. Table 3 was updated in Boralex LP's response to BCUC IR 2.1 to reflect actual Q3-Q4 data and was then further updated in the Application Update filed on April 29, 2020 to account for changes necessitated primarily due to the impacts of the novel coronavirus (COVID-19).

90. The updated revenue requirement from the Application Update, which is the basis on which the applied-for rates for Boralex LP's service to BC Hydro are now based, is as follow:

Table 3: Revenue Requirement 2019 to 2022 ($000's)

	2019	2020	2021	2022
Rate Base	$13,507	$13,904	$15,905	$19,749
Deemed Equity	$6,754	$6,952	$7,952	$9,874
Deemed Debt	$6,754	$6,952	$7,952	$9,874

	2019 (Q3-Q4)	2020	2021	2022
Return on Equity	$331	$678	$737	$882
Return on Debt	$182	$373	$406	$485
Depreciation Expense	$134	$282	$311	$368
Income Taxes	$0	$0	$0	$0
Property and School Taxes	$177	$362	$373	$384
Water Rentals	$33	$66	$68	$69
O&M	$987	$1,881	$2,347	$2,299

[49] Boralex LP response to BCUC IR 54.2.2 (Exhibit B-13).

[50] Exhibits B-6 and B-13.

Gross Revenue Requirement	$1,844	$3,642	$4,241	$4,487

Ocean Falls Retail Customer Revenue	$50	$94	$96	$98
Ocean Falls Industrial Customer Revenue	$304	$533	$503	$512
Total	$354	$627	$599	$610

Net Revenue Requirement	$1,490	$3,015	$3,642	$3,877

91. The reasons for the update to the revenue requirement are explained in the Application Update and are primarily due to the impacts of COVID-19, including the one year delay in the commencement of the Penstock 2 rehabilitation project and hiring delays for new employees.

I. RATE BASE

Opening Rate Base

92. Although the Ocean Falls Facilities have been operating for many years, prior to July 1, 2019 the rates for Boralex LP's service to BC Hydro were those set out in the 1986 EPA which were based on negotiations and not cost of service. Accordingly, for purposes of establishing cost of service based rates for BC Hydro commencing July 1, 2019, it was first necessary to establish the opening rate base for the Ocean Falls Facilities.

93. The methodology for determining the opening rate base as of January 1, 2019 is described in paragraphs 70 to 81 of the Application. The opening rate base was determined by (i) starting with the historical depreciated cost of the Ocean Falls Facilities as at December 31, 2008 as accepted by the Commission at the time of the acquisition of the facilities by Boralex LP from CCPC, (ii) adding the cost of capital additions made by Boralex LP from the time of acquisition of the facilities to December 31, 2018, and (iii) deducting depreciation expense over this period.

94. With regard to the historical depreciated cost of the Ocean Falls Facilities as of December 31, 2008, the Commission approved the acquisition of the facilities by Boralex LP from CCPC pursuant to Order and Decision G-180-08 dated December 5, 2008 and granted exemption Order G-26-10 to Boralex LP on the basis that Boralex LP's rates would be set based on the historical, depreciated cost of the Ocean Falls Facilities in the event a customer complaint cannot be resolved and the Commission decides to set cost based rates.

95. In this regard, the Commission's approval of the sale of the Ocean Falls Facilities by CCPC to Boralex LP was made conditional on CCPC providing the Commission a detailed listing of the Ocean Falls Facilities with their historic depreciated value. This information was provided by CCPC to the Commission

on January 10, 2009. As indicated in paragraph 72 of the Application, by letter dated January 20, 2009 the Commission then prepared a tabulation of the assets with a total net book value as at December 31, 2008 of $7,242,500 based on the CCPC filing, and advised that it would accept this valuation subject to confirmation by CCPC that this would be the estimated re-valued total net book value of the assets as of December 31, 2008. CCPC confirmed the Commission's tabulation by letter to the Commission dated January 21, 2009, and the purchase and sale of the facilities was subsequently completed on this basis.

96. Accordingly, the amount of $7,242,500 is the net book value (i.e., original cost less depreciation claimed by CCPC) at December 31, 2008 accepted by the Commission.

97. Table 4 of the Application sets out the tabulation of this amount by the Commission in its January 20, 2009 letter. However, the historical depreciated value of the Ocean Falls Facilities accepted by the Commission was based on broad asset categories rather than individual assets. In order to group the assets into common asset pools for depreciation purposes, Boralex LP extracted two additional asset categories to recognize the different depreciation lives applicable to (i) the powerhouse building versus the turbine-generators in the building, and (ii) the overhead versus subsea segments of the 45 km transmission line between Ocean Falls and Shearwater.[51] The adjusted categories and historic depreciated costs are set out in Table 5 of the Application. However, the total historical depreciated amount of $7,242.500 accepted by the Commission remains the same.

98. The next step in determining the opening rate base as at January 1, 2019 was to add the capital additions from January 1, 2009 to December 31, 2018.

99. Since acquiring the Ocean Falls Facilities from CCPC, Boralex LP has invested $7,625,000 in capital additions to maintain the structural and operational integrity of the facilities and to continue to provide safe, secure and reliable service to BC Hydro.

100. Details regarding the year by year capital additions between 2009 and 2018 were provided in paragraphs 76 and 77 of the Application. Additional information regarding certain of the capital additions was provided in response to information requests.[52]

101. In Boralex LP's submission, the record in this proceeding demonstrates that all of the capital expenditure made by Boralex LP during this period were reasonable and prudent and necessary in order for Boralex LP to continue to provide safe, secure and reliable service.

102. Moreover, as noted above with regard to how Boralex LP has operated and maintained the Ocean Falls generating units, since the power prices paid by BC

[51] Boralex LP responses to BCUC IRs 5.1 and 6.1.4 (Exhibit B-6).

[52] Including Boralex LP's responses to BCUC IRs 4.1 to 4.7 and 5.2 to 5.4 (Exhibit B-6) and 35.1 to 36.1 (Exhibit B-13), BC Hydro IR 3.3 (Exhibit B-7), and BCOAPO IR 33.1 (Exhibit B-8).

Hydro between 2009 and 2018 were fixed under the 1986 EPA and not determined on a cost of service basis, Boralex LP had no incentive during this period to incur costs that were not necessary in order for Borlalex LP to maintain safe, secure and reliable service.

Depreciation

103. The final step in the calculation of the opening rate base as at January 1, 2019 was to deduct depreciation expense over the period from January 1, 2009 to December 31, 2018.

104. Boralex LP has calculated depreciation expense on a straight-line basis using the depreciation rates set out in Table 7 of the Application, which are based on the estimated depreciation life of each asset category.

105. Boralex LP did not undertake a formal depreciation study. Rather, Boralex LP estimated the depreciation life for each asset category based on typical depreciation lives for similar hydroelectric, substation and distribution assets applied by other Canadian electric utilities.[53] In response to BCUC IR 34.1.1[54] Boralex LP also compared its proposed depreciation lives to the current and recommended depreciation lives for similar BC Hydro facilities set out in BC Hydro's F2020-F2021 Revenue Requirements Application. That comparison shows that Boralex LP's estimated depreciation lives are, if anything, longer the BC Hydro depreciation lives resulting in lower depreciation rates for Boralex LP.

106. Boralex LP believes that this is a reasonable approach to establishing depreciation rates for the Ocean Falls Facilities because of the very small size of the Ocean Falls asset base and the likelihood that the results of a formal depreciation study would not be materially different than the rates set out in Table 7.[55]

107. Boralex LP submits that the depreciation lives and corresponding depreciation rates set out in Table 7 of the Application are reasonable and appropriate for each of the Ocean Falls asset categories.

Forecast Capital Additions

108. Boralex LP's forecast capital additions over the test period were set out in Table 11 of the Application. Table 11 was updated in Boralex LP's updated response to BCUC IR 7.1[56] to reflect, among other things, the cost estimate for the revised penstock rehabilitation project, a change in the turbine rehabilitation work schedule, and actual 2019 capital additions (both for the full year and for Q3-Q4 2019). Table 11 was further updated in the Application Update to reflect the one year delay in the penstock rehabilitation project due to COVID-19 and a change

[53] Boralex LP responses to BCUC IRs 6.1 (Exhibit B-6) and 34.3 (Exhibit B-13).

[54] Exhibit B-13.

[55] Boralex LP response to BCUC IR 6.1.2 (Exhibit B-6).

[56] Exhibit B-9.

in the accounting treatment of the cost of power that will be purchased by Boralex LP from BC Hydro under Tariff Supplement No. 7 during the penstock shutdown period to enable Boralex LP to continue to provide service to its retail customers during this period.

109. The update forecast capital additions from Table 11 of the Application Update are as follows:

Table 11: Forecast Capital Additions (2019 to 2022) ($000's)

Project No.	Project	Q3-Q4 2019	2020	2021	2022	Total
1	Penstock Rehabilitation	$137	-	$1,069	$2,562	$3,768
2	Turbine Rehabilitation	-	$313	$268	$244	$824
3	Powerhouse Electrical	-	$67	$362	$371	$800
4	Ocean Falls Switchyard	-	$53	-	$215	$268
5	Shearwater Substation	-	$104	$288	$262	$654
6	Interconnection Line	-	$15	$200	$205	$420
7	General Plant	$37	$125	$125	$354	$641
	Total	$174	$678	$2,311	$4,212	$7,375

110. Boralex LP filed a number of third party engineering assessment and inspection reports regarding the dam, the penstock, and the powerhouse and substation electrical facilities.[57] These third party engineering reports, together with Boralex LP's own internal inspections, engineering assessments and professional judgement, support the need, timing and forecast cost of the capital projects to be undertaken during the test period. The review and approval of the projects and associated expenditures was conducted and determined through a rigorous internal budget and governance process involving site, regional and general operations managers and the President and Chief Executive Officer, the Vice President and Chief Operating Officer and the Chief Financial Officer of Boralex Inc.[58]

111. Capital cost estimates for the projects are based on a combination of industry experience, contractor quotes, supplier quotes, and Boralex LP's experience in completing capital projects at Ocean Falls. The estimates fall into the Class 3 designation as per AACE standard 17R-97 with an expected average accuracy of +30%/-15%.[59]

112. Boralex LP has provided extensive justification of the need and timing for each of the planned capital projects in the Application, in the responses to information requests from the Commission and interveners[60] and in the Application Update.

[57] Boralex LP response to BCOAPO Supplemental Information Request 6 dated December 13, 2019 (Exhibit B-4, Appendix A); Boralex LP response to BC Hydro IR 7.1.1 (Exhibit B-7); Updated BBA Technical Report Penstock 2 filed on April 29, 2020 (Exhibit B-12)]

[58] Boralex LP's responses to BC Hydro IR 2.1 (Exhibit B-7) and BCUC IR 39.1 (Exhibit B-13).

[59] Boralex LP response to BCUC IR 7.4 (Exhibit B-6).

[60] Including Boralex LP's responses to BCUC IRs 7.1 to 7.17, 8.4 and 8.5 (Exhibits B-6 and B-9) and 37.1 to 40.3 (Exhibit B-13), BC Hydro IRs 2.1 to 8.1.1 (Exhibit B-7) and 22.1 to 26.4 (Exhibit B-15)

All the projects are essential to maintain safe and reliable operation of the Ocean Falls Facilities. Boralex LP has deferred beyond the forecast period project work that it believes can reasonably be delayed without materially impacting safety or operational reliability.[61]

113. The most significant capital project is the Penstock 2 rehabilitation project. Penstock 2 is a large steel riveted 3.6 m diameter penstock that was initially installed in 1917 to serve the four generating units in the powerhouse.[62] The penstock has incurred rivet deterioration, localized corrosion pitting and metal stress over its long service life.[63] Boralex LP has actively monitored and assessed the condition of Penstock 2 since acquiring the Ocean Falls Facilities and, in consultation with its external engineering consultant BBA Engineering, has determined that it is necessary to commence rehabilitation work during the test period.[64]

114. As discussed in Boralex LP's response to BCUC IR 7.1[65], based on advice and discussions with BBA Engineering, Boralex LP has decided to rehabilitate Penstock 2 by replacing penstock sections with new sections on a staged basis, rather than undertaking the work and activities described in paragraphs 87 and 88 of the Application (i.e., conducting spot repairs and adding steel reinforcements to address localized areas of corrosion and metal fatigue, removal of internal and external corrosion debris, rehabilitating failed rivets and installation of an inner liner and applying an outer coating). This decision was reached in part based upon review of a recent rehabilitation project similar to that initially proposed for Penstock 2 on a similar size and vintage riveted penstock, which had unsatisfactory results.

115. Rehabilitating Penstock 2 with new sections will result in a penstock that is fully up to current design codes, will require less ongoing maintenance and associated costs and will have a life expectancy of 50 years (compared to 25 years for the initially proposed rehabilitation plan) which can be further extended with routine maintenance.

116. The rehabilitation project will be completed in discrete stages over several years to minimize the required shutdown window in any single year, thereby reducing the period that BC Hydro's Shearwater diesel generation station needs to be in operation. Work requiring plant shutdowns will continue to be conducted during a six week window in the spring each year (mid-April to the end of May) to align with the lightest seasonal loads in the Bella Bella NIA and Ocean Falls.

117. Boralex LP had originally intended to commence the first phase of the rehabilitation work in 2020. However, as explained in the Application Update,

[61] Boralex LP response to BCUC IR 7.2 (Exhibit B-6) and BCOAPO 34.1 (Exhibit B-13).

[62] Penstock 1 was also a 3.66 m diameter steel riveted penstock constructed in the 1920's that was used to service the mechanical pulping hydraulic turbines in the ground wood building. Penstock 1 was removed in 1999 subsequent to the closer and decommissioning of the Ocean Falls pulp and paper mill in 1980 (Application p. 11).

[63] Boralex LP response to BCUC IR 8.5 (Exhibit B-6).

[64] Boralex LP response to BCOAPO IR 38.1 (Exhibit B-16).

[65] Exhibit B-6, updated in Exhibit B-9.

due to COVID-19 Boralex LP has had to delay the commencement of the project by one year, which has the effect of delaying the subsequent stages of the project by one year as well. The forecast costs of the project are now $0 in 2020, $1,069,000 in 2021 and $2,252,000 in 2022. Project work will continue in 2023 and 2024 and an additional engineering study will be undertaken in 2021 to determine whether head gate closure improvements or a second point of closure will be required for the penstock.

118. BBA Engineering prepared an updated engineering report dated April 23, 2020 regarding the rehabilitation project that was filed separately by Boralex LP with the Application Update.[66] The BBA Report reflects its recommendation to undertake the revised project on a staged basis as described in Boralex LP's response to BCUC IR 7.1 and the one year delay in the project schedule due to COVID-19.

119. Appendix D to the BBA Report sets out a monitoring schedule and plan for Penstock 2 that Boralex LP has followed since last Fall when the initial BBA Report was prepared. Boralex LP will continue to follow this schedule and plan over the course of this year and until the entire project is completed.

120. In Boralex LP's submission, the Penstock 2 rehabilitation project has been fully justified by Boralex LP in this proceeding and the forecast cost estimates are reasonable.

121. The most significant capital expenditures beyond the test period for the long term operation of the facilities are the completion of the Penstock 2 rehabilitation project, any dam remediation work that may be needed, and ongoing capital maintenance of the 45 km transmission line between Ocean Falls and Shearwater as the structures and other line components reach end of life condition.[67] Once the projects presently underway and these future major projects have been completed, Boralex LP expects that there will be an extended period of lower annual capital expenditure requirements.[68]

AFUDC and ODC

122. None of the forecast costs of the planned capital projects over the test period include any allowance for AFUDC or capitalized overheads (ODC).

123. With regard to AFUDC, Boralex LP has not included any AFUDC in the forecast capital costs for the reasons set out in Boralex LP's response to BCUC IR 8.1[69]. By not including AFUDC, Boralex LP will bear the cost of financing the capital projects until they are transferred to rate base, and therefore has an incentive to complete the project on time and on budget.[70]

[66] Exhibit B-12.

[67] Boralex LP response to BCUC IR 39.3 (Exhibit B-13).

[68] Boralex LP response to BCUC IR 39.4 (Exhibit B-13).

[69] Exhibit B-6.

[70] Boralex LP response to BC Hydro IR 10.17 (Exhibit B-7).

124. With regard to ODC, Boralex LP agrees that it may be appropriate to allocate a portion of its operating expenditures as capitalized overhead and is amenable to doing so in the future.[71] Boralex LP proposes to address this issue in its next rate application to the Commission.

Working Capital

125. As described in paragraph 126 of the Application and Boralex LP's response to BCUC IR 9.1, Boralex LP has proposed a $400,000 working capital allowance based on approximately three months of O&M expenses. In the absence of another method, such as a formal lead-lag study, Boralex LP also endeavoured to estimate its working capital requirements by calculating the difference between its balance sheet receivables and payables.

126. In its IR 41.3 to Boralex LP, the Commission provided an extract from the Economics For Regulation by Canadian Gas Association course notes which indicates that an alternative approach, sometimes used when a lead-lag study has not been conducted, is the 45-day rule where 1/8 of a year (45 days) of a utility's O&M expenses is designated as the working capital allowance.

127. As indicated in Boralex LP's response to BCUC IR 41.3.1[72], Boralex LP believes that the use of the 45-day rule would not be unreasonable to estimate Boralex LP's working capital requirement. Based on Boralex LP's forecast O&M expenses over the test period, this would result in a working capital allowance of $262,000.

Test Period Rate Base

128. The resulting rate base for the Ocean Falls Facilities for the test period is shown in the update to Table 20 of the Application set out in the Application Update:

Table 20: Forecast 2019 to 2022 Rate Base ($000's)

	2019	2020	2021	2022
Starting Rate Base	$12,834	$13,107	$13,504	$15,505
Add: Capital Additions	$542	$678	$2,311	$4,212
Subtract: Depreciation	-$268	-$282	-$311	-$368
Ending Rate Base	$13,107	$13,504	$15,505	$19,349
Add: Working Capital	$400	$400	$400	$400
Total Rate Base	$13,507	$13,904	$15,905	$19,749

[71] Boralex LP response to BC Hydro IR 12.2.1 (Exhibit B-6).

[72] Exhibit B-13.

J. REVENUE REQUIREMENT COMPONENTS

129. The following are Boralex LP's submissions with regard to each of the components that make up the revenue requirement in each year of the test period.

Capital Structure and Rate of Return on Common Equity

130. Boralex LP has based its proposed capital structure and allowed rate of return on common equity (ROE) by reference to the benchmark utility used by the Commission to establish the capital structure and ROE for other utilities regulated by the Commission.

131. In its Stage 1 Generic Cost of Capital Decision dated May 10, 2013, the Commission found that FortisBC Energy Inc. (FEI) was the appropriate benchmark utility. In its subsequent Decision and Order G-129-16 dated August 10, 2016 regarding FEI, the Commission set FEI's common equity ratio at 38.5% and its ROE at 8.75%, and confirmed that the common equity component and ROE approved for FEI in that Decision would continue to serve as the benchmark for other utilities in British Columbia.

132. Boralex LP has assessed its business risks relative to those of FEI using a modified version of the risk matrix developed by the Commission to evaluate the overall risk of Thermal Energy Services (TES) utilities compared to the benchmark utility that is attached as Appendix E to the Commission's Stage 1 GCOC Decision. In its Stage 1 Decision, the Commission held that small utilities, other than TES utilities, can modify the matrix to facilitate a similar comparison of their own risks to those of FEI.[73]

133. Table 21 of the Application is a modified version of the Commission's risk matrix and compares the risks faced by Boralex LP with those of FEI. In all categories of risk other than fuel related risk factors associated with natural gas versus hydroelectricity, Boralex LP faces significantly higher risks than FEI.

134. While Boralex LP relies on all of the risk factors set out in Table 21 in assessing its risks relative to FEI, Boralex LP wishes to highlight the following risk factors that in Boralex LP's submission are significantly higher than the comparable risks faced by FEI:

    (a) *System performance risk*: FEI owns and operates a diversified natural gas distribution system largely in urban areas including the Lower Mainland. In contrast, Boralex LP generates, transmits and distributes electricity in a remote and isolated location and is dependent on a single non-redundant 45 km transmission line over extremely difficult and hard to access terrain that is critical to its ability to deliver electricity to the Bella Bella NIA, its primary load and revenue source.

[73] Stage 1 Generic Cost of Capital Decision dated May 10, 2013, page 101.

(b) *Operating cost risk*: Because FEI operates in largely urban areas it has ready and easy access to its distribution system facilities and ready and abundant access to the trained personnel, machinery, supplies and equipment needed to operate and maintain its facilities and respond to any system incidents that might cause any service disruptions. In contrast, the Ocean Falls Facilities are located in an isolated and remote location with an extremely harsh operating environment. There is no road access to the facilities and water access is the only reliable year-round access. The transmission line can only be accessed by water, on foot or by helicopter. This imposes much higher operating cost risks in operating and maintaining the Ocean Falls Facilities and responding to emergencies than those faced by FEI. It is also more difficult to recruit, train and retain qualified operating personnel who are willing to work in Ocean Falls, which is particularly relevant in light of the need to hire new employees to replace those who are retiring in the near future. Boralex LP has no operating cost related deferral accounts to transfer operating cost risks to BC Hydro.

(c) *Construction cost risk:* The remote and extremely harsh environment in which Boralex LP operates is significantly more challenging than that in which FEI operates. The isolated location of the facilities, where water access is the only practical means of bringing in materials, equipment and personnel for construction work, imposes significantly higher risks in forecasting, planning and executing capital projects. For example, adverse weather conditions or on-site equipment breakdowns can cause significant delays and cost increases. Boralex LP has no capital-related deferral accounts to transfer construction cost risks to BC Hydro.

(d) *Customer base and customer default risk*: FEI has a very large and economically and geographically diversified residential, commercial and industrial customer base. In contrast, Boralex LP's customer base is very small with very low diversity and slow growth. Approximately 12% of Boralex LP's gross revenue requirement comes from just two industrial customers (representing about 65% of Boralex LP's average annual return on equity of $765,000 in 2020, 2021 and 2022) who are operating in the same remote and isolated location. One customer is engaged in a politically sensitive industry (fish farming) and the other one is engaged in a new and highly speculative industry (cryptocurrency mining). The electricity sales agreements with these two customers have energy charge rate structures with no minimum take or fixed charge obligations on the part of the customer. The loss of either of these customers would have a material adverse impact on Boralex LP's ability to earn its allowed return on common equity. FEI has no equivalent single customer default risk and significantly lower overall customer related risks.

(e) *Load forecast uncertainty*: FEI faces minimal short term load forecasting risk. In contrast, Boralex LP is taking all load forecasting risk under the 100% energy charge rate structure with BC Hydro and under the electricity sales agreements with its two industrial customers. Under the two-tier declining block energy charge rate structure for BC Hydro, if the BC Hydro load in any year is less than the Tier 1/Tier 2 energy threshold

(which has been set by reference to BC Hydro's actual average historic load and not some lower level), Boralex LP loses significantly more revenue than it gains if the load happens to be greater than the threshold.

(f) *Utility size:* FEI has a very large and diversified utility business. In contrast, Boralex LP is a very small utility operating in a remote and isolated location which makes it significantly more difficult and challenging to operate and maintain its facilities and attract financing on reasonable terms and conditions. Because of its small size, any increases in Boralex LP's operating or construction costs or decreases or losses in load can have a disproportionately much higher adverse impact on Boralex LP's earnings compared to those of FEI.

135. Boralex LP's assessment of its overall risk is based on a qualitative assessment of each risk factor relative to FEI. However, Boralex LP also had regard for how certain risk factors could impact its ability to achieve its allowed return on common equity, including from (i) the loss of one or more of its industrial customers, (ii) lower than forecast sales to BC Hydro, (iii) loss of sales to its customers, particularly BC Hydro, due to an outage of the Ocean Falls Facilities, including along the 45 km transmission line from Ocean Falls to Shearwater, and (iv) higher than forecast O&M or capital costs.[74]

136. In Boralex LP's submission, Boralex LP clearly faces significantly higher overall risks than FEI. Having regard for these significantly higher risks, Boralex LP submits that the appropriate common equity ratio for Boralex LP is 50% and that the appropriate ROE risk premium over the benchmark ROE of 8.75% is 125 basis points, resulting in an ROE of 10%.

137. Boralex LP notes that its actual common equity ratio is higher, not lower, than 50%.[75] So this is not a case of a utility requesting approval of an equity ratio that is higher than the utility's actual equity ratio, which would bring into question why a higher ratio is required and appropriate if the utility has been able to successfully finance its operations with a lower equity ratio.

138. Boralex's LP's actual equity ratio is higher than 50% because (i) Boralex Inc. has needed to inject additional equity into Boralex LP to fund capital expenditures required to maintain safe, secure and reliable service since acquiring the facilities, and (ii) Boralex LP has been paying down the long term debt that was issued following the acquisition of the facilities.[76] Following the Commission's decision on the Application, Boralex LP would intend to refinance the existing debt (if cost effective to do so having regard to the make-whole provisions of the existing loan referred to in Boralex LP's response to BCUC IR 42.2) or raise additional debt, which would have the effect of reducing the equity ratio from the current level.

[74] Boralex LP response to BCUC IR 11.7 (Exhibit B-6).

[75] Boralex LP response to BCUC IR 42.1 (Exhibit B-13).

[76] Boralex LP response to BCUC IR 42.2 (Exhibit B-13).

Debt Interest Rate

139. Unlike many small utilities that do not issue debt to third party lenders, Boralex LP does have long term third party debt that was issued on an arm's length basis following its acquisition of the Ocean Falls Facilities. As outlined in paragraph 133 of the Application, the loan was made in 2011, is secured by the Ocean Falls Facilities, bears interest at a fixed rate of 6.55% per annum with monthly payments of principal and interest and matures in April 2024.

140. The 6.55% interest rate on Boralex LP's current debt is Boralex LP's actual cost of debt that will not mature until April 2024, beyond the end of the test period. However, in preparing the Application Boralex LP sought the advice of its current lender of what debt interest rate would be available to Boralex LP if it were to issue new debt on a stand-alone basis (i.e., as a stand-alone utility borrowing on a long term basis without any credit support, such as a loan guarantee, from its parent or an affiliated entity).

141. Boralex LP's current lender, who is intimately familiar with the Ocean Falls Facilities, advised Boralex LP that assuming the level and stability of Boralex LP's cash flows remain substantially the same following the Commission's approval of Boralex LP's rates for service to BC Hydro, if it were to finance the debt component of Boralex LP on stand-alone basis, the interest rate on the debt would be 5.3%.[77]

142. Having regard for the 6.55% actual rate of interest that Boralex LP is paying on its existing debt, and the advice of Boralex LP's lender on what it would cost to issue new debt to finance the debt component of Boralex LP's capital structure, Boralex LP submits that an appropriate deemed interest rate on the debt component of its capital structure is 5.5%.

143. Because Boralex LP has actually issued debt to a third party lender, this is not a case where it is necessary or appropriate to establish a deemed interest rate on the debt component of Boralex LP's capital structure by reference to the default interest rate setting mechanism adopted by the Commission in its Stage 1 and Stage 2 Generic Cost of Capital Decisions for small utilities that do not issue their own third party debt.[78]

Depreciation Expense

144. Depreciation expense over the test period has been calculated using the depreciation rates set out in Table 7 of the Application. As discussed above, Boralex LP submits that these rates are reasonable and appropriate for the Ocean Falls Facilities.

[77] Application para. 135.

[78] In its Stage 2 Generic Cost of Capital Decision the Commission stated (at page 123) that: "In reference the Stage 1 Decision, the Panel confirms that the default debt component of the capital structure is set to track a benchmark credit spread that reflects BBB or BBB(low) rated debt relative to the 10-year Government of Canada bond yield."

Income Tax Expense

145. As discussed in paragraph 140 of the Application, Boralex LP has adopted the "flow-through" methodology for calculating income expense, which Boralex LP understands is the methodology adopted by other utilities regulated by the Commission. Boralex LP has sufficient capital cost allowance to reduce cash income tax expense to zero over the 2019 to 2022 period and accordingly there is no income tax expense included in the revenue requirement over the test period.

Property and School Taxes and Water Rentals

146. Boralex LP's historic and forecast property and school taxes and provincial water rentals are as follows: [79]

	Actual						Forecast		
	2016	**2017**	**2018**	**2019 Q1-Q2**	**2019 Q3-Q4**	**2019 Total**	**2020**	**2021**	**2022**
Property and School Taxes and Water Rentals	$380,000	$388,000	$401,000	$208,203	$208,203	$416,407	$428,249	$440,433	$452,970
Water Rentals	$59,000	$60,000	$64,000	$32,500	$32,500	$65,000	$66,300	$67,626	$68,979
Credit Applied to Year	$80,000	$82,000	$85,000						
Property Taxes (Net of Credit)	**$241,000**	**$246,000**	**$252,000**	**$175,703**	**$175,703**	**$351,407**	**$361,949**	**$372,807**	**$383,991**

147. Boralex LP's property taxes increased significantly in 2019. As explained in Boralex LP's response to BCUC IR 14.1[80], the 2019 assessed value of the Ocean Falls Facilities is similar to the lower assessed value of the facilities that Boralex LP was able to obtain by appealing its 2016, 2017 and 2018 assessments (which gave rise to the credits set out in the table above). Accordingly, the increase in 2019 is not driven by an increase in assessed value but by a significant increase in the tax rate charged by the Ocean Falls Improvement District from approximately 10% in 2018 to approximately 24% in 2019 due to an increase in the District's operating budget. Unlike assessment values, increases in the District's operating budget or tax rate cannot be appealed and therefore Boralex LP has no ability to control or mitigate the property tax increase in 2019.

148. Boralex LP anticipates that property tax increases will continue over the test period and has assumed a modest 3% annual increase for forecasting purposes. Actual water rental costs were $65,000 in 2019 and Boralex LP has assumed a 2% annual increase for forecasting purposes.

[79] Boralex LP response to BCUC IR 44.1 (Exhibit B-13).

[80] Exhibit B-6.

149. Boralex LP submits that its forecasts of property and school taxes and water rental costs are reasonable.

Operating & Maintenance Expenses

150. Boralex LP's forecast O&M expenses for the test period are set out in Table 27 of the Application. Table 27 was updated in Boralex LP's updated response to BCUC IR 15.1[81] to reflect actual Q3-Q4 data and was then further updated in the Application Update. Boralex LP's historical O&M expenses for 2016, 2017 and 2018 are set out in Table 26 of the Application.

151. The updated forecast O&M expenses from Table 27 of the Application Update are as follows:

Table 27: Forecast O&M Expenses ($000's)

O&M Line Item	2019 (Q3-Q4)	2020	2021	2022
Employee Costs	-	-	-	-
Salaries and Benefits	$275	$606	$793	$776
Expenses	$77	$224	$225	$164
Recruitment	-	$5	$5	-
Training	$2	$15	$38	$46
Corporate Services	-	-	-	-
Corporate Services	$59	$157	$268	$276
Engineering and Environment	$25	$59	$61	$63
Operations Senior Management	$9	$18	$19	$19
Operations Site Management	$48	$104	$185	$191
Maintenance and Repairs	-	-	-	-
Control Systems	$166	$138	$140	$143
Machinery	$49	$35	$35	$36
Turbines-Generators	$1	$50	$51	$52
Heavy Machinery & Mobile Equipment	$17	$28	$28	$29
Dam, Buildings and Land	$44	$73	$74	$76
Oil, Fuel and BC Hydro Power	$18	$25	$77	$78

[81] Exhibit B-9.

O&M Line Item	2019 (Q3-Q4)	2020	2021	2022
Health, Safety and Environment	$24	$23	$23	$23
Insurance	$52	$105	$107	$109
Permits and Land Rights	$1	$6	$6	$6
Third Party Services	$21	$15	$15	$15
Regulatory Costs	$97	$195	$195	$195
Total O&M Expenses	$987	$1,881	$2,347	$2,299

152. Boralex LP has provided detailed explanations and justification for forecast O&M expenses in the Application, the Application Update and its responses to the information requests, including the reason for the increase in certain O&M costs over historic levels. Boralex LP submits that the forecast costs are reasonable and necessary to enable Boralex LP to continue to provide safe, secure and reliable service over the test period.

153. Most of the information requests regarding the forecast O&M cost categories were focused on two categories of costs, namely, Employee Costs and Corporate Services.

Employee Costs

154. Employee Costs are the cost of employees directly employed by Boralex LP. Boralex LP has five full time employees and four part-time workers. Of the five full time employees, four are operators and one is responsible for facility maintenance. Of the four part-time workers, one is a cleaning person, one is a carpenter, one is a machinist/welder/millwright and one is a general labourer.[82]

155. Boralex LP has provided a detailed explanation for the Employee Costs over the test period. The most significant cost increase arises due to employee retirements, the need to hire replacements and the overlapping tenure between the retiring and new operators.

156. As explained in Boralex LP's response to BCUC IR 45.1[83], given the broad range of responsibilities that the Ocean Falls operators have compared to the operators in a typical hydroelectric generation plant, the required overlap period for the new operators is approximately two years. New operators need this time to work side-by-side with the existing operators to adequately benefit from their decades of knowledge and experience. Boralex LP believes that a shorter overlap period would potentially put operational continuity and system reliability at risk.

157. Three full time employees will be retiring during or shortly after the test period: the maintenance employee will be retiring at the end of 2021, one operator will

[82] Boralex LP responses to BCOAPO IRs 10.2 and 10.3 (Exhibit B-8).

[83] Exhibit B-13.

be retiring in March 2022 and a second operator will be retiring in March 2023. A new operator was hired in January 2019 and a second operator is planned to be hired in March 2021. A new maintenance employee is planned to be hired in June 2021 to replace the current maintenance employee who will be retiring at the end of 2021.[84]

158. The Employee Costs include the cost of a one-time retiring allowance to which each employee is entitled. The maximum retiring allowance is equal to 3% of the total years worked multiplied by the employee's annual salary at the time of retirement, which in Boralex LP's submission is very reasonable and modest amount in light of the fact that these long service employees have no pensions or other retirement benefits.[85]

159. Employee cost will be lower in 2023 than the comparable costs in 2021 because the number of full time employees is forecast to be back to five after March 2023. However, the cost per employee is expected to be higher because cost of living adjustments and the set of skills required to operate a remote islanded facility like Ocean Falls are scarcer today than they were a decade or more ago when the retiring employees were recruited.[86]

Corporate Services

160. The forecast revenue requirement includes the cost of a number of corporate services provided by Boralex Inc. to Boralex LP that are required by Boralex LP to carry on its utility business and operations in Ocean Falls. Boralex LP does not have its own personnel and resources needed to provide these services and therefore relies on Boralex Inc. for these services.

161. The corporate services provided by Boralex Inc. include senior and onsite management of the operations in Ocean Falls, engineering and environmental services, and corporate or head office services, including accounting, finance, tax, legal, communications, human resources, information technology and regulatory affairs.

162. The methodology used to determine the cost of these services is based on a forecast of the amount of time spent by each Boralex Inc. department on Boralex L.P. and Ocean Falls matters in each of the test years and the hourly rate applicable to the level of service provided. Accordingly, the methodology ensures that Boralex LP only bears the appropriate cost of these services commensurate with the level of service provided.[87]

163. The methodology and process used to determine the cost of the corporate services was summarized by Boralex LP as follows:[88]

[84] Boralex LP response to BCUC IR 15.1 (Exhibit B-6) and Application Update (Exhibit B-11).

[85] Boralex LP response to BC Hydro IR 32.2 (Exhibit B-15).

[86] Boralex LP response to BCUC IR 15.2 (Exhibit B-6).

[87] Boralex LP response to BCUC IR 16.2 (Exhibit B-6).

[88] Boralex LP response to BCOAPO Supplemental Information Request 3 dated December 13, 2019 (Exhibit B-4, Appendix A).

(a) All Boralex Inc. department heads were canvassed to ascertain whether the department, and if so who in the department, provides support or services to Boralex LP on a regular basis.

(b) All individuals within each identified department who provide support or services to Boralex LP on a regular basis were then contacted to obtain (i) the nature of the support or services provided or work performed, and (ii) the estimated number of hours on an annual basis. The estimated number of hours had regard for the forecast level of activity, including the capital program to be undertaken over the test period and the regulation of the rates for Boralex LP's service to BC Hydro.

(c) An average hourly rate (including benefits) per employee category was then applied based on the salary (and benefits) of that employee category.

(d) The estimated hours by department employee were then multiplied by the applicable average hourly rates for the employee to arrive at individual employee costs.

(e) The individual employee costs within each department were then totaled to arrive at the total department cost.

(f) The total Corporate Services costs to be recovered from Boralex LP were then arrived at by totalling the individual department costs.

164. The costs of corporate services set out in Table 27 above reflect an update to the costs due to the impact of COVID-19. As set out in the Application Update, these include the delay in the hiring of an additional site supervisor (part of Site Management costs) from Q1 2020 to Q1 2021 and the delay in the hiring of a regulatory affairs person (comprising Regulatory Affairs costs) from Q1 2020 to Q4 2020.

165. The cost of Corporate Services includes the cost of an additional person responsible for providing utility regulatory support to Boralex LP now that the rates for Boralex LP's service to BC Hydro will be regulated on a cost of service basis.[89] The cost of the other Corporate Services reflect only the current level of corporate services activities provided by Boralex Inc. and do not reflect any additional workload and costs associated with rate regulation. Accordingly, without this additional regulatory person, the cost of other Corporate Services (including Accounting, Finance and Tax and Legal Services) would need to be increased to reflect the additional workload. Boralex Inc. believes that it is more efficient and cost effective to centralize all regulatory functions within the additional staff person rather than decentralizing and trying to perform these functions in each of the various departments which provide corporate services to Boralex LP.[90]

[89] Boralex LP response to BCUC IR 18.2 (Exhibit B-6).

[90] Boralex LP response to BCUC IR 47.2 (Exhibit B-13).

166. As was explained in the Application and in the responses to information requests, the historic amounts for Corporate Services that were actually charged by Boralex Inc. as shown in Table 26 of the Application reflects only a small general fee for corporate services (approximately $35,000 per annum) and an allocation of certain engineering costs. The historic amounts do not reflect the actual cost of the various services provided by Boralex Inc. to Boralex LP. Historically, Boralex Inc. did not charge Boralex LP for the full cost of the Corporate Services because Boralex Inc. owns 100% of Boralex LP and Boralex LP's rates for sales to BC Hydro were fixed under the 1986 EPA (and not determined on a utility cost of service basis). Consequently, charging for these services would have simply increased Boralex LP's costs with no corresponding increase in revenue and would have had no net financial impact on Boralex Inc.'s consolidated earnings.[91]

167. Boralex LP has provided extensive justification in the Application and in its responses to information requests regarding the nature and forecast cost of Corporate Services. In Boralex LP's submission, the nature of the corporate services provided by Boralex Inc. are necessary and appropriate in order for Boralex LP to carry on its utility business and operations at Ocean Falls and the associated costs of these services are fair and reasonable.

K. FIRST NATIONS DEFERRAL ACCOUNT

168. Boralex LP is seeking Commission approval to establish a deferral account to record any costs incurred by Boralex LP over the test period associated with its ongoing relationship building activities with the Heiltsuk Nation. Boralex LP is not seeking Commission approval of any other deferral accounts.

169. Since acquiring the Ocean Falls Facilities Boralex LP has fostered a strong working relationship with the Heiltsuk Nation and both parties wish to maintain and build on this relationship based on mutual communication, goodwill, trust and respect.

170. To this end, Boralex LP and the Heiltsuk Nation have been negotiating a confidential MOU to guide the relationship between the parties. The MOU under discussion between the parties contemplates that Boralex LP and the Heiltsuk Nation may agree to engage in specific activities that may further the parties' interests. These activities may include, for example, employment and training opportunities, contracting and other business opportunities for Heiltsuk members at or in connection with the Ocean Falls Facilities. The draft MOU also contemplates the negotiation of a benefits agreement between the parties regarding the operation of the Ocean Falls Facilities.[92]

171. The implementation of the MOU may result in Boralex LP incurring certain additional costs regarding the Ocean Falls Facilities that are not reflected in the Application. Costs associated with the implementation of the MOU would have been included in the forecast cost of service if Boralex LP was able to forecast the costs. However, as explained in Boralex LP's responses to information

[91] Boralex LP response to BCUC IR 17.4 (Exhibit B-6).

[92] Application paras. 167 and 168.

requests, Boralex LP does not have an estimated timeline for the finalization of the MOU and the nature, extent and timing of any such costs cannot be determined at this time.[93] The deferral account would therefore record any additional cost incurred by Boralex LP arising out of these activities during the test period.

172. Boralex LP is not seeking any approvals from the Commission at this time regarding the disposition of any amounts that might be recorded in deferral account during the test period.[94] Boralex LP is only seeking approval to establish the deferral account. If the account is approved, the treatment of any amounts recorded in the account, including details regarding the justification and reasonableness of the amounts, will be included in Boralex LP's next rate application to the Commission for the period beyond 2022.

L. TERMS AND CONDITIONS OF SERVICE

173. The proposed terms and conditions for Boralex LP's service to BC Hydro are attached as Appendix B to the Application. The terms and conditions are substantially the same as the terms and conditions of service approved by the Commission on an interim basis effective July 1, 2019 pursuant to Order G-143-19. A blacklined version of the proposed final terms and conditions of service, with explanatory notes, showing the changes to the interim terms and conditions of service is also included in Appendix B to the Application.[95]

174. The proposed terms and conditions of service, like the interim terms and conditions of service, are based on the terms and conditions of service set out in the 1986 EPA and therefore essentially continue the terms and conditions on which electricity has been supplied from the Ocean Falls Facilities to BC Hydro for over 30 years. There are no proposed changes to the basis on which Boralex LP will be providing service to BC Hydro over the period covered by this Application and no proposed changes to the energy charge rate structure for Boralex LP's service to BC Hydro. Accordingly, Boralex LP does not believe that any substantive changes are required to the terms and conditions of service that were established under the 1986 EPA.

175. BC Hydro did not ask Boralex LP any information requests regarding the proposed terms and conditions of service.

176. Boralex LP submits that the terms and conditions are reasonable and appropriate.

[93] Boralex LP responses to BCUC IRs 27.2 and 27.5 (Exhibit B-6).

[94] Boralex LP response to BCUC IR 27.6 (Exhibit B-6).

[95] Section 4(b) of the terms and conditions of service will need to be updated to reflect the final approved rates for Boralex LP's service to BC Hydro.

M. CONCLUSION

177. Boralex LP has been a responsible and prudent owner and operator of the Ocean Falls Facilities since it assumed ownership of the facilities in 2009.

178. Boralex LP's service to BC Hydro has been extremely reliable. Safe, secure and reliable service to BC Hydro is highly beneficial to BC Hydro, its ratepayers and the local communities. Clean renewable electricity from Boralex LP allows BC Hydro to avoid operating its expensive and environmentally undesirable diesel generating station at Shearwater.

179. Boralex LP has provided extremely reliable service to BC Hydro notwithstanding the age of the Ocean Falls Facilities and despite the remote and isolated location of the facilities and the very harsh operating environment in this part of the Province.

180. The forecast revenue requirement and proposed rates for Boralex LP's service to BC Hydro reflect the fair and reasonable costs that are necessary for Boralex LP to continue to provide safe, secure and reliable service during the test period.

181. The Application contains a number of features that are very favourable to BC Hydro. These favourable features include:

    (a) Under the proposed 100% energy charge rate structure, BC Hydro only pays for the electricity that it actually requires and that Boralex LP actually delivers. This in turn provides a very strong built-in incentive for Boralex LP to continue to provide highly reliable service to BC Hydro.

    (b) Under the two-tier declining block rate structure, BC Hydro can reduce its average cost of electricity in years when its load exceeds the Tier 1/Tier 2 threshold. The significantly lower Tier 2 rate gives BC Hydro an incentive to lower its average cost of electricity by encouraging the greater use of electricity in the Bella Bella NIA by, for example, displacing oil-fired or propane-fired space heating. This would be beneficial to all stakeholders, including the local communities.

    (c) The Tier 1/Tier 2 threshold has been set at a level based on the actual average deliveries to BC Hydro over the past five years, not some lower level, and because of the significantly lower Tier 2 rate most of the net revenue requirement is recovered from the sale of Tier 1 energy. Consequently, while BC Hydro benefits from a lower average cost of electricity if its actual load exceeds the Tier 1/Tier 2 threshold in any year, Boralex LP will lose significantly more revenue if the actual load is below the threshold than it will gain if the actual load is above the threshold.

    (d) Boralex LP, not BC Hydro, is assuming the risk that the forecast revenue from Boralex LP's retail and industrial customers will materialize over the test period. All the forecast revenue from these customers has been credited to BC Hydro and there is a much higher risk that this revenue will be less, not greater, than forecast.

(e) Apart from the proposed First Nations relationship building deferral account, there are no cost of service, load or revenue related deferral accounts that would transfer risks and costs from Boralex LP to BC Hydro and result in higher rates for BC Hydro.

(f) The terms and conditions of service for Boralex LP's service to BC Hydro continue the terms and conditions on which electricity has been successfully supplied from the Ocean Falls Facilities to BC Hydro for over 30 years. Boralex LP is not seeking to impose more onerous terms and conditions on BC Hydro.

182. The Commission should determine that the applied-for rates, terms and conditions of service and First Nations deferral account are just and reasonable.

ALL OF WHICH IS RESPECTFULY SUBMITTED this 30th day of June, 2020.

ATTACHMENT A

Hemlock Valley Electrical Services v. British Columbia (Utilities Commission)

BRITISH COLUMBIA LAW REPORTS

SECOND SERIES

Reports of Selected Cases from the Courts of British Columbia and Appeals.

[Indexed as: **Hemlock Valley Electrical Services Ltd. v. British Columbia (Utilities Commission)**]

HEMLOCK VALLEY ELECTRICAL SERVICES LTD.
v. BRITISH COLUMBIA UTILITIES COMMISSION
and ATTORNEY GENERAL OF BRITISH COLUMBIA

Court of Appeal
Hutcheon, Cumming and Hinds JJ.A.

Heard – February 12 and 13, 1992.
Judgment – March 26, 1992.

Public utilities – Rates and charges – Changes – Utilities Commission Act empowering commission to determine fair and reasonable return upon appraised value of property of regulated utilities – Commission having duty to set rates to allow opportunity to earn that return.

The appellant was a small special purpose utility which was the sole supplier of electricity to approximately 192 residential customers. In May 1990 the appellant applied to the British Columbia Utilities Commission for a rate increase of 7.32¢ per kW.h on a rate of 8.65¢ per kW.h. In July 1990 the commission allowed an interim increase of 3.7¢ per kW.h. Following a public hearing the commission approved an increase of 3.77¢ per kW.h, but declined to permit the immediate full implementation of the increase and instead directed that it be phased in by increases of 1.51¢ in July 1990, 1.51¢ in May 1990 and 0.75¢ in May 1992. The appellant brought an appeal against the phase-in provisions of the decision.

Held – Appeal allowed; matter remitted to commission.

The *Utilities Commission Act* empowers the commission to determine what is a fair and reasonable rate of return upon the appraised value of the property of the regulated utilities, but, having done so, requires the commission to set rates so as to allow recovery

of a rate which permits an opportunity to earn that return. Here, the commission correctly exercised its discretion to determine what a just and reasonable return was, but wrongly failed to permit the appellant to charge a rate which gave it an opportunity to earn that return. The balancing of interests required by the Act was performed by the commission when it settled the rate base, fixed the rate of return and determined the costs of operation allowable for rate-making purposes. In directing the three-year phase-in, the commission was not balancing interests or, if it was purporting to do so, it acted improperly. If it wished to avoid "rate shock" to the appellant's customers by a phase-in period, it would have to do so in a way which met the requirements of the Act.

Cases considered

British Columbia Electric Railway Co. v. British Columbia Public Utilities Commission, [1960] S.C.R. 837, 33 W.W.R. 97, 82 C.R.T.C. 32, 25 D.L.R. (2d) 689 – considered.

British Columbia Hydro & Power Authority v. Westcoast Transmission Co., [1981] 2 F.C. 646, 36 N.R. 33 (C.A.) [leave to appeal to S.C.C. refused 37 N.R. 540, (sub nom. *British Columbia Petroleum Corp. v. Canada (National Energy Board)*) 38 N.R. 87] – referred to.

California-Pacific Utilities Co., Re, 52 P.U.R. 3d 446 (1964) – considered.

Pacific Telephone & Telegraph Co., Re, 65 P.U.R. 3d 517 (1966) – considered.

Statutes considered

Public Utilities Act, R.S.B.C. 1948, c. 277
- s. 2(1) – referred to.
- s. 16(1) – referred to.

Utilities Commission Act, S.B.C. 1980, c. 60
- s. 65 [am. 1983, c. 10, s. 21 (Sched.)] – considered.
- s. 66(1)(*a*) – considered.
- s. 66(1)(*b*) – considered.
- s. 115 – referred to.
- s. 118 – referred to.

Water Act Amendment Act, S.B.C. 1929, c. 67 – referred to.

APPEAL from order of British Columbia Utilities Commission.

Chris W. Sanderson and *Barbara Cornish*, for appellant.
Gordon A. Fulton, for respondent B.C. Utilities Commission.
Patrick G. Foy, for respondent Attorney General of British Columbia.

(Doc. Vancouver CA013604)

March 26, 1992. The judgment of the court was delivered by

CUMMING J.A.:–

DECISION APPEALED FROM

1 This is an appeal from O. G-11-91 of the British Columbia Utilities Commission (the "commission") pronounced January 30, 1991 reaffirming the terms of O. G-77-90, made October 17, 1990, which permitted the appellant utility, Hemlock Valley Electrical Services Ltd. ("HVES"), to

increase the rate it charges for the supply of electrical services, but ordered that the rate base costs be phased in over a period of three years.

2 On March 7, 1991, pursuant to s. 115 of the *Utilities Commission Act*, S.B.C. 1980, c. 60, Toy J.A. granted leave to appeal to this court and directed that the operation of commission O. G-11-91 be stayed upon terms to which further reference will later be made.

FACTS

3 HVES, a wholly owned subsidiary of Hemlock Valley Resorts Inc., is a small, special purpose utility which is the sole supplier of electrical service to a group of approximately 192 residential customers living in a single community located around the Hemlock Valley ski hill in the lower mainland of British Columbia. HVES also provides service to the ski hill itself.

4 HVES was incorporated in 1979 and on June 20, 1980 was granted a certificate of public convenience and necessity by O. C-23-80 of the British Columbia Energy Commission, the predecessor of the present commission.

5 On November 13, 1982 HVES filed a rate application with the commission (the "1982 application"). A public hearing was held on June 7, 1983 and the commission rendered its decision on July 8, 1983 (the "1983 decision").

6 At that time HVES' operations were described as follows:

> Hemlock is a subsidiary of Hemlock Valley Recreations Ltd. ("Hemlock Recreations"), which company owns and leases land in the Hemlock Valley of the Lower Mainland of British Columbia for year-round recreational use. Hemlock provides underground electric service to residential consumers and to Hemlock Recreations for use in a ski lodge, lifts and a maintenance area; to Hemlock Property Management Ltd. for residential use on residential properties; and to Hemlock Valley Sanitary Service Ltd. for a sewer system serving the recreation area. All three companies are wholly owned subsidiaries of Hemlock Recreations.

7 In the 1983 decision the commission declined to allow HVES a return on its rate base and ordered that electrical rates be set at 11.5¢ per kW.h with a $15 per month minimum charge, effective July 1, 1983. The commission noted:

(a) the Hemlock recreational area was still in the developmental stage;

(b) the development had been materially affected by a downturn in the provincial economy;

(c) HVES had taken significant steps to reduce the cost of power and improve the reliability of service through the interconnection with B.C. Hydro;

(d) undertakings were given in the prospectus of Hemlock Valley Estates Limited indicating that a purchaser of property could expect that all services would have been completed and paid for by the developer from its own resources.

8 The commission concluded that in the circumstances of HVES a reasonable approach to rates would be based on a break-even approach between revenue and expenses.

9 In its decision of October 17, 1990 the commission said of the 1983 decision:

> It is clear that in the 1983 decision the interdependency of electric and other services with the resort enterprise at Hemlock Valley was fully understood. It is also clear that the commission felt some consternation about the 7.69 per cent negative return on rate base flowing from the 1980 decision. It was also apprehensive that the continued existence of Hemlock Valley as a going concern was being "materially affected by the downturn in the provincial economy." Moreover, it was looking at the changeover from diesel generators to a tie-line with B.C. Hydro. The change in source of power was unquestionably correct in the long-term, but it imposed an annual amortization cost of $98,840.18 for the years immediately ahead. That addition of nearly $100,000 per year materially distorted the profit and loss statement. In the circumstances, the commission, in its 1983 decision, chose to ignore return on rate base as an appropriate means of fixing fair and reasonable rates, and chose instead a pragmatic break-even approach between revenue and expenses. It also added a small allowance for contingencies. Management of the utility was evidently prepared to accept this approach.

10 By commission O. G-65-83, dated August 23, 1983, HVES was again ordered to amend its rates to reflect the sale of a portion of its electric utility plant to B.C. Hydro.

11 On July 10, 1984 HV Recreations, the parent of HVES, went into receivership. HV Recreations remained in receivership until January 15, 1987 when Skipp L.J.S.C. (as he then was) approved the sale of the assets of HV Recreations, including the HVES shares, to one Michael Robbins or his assignee. Sometime after January 15, 1987 the HVES shares were transferred to Hemlock Valley Resorts Inc. ("HV Resorts"). HV Resorts remains the sole shareholder of HVES. Throughout 1987 and 1988 there were various changes in the ownership of HV Resorts and on October 27, 1988 its shares were acquired by Mr. Joseph Peters. There has been no

change in the ownership of the assets or shares of HV Resorts since that date.

12 In 1984 and again in 1986 increased rates were approved to reflect, firstly, an increase in B.C. Hydro's water rental fees and, secondly, an increase in the cost to HVES of purchasing power from B.C. Hydro.

13 As of the spring of 1990 the rate being charged by HVES was 8.65¢ per kW.h. That rate had been in effect since September 26, 1986.

14 On May 31, 1990 HVES applied to the commission to increase its tariff rates by 7.32¢ per kW.h, an 84.6 per cent increase. The reasons given were to permit the recovery of recently approved rate increases to B.C. Hydro, forecast operating costs and a return on rate base. In the 1990 application, HVES proposed a rate base of $366,511 with a 13 per cent return on the debt component and a 15 per cent return on the equity component of that rate base.

15 Prior to a public hearing the commission, by O. G-58-90, ordered that effective July 1, 1990 HVES be allowed an interim increase of 3.7¢ per kW.h in its rates to permit the recovery of the increased cost of purchased power from B.C. Hydro and increased operating costs. The operative part of that order read:

> 1. The Rate Base costs included in the Application will not form part of the interim increase allowed in item No. 2 of this Order at this time.
>
> 2. The Commission will accept, subject to timely filing, effective July 1, 1990, an amendment to its Electric Tariff Rate Schedule incorporating an increase of 3.70 cents/kW.h over existing rates on an interim basis, with the interim increase subject to refund with interest calculated at the average prime rate of the bank with which HVES conducts its business.
>
> 3. HVES, by way of a Customer Notice, is to inform each customer, as soon as possible, of the application before the Commission, the approved interim increase and the effect on average annual billings. HVES is to provide the Commission with a copy of the Customer Notice.

16 On August 2, 1990 the commission directed that a public hearing commencing September 24, 1990 be held in respect of HVES' application of May 31, 1990 and gave directions with respect to notice of the hearing and participation by intervenors and interested persons intending to participate in the public hearing.

17 The Hemlock Valley Ratepayers Association intervened and, we were advised, played a significant role at the hearing. Its submissions covered many areas, correcting a number of statements in the application and disputing a number of forecasts. Among other things, the rate base

component in the application was opposed on the basis that the utility systems were fully paid for by the developers.

18 The commission received evidence of complaints of unsatisfactory service, inadequate HVES accounting documentation, concerns about paying for the recreational commercial venture through utility payments (commercial power use is unmetered), detailed comments on HVES' proposed operating and maintenance expenses, comparisons to residential rates in other areas, and other matters.

19 Following the public hearing on September 24 and 25, 1990, by commission O. G-77-90 dated October 17, 1990, the commission issued a decision (the "original decision") with respect to the 1990 application.

20 The operative part of O. G-77-90 reads:

> 1. The Rate Base and Revenue Requirement for the Test Period are set out in Schedules contained in the Decision.
>
> 2. The Commission will accept, subject to timely filing, amended Electric Tariff Rate Schedules which confirm to the terms of the Commission's October 17, 1990 Decision.
>
> 3. HVES is to proceed with refunds to its customers of record on and after July 1, 1990, where necessary. Such refunds are to include interest calculated as specified in O. G-51-90.
>
> 4. HVES will comply with the several directions incorporated in the Commission Decision.

I have appended as App. A to these reasons [pp. 25-30] the schedules referred to in para. 1 of the commission order.

21 By the original decision the commission declined to permit the full implementation of the approved rate increase immediately but instead directed that it be phased in by increases of 1.51¢ per kW.h effective July 1, 1990, and 1.51¢ per kW.h and 0.75¢ per kW.h effective May 1, 1991 and May 1, 1992 respectively.

22 It is this rate adjustment phase-in which is the principal focus of this appeal.

23 By letter dated November 8, 1990, HVES requested that the commission reconsider certain aspects of the original decision pursuant to s. 114 of the Act on the basis that:

(a) Reconsideration was appropriate because HVES had not been provided with an opportunity to deal with the phase-in issue in its rate application;

(b) Once the commission had determined that there was a rate base and that a 13 per cent return on it was "just and reasonable," pursuant to the Act, the commission was obliged to permit HVES an opportunity to recover sufficient revenue to capture that return.

24 On January 30, 1991, by O. G-11-91, the commission ordered that the request by HVES to vary O. G-77-90 be denied and that HVES was to proceed with refunds to customers and to comply with all other directions in that order.

25 The operative part of O. G-11-91 reads:

> NOW THEREFORE the Commission orders as follows:
>
> 1. The Request, by HVES to vary the October 17, 1990 Commission Decision and Order No. G-77-90, is denied and the Commission's Reasons for Decision is attached as Appendix A.
>
> 2. The Commission reaffirms and orders HVES to proceed with refunds to customers along with other directions incorporated in its October 17, 1990 Decision and Order No. G-77-90.

26 It is from O. G-11-91 that this appeal is taken.

GROUNDS OF APPEAL

27 As set out in the appellant's factum the grounds of appeal are:

> that the Commission erred in pronouncing Order No. G-11-91, which reaffirmed Commission Order No. G-77-90 when Order No. G-77-90 contained an error in law . . . in that the Order:
>
> (a) failed to permit HVES the opportunity to recover a portion of its rate base costs over three years notwithstanding that the Commission had determined that that portion of its rate base costs was necessary for the establishment of rates which were just and reasonable under the *Utilities Commission Act*, S.B.C. 1980, c. 60 (the "Act");
>
> (b) required a refund of monies which the Commission had determined were necessary to permit HVES an opportunity to receive a just and reasonable rate under the Act.

REASONS FOR THE DECISIONS OF THE COMMISSION

1. *Original Decision*

28 In the original decision of October 17, 1990, under the heading "Determination of Rate Base," the commission, after reviewing the 1983 decision, went on to say:

> This division of the commission considers that the 1983 decision was a practical decision to tide the enterprise at Hemlock Valley over a particularly difficult period. Sooner or later, however, longer-term prospects must be faced squarely. The tie-line has been amortized over five years. Evidence

(Exs. 14 through 21) clearly indicates that recovery of plant expenditures was anticipated through utility rates. *Therefore the commission believes that a return to more traditional rate-making practice is justified.*

It was proposed to the commission by the intervenors at the hearing that rate base should not be recognized. The cornerstone of rate base is appraised value of utility property, which is usually taken to be original cost of plant. The commission cannot, by a stroke of the pen, eliminate the appraised value of the property; to do so would be confiscation of property . . .

And concluded:

The commission has considered alternative calculations for rate base and concludes that no material difference results from any refinements which might be made. Therefore, the commission accepts the company's evidence, and finds the rate base to be $366,511 for the test period.

29 The commission then continued:

4.2 *Capital Structure*

The company currently has no viable capital structure of its own. Its financing has been by way of loans from the parent company. The applicant proposes a deemed 50/50 per cent debt/equity ratio in this application. It is a frequent practice of regulatory tribunals to use a notional capital structure. While 50 per cent equity is much higher than would be usual for utilities in general, the higher proportion of equity in this case can be considered as reasonable, bearing in mind the relative risks in the case of the company.

4.3 *Return on Rate Base*

The company has proposed a return of 13 per cent on the debt component, and 15 per cent on the equity component of the rate base. Standing alone, these figures certainly fall within a reasonable range in today's market. Nevertheless, the commission considers it essential to consider the particular circumstances of the company in this decision. While it is true that risky investments typically command higher returns, that position considers primarily the potential investors' point of view in placing funds at the utility's disposal. From the existing shareholders' point of view, the realization of an allowable rate of return depends upon the ability of management to run an efficient organization, and for external factors to favourably affect the prosperity of the company. Bearing in mind the interrelationship of the resort and utility elements at Hemlock, and the current circumstances of the utility, the commission cannot accept a return on equity for rate-making purposes of 15 per cent. *For the foregoing reasons, the commission believes that a 13 per cent return on debt and a 13 per cent return on equity are both just and reasonable within the spirit of s. 65(3) and (4) of the Act*, which states:

"(3) It is a question of fact, of which the commission is the sole judge, whether a rate is unjust or unreasonable, or whether, in any case, there is undue discrimination, preference, prejudice or disadvantage in respect of a rate of service, or whether a service is offered or furnished under substantially similar circumstances and conditions.

"(4) In this section a rate is 'unjust' or 'unreasonable' if the rate is

> "(*a*) more than a fair and reasonable charge for service of the nature and quality furnished by the utility,
>
> "(*b*) insufficient to yield a fair and reasonable compensation for the service rendered by the utility, or a fair and reasonable return on the appraised value of its property, or
>
> "(*c*) unjust and unreasonable for any other reason."

30 Under the heading "Cost of Service" the commission, over several pages, reviewed in detail various components of the cost of service which HVES estimated it would incur and for which it sought a rate sufficient to enable it to recover, and considered the objections to and criticisms of those cost components raised by the intervenors and various witnesses. It is not necessary here to review this aspect of the material in any great detail: it is sufficient to say that where the commission did not accept in full the submissions of HVES it reduced the eligible cost component by the amounts set out in the schedules to its order (see, in particular, sheet 5 of App. 1) with the result that HVES' revenue requirements, for rate-making purposes, were reduced accordingly. The commission also made a number of directions and recommendations to the company, of which the following are examples:

> *The commission directs the company to prepare and file with the commission an operating budget at the beginning of each fiscal year . . .*
>
> *The commission therefore directs that the company provide the commission with a time schedule for the completion of the work, as well as specific advice when the work is completed. In addition, the company is directed to file a copy of its preventive maintenance program by November 1, 1990,*

but these did not result in any further adjustments to the estimates of allowable and recoverable costs of service.

31 The commission then turned its attention to the question of "quality of service" and reviewed a number of complaints and dissatisfactions expressed by the intervenors. It concludes its discussion of this issue by saying:

> During the course of the hearing, the commission was impressed with the sincerity, variety and degree of expertise shown by the witnesses for the principal intervenor, the Hemlock Valley Ratepayers' Association. It is suggested to the company that consideration might well be given to drawing on this pool of talent. *The commission strongly recommends that a "utility consultation committee" be established by HVES, with members from the utility and representative ratepayers. Quarterly information meetings should serve to improve communications in the interest of the common goals of all the participants on the mountain.*

Apart from the recommendation which the commission made in this passage, nothing else was said by the commission with regard to quality of service and, most importantly, as will be noted later, no further adjustments were made to the rate base, rate of return or the allowable components of recoverable cost of service (other than those specifically referred to) by reason of any concern related to the quality of service provided by HVES to its customers.

32 The commission summarized its decision as follows:

> 7.0 DECISION SUMMARY
>
> 7.1 *Revenue Requirement*
>
> Section 44 of the *Utilities Commission Act* requires that:
>
> "44. Every public utility shall maintain its property and equipment in a condition to enable it to furnish, and it shall furnish, a service to the public that the commission considers is in all respects adequate, safe, efficient, just and reasonable."
>
> It is the duty of the commission to see that this is done. It is also the duty of the commission to ensure that the utility has sufficient revenue to enable it to perform these functions. However, it must always be satisfied that the level of funding provided for is within the company's ability to use efficaciously.
>
> *On the basis of the evidence presented, the commission has set a revenue requirement to satisfactorily meet the above objectives (refer to attached schedules).*
>
> 7.2 *Rate Adjustment Phase-In*
>
> As mentioned in s. 1.0, the application contemplated a rate increase of 84.6 per cent in the test year. The adjustments to the cost of service in this decision have mitigated some of the potential rate shock. The commission considers that a return on rate base should be allowed; however, it believes that the ratepayers should be protected from the full impact initially. In arriving at this conclusion, the commission has recognized that there was a hiatus of some seven years between applications. In addition, the future economics and the viability of the mountain are at stake.
>
> *Accordingly, the commission orders that the rate base costs be phased in over three years. The commission requires the utility to file amended rate schedules incorporating an increase of 1.51¢ per kW.h over permanent rates effective July 1, 1990, and for further increases of 1.51¢ per kW.h and 0.75¢ per kW.h effective May 1, 1991 and May 1, 1992, respectively.*

2. *Reconsideration Decision*

33 In refusing the request of HVES for reconsideration and confirming its original decision, the commission said, under the heading "Jurisdiction":

2.0 JURISDICTION

The argument made on behalf of HVES has as its essence the jurisdiction of the commission, and it is set out in the letter dated December 14, 1990.

On p. 2 of that letter, s. 65(4) of the Act is quoted in its entirety, as is s. 66(1)(*a*) and (*b*). The submission then goes on:

"The words of Section 65(1)(b) [reference should be s. 65(4)(*b*)] and Section 66(1)(b) of the Act are a clear statutory direction to the Commission on how to determine a just and reasonable rate. In our respectful submission, in the presence of clear language, the Commission may not disregard those statutory provisions and substitute its own opinion of what is just or reasonable in any given case."

It is the commission's view that the submission is flawed in that it evidently invites the commission to ignore the clear language of s. 65(4)(*a*) and (*c*), and concentrate instead only on s. 65(4)(*b*) which supports the position of HVES. The commission holds that, in fixing a rate, it must have due regard to the whole of s. 64. Section 66(1)(*b*) makes this abundantly clear:

"the Commission shall have due regard, among other things, to the fixing of a rate that is not unjust or unreasonable, within the meaning of Section 65."

34 After referring to and distinguishing the decision of the Supreme Court of Canada in *British Columbia Electric Railway Co. v. British Columbia Public Utilities Commission*, [1960] S.C.R. 837, 33 W.W.R. 97, 82 C.R.T.C. 32, 25 D.L.R. (2d) 689, the commission continued:

The point which seems to be missed is that the commission's decision of October 17, 1990 must be taken as a whole and should be read and understood as such. It is not a decision on rate of return, followed by decisions at a later time on other matters. The phase-in is an integral part of the finding on just and reasonable rates. The decision as a whole should make it abundantly clear that the commission had concerns about "the nature and quality (of service) furnished by the utility." The impact on the customers of a large percentage increase suddenly imposed was another example of an "other reason" [s. 65(4)(*c*)] to which the commission gave due regard in deciding to phase in the increase in three steps. The commission was not prepared to grant an immediate increase in the amount requested by the applicant, but granted instead a modest increase initially and set a target for an allowable rate of return which HVES could work towards, together with suggestions and commentary on how the company might improve its operation.

35 The commission then turned to the question of "rate shock" and rejected the submission of HVES with respect to the three-year phase-in of the allowed rate increase. It stated its determination as follows:

The *Utilities Commission Act* places a duty upon the commission to balance all the factors which the Act includes as matters for due regard when fixing rates. HVES has emphasized one element, namely, return on the appraised value of the utility's property in terms of typical costs of money in the financial markets. It refers, in reply to argument by HVES to "the absolute

limitation imposed by s. 65(4)(b)." The commission does not accept that any such absolute limitation applies, but is of the view that counsel for HVES, at pp. 4 and 5 [There is an error in Karen Knott's quote.] has correctly recognized the breadth of the commission's mandate.

ISSUE

36 The issue before us, simply stated, is: "was the commission right?"

DISCUSSION

37 Any discussion of the scope of the commission's rate-making powers begins, of necessity, with the seminal decision of the Supreme Court of Canada in *British Columbia Electric Railway Co. v. British Columbia Public Utilities Commission*, supra. In that case the Supreme Court had before it a legislative scheme prescribed by the *Public Utilities Act*, R.S.B.C. 1948, c. 277 (the "old Act") similar to (and here the appellant submits, identical to) the scheme found in the *Utilities Commission Act* (the "new Act"). It will, I think, be convenient to set out side by side the relevant provisions of the two statutes so that their similarities or differences may be readily apparent.

OLD ACT	NEW ACT
Interpretation.	**Discrimination in rates**
2.(1) In this Act . . .	65. (1) A public utility shall not make, demand or receive an unjust, unreasonable, unduly discriminatory or unduly preferential rate for a service furnished by it in the Province, or a rate that otherwise contravenes this Act, regulations, orders of the commission or other law.
"Unjust" and "unreasonable" as applied to rates shall be construed to include respectively injustice and unreasonableness, whether arising from the fact that rates are excessive as being more than a fair and reasonable charge for service of the nature and quality furnished by the public utility, or from the fact that rates are insufficient to yield fair compensation for the service rendered, or arising in any other manner:	(2) A public utility shall not, as to rate or service, subject any person or locality, or a particular description of traffic, to an undue prejudice or disadvantage, or extend to any person a form of agreement, a rule or a facility or privilege, unless the agreement, rule, facility or privilege is regularly and uniformly extended to all persons under substantially similar circumstances and conditions for service of the same description, and the commission may, by regulation, declare the circumstances and conditions that are substantially similar.
16. (1) In fixing any rate	
(*a*) The Commission shall consider all matters which it deems proper as affecting the rate.	
(*b*) The Commission shall have due regard, among other things, to the protection of the public from rates that are excessive as being more than a fair and	

reasonable charge for services of the nature and quality furnished by the public utility; and to giving to the public utility a fair and reasonable return upon the appraised value of the property of the public utility used, or prudently and reasonably acquired, to enable the public utility to furnish the service.

(*c*) Where the public utility furnishes more than one class of service, the Commission shall segregate the various kinds of service into distinct classes or categories of service; and for the purpose of fixing the rate to be charged for the service rendered, each distinct class or category of service shall be considered as a self-contained unit, and the rates fixed for each unit shall be such as are considered just and reasonable for that unit without regard to the rates fixed for any other unit. If it is considered by the Lieutenant-Governor in Council that the rates as so determined might be inequitable or contrary to the general public interest, the Lieutenant-Governor in Council may direct that two or more classes or categories of service shall be considered as one unit in fixing the rate.

(3) It is a question of fact, of which the commission is the sole judge, whether a rate is unjust or unreasonable, or whether, in any case, there is undue discrimination, preference, prejudice or disadvantage in respect of a rate or service, or whether a service is offered or furnished under substantially similar circumstances and conditions.

(4) In this section a rate is "unjust" or "unreasonable" if the rate is

(*a*) more than a fair and reasonable charge for service of the nature and quality furnished by the utility,

(*b*) insufficient to yield a fair and reasonable compensation for the service rendered by the utility, or a fair and reasonable return on the appraised value of its property, or

(*c*) unjust and unreasonable for any other reason.

Rates

66. (1) In fixing a rate under this Act or regulations

(*a*) the commission shall consider all matters that it considers proper and relevant affecting the rate,

(*b*) the commission shall have due regard, among other things, to the fixing of a rate that is not unjust or unreasonable, within the meaning of section 65, and

(*c*) where the public utility furnishes more than one class of service, the commission shall segregate the various kinds of service into distinct classes of service; and in fixing a rate to be charged for the particular service rendered, each distinct class of service shall be considered as a self contained

> unit, and shall fix a rate for each unit that it considers to be just and reasonable for that unit, without regard to the rates fixed for any other unit.

38 The facts giving rise to the *British Columbia Electric* case are succinctly set forth in the majority judgment of Martland J. (for himself and Cartwright and Ritchie JJ.) at pp. 850-51 of the report [S.C.R.]:

> The appellant and British Columbia Electric Company Limited (together called "the Company") are related companies and between them own and operate equipment and facilities for the transportation of persons and property by railway, trolley coach and motor buses and for the production, generation and furnishing of gas and electricity, all for the public for compensation.
>
> The Company is regulated by the Public Utilities Commission of British Columbia (called "the Commission") pursuant to the provisions of the *Public Utilities Act*.
>
> By appraisal the Commission ascertained the value of the property of the Company used, or prudently and reasonably acquired, to enable the Company to furnish its services. The appraisal was made as of December 31, 1942, and since then has been kept up to date. The appraised value is referred to as "the rate base".
>
> By Order-in-Council No. 1627, approved on July 16, 1948, the Commission was directed to consider the classes or categories of the regulated services of the Company as one unit in fixing the rates.
>
> On September 11, 1952, the Commission after public hearing made "Findings as to Rate of Return" and decided that, "until changed financial and market circumstances convince the Commission that a different rate should be applied, the Commission will in its continuing examination of the Company's operations apply the rate of 6.5%" on the rate base as a fair and reasonable rate of return for the Company. This decision remains unchanged.
>
> The Company from time to time amended its rate schedules with the consent of the Commission and filed with the Commission schedules showing the rates so established. On April 23, 1958, it applied for the consent of the Commission, under s. 17 of the *Public Utilities Act*, to file amended schedules containing increased rates for its electric service on the Mainland and on Vancouver Island. On July 28, 1958, it also applied for the consent of the Commission to file amended schedules containing increased transit fares for its transit systems in Vancouver and other Mainland areas and in Victoria and surrounding areas.
>
> Public hearings were held by the Commission and it handed down its decision with respect to the electric applications on July 14, 1958, and with respect to the transit applications on October 30, 1958.
>
> Briefly, the decisions of the Commission accepted the proposed rate schedules submitted by the Company, except that it refused to approve the proposed increases in the principal residential electric rates on the Mainland and on Vancouver Island. It directed that those rates be scaled down by approximately 25%. In its decision with respect to electric rates the Commission stated:

"The Commission has therefore consented to the filing to be effective July 15th, 1958, of all the rate schedules submitted by the Company for the Mainland and Vancouver Island, as modified and supplemented by the Company during the course of the hearings on its application, except the residential rate schedules and Mainland Rate 3035 for industrial users.

"The Commission has decided that the principal residential rate on the Mainland (Schedule 1109) and the principal residential rate on the Island (Schedule 1110 under which the principal divisions are Billing Codes 1110 and 1112) should be adjusted to yield not more than three-quarters of the additional revenue proposed. The adjustment must be applied primarily to reduce sharp changes in impact and lessen disproportionately large percentage increases in the consumption range of 60 KWH to 280 KWH per month. Comparable adjustments must also be made in some of the related special residential rates of lesser importance. Most of the relief would be given to the small residential user."

At the same time the Commission decided that further increases in the commercial and industrial rates to compensate for this reduction in the proposed residential rates would not be justified.

At p. 849 Martland J. had said:

Pursuant to the provisions of subs. (1) of s. 107 of the *Public Utilities Act* of British Columbia, R.S.B.C. 1948, c. 277, the Public Utilities Commission of that Province stated a case for the opinion of the Court of Appeal of British Columbia. Five questions were submitted for the consideration of the Court, of which the first was as follows:

"(1) (*a*) Was the Commission right in deciding as appears in the said Reasons for Decision of 14th July, 1958, that no one of the matters and things referred to in clauses (*a*) and (*b*) of subsection (1) of Section 16 of the 'Public Utilities Act' should as a matter of law be given priority over any other of those matters or things and that, if a conflict arises among these matters or things, it is the Commission's duty to act to the best of its discretion?

"(*b*) If the answer to question (1) (*a*) is 'No', what decision should the Commission have reached on the point?"

Question (1)(*a*) was answered in the affirmative. The appellant, by special leave of this Court, has appealed from that portion of the judgment of the Court of Appeal which comprises the answer given by it to question (1). The other four questions and the answers given to them are not in issue in this appeal.

39 After summarizing the facts as I have set them out from the judgment of Martland J., his Lordship continued, at pp. 852-53:

In the reasons given for its decision the Commission deals with the effect of clauses (*a*) and (*b*) of s. 16(1) and says:

"With great respect, the Commission considers that although for this purpose the statutory duty of the Commission to have due regard to all matters which the Commission deems proper as affecting the rate might without any significant inaccuracy be described as the right of the Commission, and its statutory duty to *have due regard to giving* the utility a fair and

reasonable return might without significant inaccuracy be described as the Commission's *responsibility for giving* the utility a fair and reasonable return, there is nothing in the Act to relieve the Commission in the case now before it from complying with the language of the Act and giving due regard to all those matters to which the legislature has directed the Commission to give due regard in fixing a rate. No one of those matters should, in the opinion of the Commission, be given as a matter of law priority over any other of those matters and if, as the legislature appears to have thought possible, a conflict arises among those matters, the Commission considers that it is its duty to act to the best of its discretion."

The Court of Appeal concurred in this view. The judgment of the Court, delivered by Sheppard J.A., refers to this question in the following words:

"A further inquiry is what weight should be given to the matters required to be considered by Sec. 16(1)(*b*) and particularly to the 'fair and reasonable return'. . . Although clauses (*a*) and (*b*) of Sec. 16(1) require certain matters to be considered, they do not state what weight is to be assigned by the Commission. Consequently, the Statute requires only that the Commission consider the matters falling within Sec. 16(1)(*a*), namely, 'all matters which it deems proper as affecting the rate' and those falling within Sec. 16(1)(*b*), namely, 'the protection of the public' and 'a fair and reasonable return' to the Utility. But the Statute does not require more, and does not require any weight to be given to these matters after they have been considered. Hence the weight to be assigned is outside any statutory requirement and must be a question of fact for the Commission in each instance."

40 At p. 854 he observed, "The necessity for giving a public utility fair compensation for the service which it renders appears in the definition of the words 'unjust' and 'unreasonable' in s. 2(1)" (quoted above).

41 At pp. 855-57, Martland J. said:

Section 16, the section with which we are concerned in this appeal, also deals with this matter of fairness of rates. In addition, it spells out the method by which a public utility is to obtain fair compensation for its service; i.e., by a fair and reasonable return upon its rate base, which rate base, pursuant to s. 45, the Commission can determine by appraisal.

Section 16 deals with the duties of the Commission in fixing rates. Clause (*a*) of subs. (1) states that the Commission shall consider all matters which it deems proper as affecting the rate. It confers on the Commission a discretion to determine the matters which it deems proper for consideration and it requires the Commission to consider such matters.

Clause (*b*) of subs. (1) does not use the word "consider", which is used in clause (*a*), but directs that the Commission "shall have due regard", among other things, to two specific matters. These are:

(i) The protection of the public from rates that are excessive as being more than a fair and reasonable charge for services of the nature and quality furnished by the public utility; and

(ii) To giving to the public utility a fair and reasonable return upon the appraised value of its property used or prudently and reasonably acquired to enable the public utility to furnish the service.

As I read them, the combined effect of the two clauses is that the Commission, when dealing with a rate case, has unlimited discretion as to the matters which it may consider as affecting the rate, but that it must, when actually setting the rate, meet the two requirements specifically mentioned in clause (*b*). It would appear, reading ss.8, 16 and 20 together, that the Act contemplates these two matters to be of primary importance in the fixing of rates.

In my opinion, therefore, these two factors should be given priority over any other matters which the Commission may consider under clause (*a*), or any other things to which it shall have due regard under clause (*b*), when it is fixing any rate.

The second portion of question (1)(*a*) was as to whether, in case of conflict among the matters and things referred to in clauses (*a*) and (*b*) of s. 16(1), it was the Commission's duty to act to the best of its discretion. I have already expressed my view regarding the priority as between those things specifically mentioned in clause (*b*) and the other matters or things referred to in clauses (*a*) and (*b*). This leaves the question as to possible conflict as between the two matters specifically mentioned in clause (*b*).

Clearly, as between these two matters there is no priority directed by the Act, but there is a duty imposed upon the Commission to have due regard to both of them. The rate to be imposed shall be neither excessive for the service nor insufficient to provide a fair return on the rate base. There must be a balancing of interests. In my view, however, if a public utility is providing an adequate and efficient service (as it is required to do by s. 5 of the Act), without incurring unnecessary, unreasonable or excessive costs in so doing, I cannot see how a schedule of rates, which, overall, yields less revenue than would be required to provide that rate of return on its rate base which the Commission has determined to be fair and reasonable, can be considered, overall, as being excessive. It may be that within the schedule certain rates may operate unfairly, relatively, as between different classes of service or different classes of consumers. If so, the Commission has the duty to prevent such discrimination. But this can be accomplished by adjustments of the relative impact of the various rates in the schedule without having to reduce the total revenues which the whole schedule of rates is designed to produce.

He then answered the question posed as follows:

Accordingly, it is my opinion that the answer to question (1)(*a*) should be "No". My answer to question (1)(*b*) would be that the Commission, in priority to any other matters which it may deem proper to consider under clause (*a*) and any of the other things referred to in clause (*b*) of s. 16(1), should have due regard to the two matters specifically mentioned in clause (*b*). In the present case, having decided that certain of the rates proposed by the appellant would impose an unreasonable burden upon certain classes of consumers, the Commission should permit the Company to submit alternative schedules of rates, which, while yielding approximately the same overall revenues, would eliminate the comparatively excessive impact of those classes of rates to which the Commission objected, until a rate schedule is devised which meets the requirements of clause (*b*) of s. 16(1).

42 Locke J. delivered a separate concurring judgment in which, as appears at p. 849 of the report, he agreed specifically with the answer to the second part of the question proposed by Martland J.

43 Both Mr. Sanderson for the appellant and Mr. Foy for the respondent Attorney General of British Columbia relied heavily upon the decision in the *British Columbia Electric* case, each asserting that it supported their opposing points of view.

44 Mr. Foy firstly drew attention to the passage in the judgment of Martland J. at pp. 855-56 where that learned judge focused on the fact that, in s. 16 of the old Act, cl. (*b*) of subs. (1) does not use the word "consider," which is used in cl. (*a*), but directs that the commission "shall have due regard," among other things, to two specific matters. He then pointed to the fact that, by virtue of the wording and structure of ss. 66(1)(*b*) and 65(4), and particularly by s. 65(4)(*c*), of the new Act, a third matter, namely, that a rate may be "unjust and unreasonable for any other reason," has been elevated to being not merely one of the matters which the commission "considers proper and relevant affecting the rate" (its mandate under s. 66(1)(*a*)), but to one of the now three (formerly only two) specific matters to which the commission is directed to "have due regard." Mr. Foy then referred to the statement of Martland J. at p. 856 that "there must be a balancing of interests." From this he argued that the commission, in directing the three-year phase-in of the rate adjustment to ameliorate the rate shock, was simply "balancing" the interests of HVES on the one hand and its customers on the other, and contended that, in so doing, it was correctly applying the law which prescribes its mandate. It was entitled to what it did, he said, because the commission had concerns about "the nature and quality of service furnished by the utility."

45 Mr. Foy argued that to accede to the position of HVES would be to accord to one of the specific matters to which the commission must have due regard (the matter referred to in s. 65(4)(*b*)) a priority over the other two, something which cannot be done.

46 Mr. Sanderson submitted that once the commission had settled the content of the rate base and determined a rate of return which is both just and reasonable, it cannot fix a schedule of rates which yields less revenue than would be required to provide that rate of return on its rate base. In this respect he relied upon what Martland J. said at p. 856 (above). He also referred at length to the judgment of Locke J. and drew attention firstly to this passage at p. 841:

> The real question might have been stated more clearly had it asked whether as a matter of law a duty rested upon the Commission to approve rates which would produce for the appellant a fair and reasonable return upon the appraised value of the property used or prudently and reasonably acquired by it to enable it to furnish the service described in the Act when the fact as to what constituted a fair return had previously been determined by the Commission. This is the matter to be determined.

47 Locke J., in his reasons commencing at p. 841, reviewed the legislative history of the old Act and of its predecessor, the *Water Act Amendment Act*, S.B.C. 1929, c. 67, American regulatory jurisprudence, and the common law and said at p. 846:

> In my opinion the true meaning of the relevant sections of the *Public Utilities Act* is that a utility is given a statutory right to the approval of rates which will afford to it fair compensation for the services rendered and that the quantum of that compensation is to be a fair and reasonable rate of return upon the appraised value of the property of the company referred to in s. 16(1)(*b*).

48 Locke J. continued at p. 847:

> Rates that fail to yield fair compensation for the service rendered are declared by s. 2 to be unjust and unreasonable as they were by s. 2 of the *Water Act Amendment Act* of 1929. The Commission is directed by s. 16(1)(*b*) to have due regard to fixing a rate which will give to the utility a fair and reasonable return upon the appraised value of its property used or prudently and reasonably acquired to enable it to furnish the service. It is the inclusion of the expression "shall have due regard" which has led the Commission and the Court of Appeal to conclude that this means that allowing a fair return upon the appraised value is simply one of the matters to be considered by the Commission in fixing the rate. Clearly no such interpretation could have been placed upon this expression under the provisions of the *Water Act* in view of the express provisions of s. 141C, and with great respect I think no such interpretation should be given to it in the present statute,

And at pp. 847-48:

> I can find nothing in this legislation indicating an intention on the part of the Legislature to empower the Commission to deprive the utility of its common law right to be paid fair compensation for the varying services rendered or to depart from the declared intention of the Legislature in the *Water Act Amendment Act* that such companies upon whom these obligations are imposed are entitled to have the quantum of such fair compensation determined as a fair return upon the appraised value of the properties required,

And finally, at p. 848:

> The obligation to approve rates which will produce the fair return to which the utility has been found entitled is, in my opinion, absolute, which does not mean that the obligation of the Commission to have due regard to the protection of the public, as required by s. 16(1)(*b*), is not to be discharged. It is not a question of considering priorities between "the matters and things referred

> to in Clauses (*a*) and (*b*) of subsection (1) of s. 16". The Commission is directed by s. 16(1)(*a*) to consider all matters which it deems proper as affecting the rate but that consideration is to be given in the light of the fact that the obligation to approve rates which will give a fair and reasonable return is absolute.

49 Mr. Sanderson accepted that the commission is required to have due regard to what is referred to in s. 65(4)(*c*) but submitted that, in directing the three-year phase-in of the rate adjustment with no offsetting provision to permit HVES to obtain sufficient revenue to recover the shortfall, the commission has committed the very sin which Mr. Foy charges against the utility, namely, that instead of having due regard – and giving effect – to the three specific matters set out in s. 65(4), it has accorded priority to either s. 65(4)(*a*) or (*c*) and relegated s. 65(4)(*b*) to simply "a matter to be considered."

50 Mr. Sanderson contended that if the commission was properly concerned to ameliorate the rate shock of a sharp rise in rates to be charged it could do so but only if, at the same time, it directed the filing of rate schedules which, over a reasonable period of time, would provide sufficient revenues to enable the utility to catch up and recover the shortfall. HVES, he said, is entitled to be made whole by the standards, in terms of the rate base and allowable rate of return thereon, which the commission itself fixed. It is only in this way that the commission can properly discharge its mandate and comply with the direction to have due regard to all the matters referred to in s. 65(4) without according priority to one or another of them.

51 The addition of s. 65(4)(*c*) in the Act, however, is not an *alternative* to s. 65(4)(*a*) and (*b*), but rather is an *additional* basis on which rates may be found to be unjust and unreasonable. Accordingly, while rates may be unjust or unreasonable for reasons other than those set out in s. 65(4)(*a*) and (*b*), it remains the law that if a rate is insufficient to yield a fair and reasonable return on rate base, it is necessarily "unjust and unreasonable" within the meaning of s. 65(4)(*b*).

52 Mr. Sanderson's submissions continued as follows:

53 A distinction has been drawn in the case law between regulatory systems which afford the administrative tribunal an unfettered discretion to fix rates and those which provide the tribunal with specific statutory directions as to how these rates are to be fixed: see *British Columbia Hydro & Power Authority v. Westcoast Transmission Co.*, [1981] 2 F.C. 646, 36 N.R. 33 (C.A.).

54 The current *Utilities Commission Act* is an example of the latter. Sections 65(4)(*b*) and 66(1)(*b*) amount to a statutory direction as to how the commission is to determine a just and reasonable rate. If, as posited by Martland J., a public utility is providing an adequate and efficient service, the statute is clear: a rate is unjust or unreasonable if it fails to yield a just and reasonable return on rate base. Here, while there may be room for improvement, the commission's recommendations with respect to quality of service referred to above are calculated to achieve what is desired. Accordingly, the commission has no discretion to fix rates which do not permit recovery of that return.

55 The virtually identical nature of the relevant provisions of the old Act and the new Act compel the conclusion that pursuant to the new Act, HVES is similarly given a statutory right to the approval of rates which will afford it the opportunity to earn a fair and reasonable rate of return upon the appraised value of its property. Commission O. G-77- 90 denies HVES that opportunity.

56 In my view Mr. Sanderson's submissions are sound and must be accepted.

57 The *Utilities Commission Act* empowers the commission to determine what is a fair and reasonable rate of return upon the appraised value of the property of regulated utilities, but, having done so, requires the commission to set rates so as to allow recovery of a rate which permits an opportunity to earn that return. In this case, the commission correctly exercised its discretion to determine what a just and reasonable return was, but wrongly failed to permit HVES to charge a rate which gave it an opportunity to earn that return. For this reason, it is my view that commission O. G-77-90 cannot stand, and that O. G-11-91 must fall with it.

58 With respect to Mr. Foy's able and forceful submissions they are, in my view, flawed, and for these reasons.

59 Firstly, in directing the three-year phase-in, the commission was not balancing interests or, if it was purporting to do, it acted improperly. The proper balancing of interests which the commission carried out was done and completed when it settled the rate base, fixed the rate of return and determined the costs of operation allowable for rate-making purposes. It must be remembered that the rate base itself was the subject of much contention at the public hearing and that only after the commission had considered alternative calculations for rate base did it decide to accept HVES' evidence in this regard. It must be remembered as well that HVES had proposed a rate of return of 13 per cent on the debt component

and 15 per cent on the equity component of the rate base. The commission denied HVES' request and fixed 13 per cent as the just and reasonable rate of return on both components. In addition, as can be seen from sheet 5 of the Appendix to these reasons, the commission made substantial downward adjustments to many of HVES' estimates of its costs of operation.

60 This is the balancing of interests which the commission carried out in performing its function. HVES has accepted the commission's decision in these respects. None are the subject of this appeal. Once this balancing of interests had been performed, it was the commission's duty to have due regard to the factors referred to in s. 65(4).

61 Secondly, I cannot accept Mr. Foy's contention that the three-year phase-in was the result of the commission's expressed concern over the quality of service. The analysis I have made of the original decision and of the reconsideration decision in my view refutes this contention. Alternatively, if in fact the commission decreed the three-year phase-in for this suggested reason it was wrong in law in doing so for it gave an unwarranted priority to one or another of the matters set out in s. 65(4) at the sacrifice of s. 65(4)(*b*).

62 Thirdly, Mr. Foy submitted that "rate shock" is a recognized phenomenon which has attracted a number of rate moderation plans, including rate base phase-ins, in the utility regulation field, and he referred to the following authorities: Bonbright, Danielsen and Kamerschen, *Principles of Public Utility Rates* (1988), pp. 260-64; D. Scotto, "Post-Operational Phase-in of Utility Plant: Prolonging the Inevitable" (1983), 112 Public Utilities Fortnightly, September 1, pp. 28-34; I.M. Massella, "Rate Moderation Plans – Cushioning 'Rate Shock' " (1984), 113 Public Utilities Fortnightly, February 16, pp. 52-56; *Re California-Pacific Utilities Co.*, 52 P.U.R. 3d 446 (1964); and *Re Pacific Telephone & Telegraph Co.*, 65 P.U.R. 3d 517 (1966).

63 The underlying principle of this theory of gradualism in the implementation of new rate schedules is perhaps best explained in the article by Scotto, "Post-Operational Phase-in of Utility Plant: Prolonging the Inevitable." There the author wrote at p. 28:

> In 1982 two new terms were added to the electric utility industry's lexicon: "rate shock" and "phase-in." Rate shock refers to a sudden and "substantial" increase in electric rates. The concept can be illusive because the demarcation between "substantial" and "nonsubstantial" rate increases is usually a function of local political and economic sensitivities rather than a definitive, universal percentage increase. However, a 50 per cent jolt in rates would

> generally be considered substantial – well beyond the tolerance levels of most state commissions and ratepayers. Increases in the 20 per cent to 30 per cent vicinity, though, are more ambiguous. Rate shock is really a manifestation of the dollar disparity between rate base and new generating plant investment – the construction work in progress (CWIP) account. For a number of utilities the CWIP to net plant ratio can exceed 100 per cent, necessitating a high revenue increase – a rate shock – to reflect the plan in rate base upon commercial operation. As an alternative to the conventional one-shot hike in rates, new rate-making techniques have been proposed which are designed to spread the revenue impact of new plan investment into the postoperative years – hence, the term "phase-in".
>
> Post-operational phase-in can be accomplished in a variety of ways, most of which rely on accounting adjustments to protect the integrity of reported earnings. *The basic thesis in each case is the same: Capital recovery is spread over the asset's useful life with no economic loss (at least in theory) to the utility.* (emphasis added)

64 It can be seen that the purpose of "phase-in" is two-fold: to ameliorate the shock of suddenly imposed significant rate increases and, at the same time, to protect the integrity of the utility's earnings. As the title to Mr. Scotto's article itself indicates, it is merely "prolonging the inevitable."

65 The two regulatory decisions, *Re California-Pacific Utilities Co.*, decided in 1964, and *Re Pacific Telephone & Telegraph Co.*, decided in 1966, appear to be out of step with the main stream of American regulatory jurisprudence for, like the decision of the commission under consideration here, they did not provide for any catch up so that the utility could, over time, realize its authorized rate of return. I cannot regard them as binding or even persuasive.

66 The power of the commission to phase in rates was perhaps presaged by Martland J. in the penultimate paragraph in his judgment in the *British Columbia Electric* case, where he said at p. 857:

> . . . the Commission should permit the Company to submit alternative schedules of rates, which, while yielding approximately the same overall revenues, would eliminate the comparatively excessive impact of those classes of rates to which the Commission objected, *until a rate schedule is devised which meets the requirements of clause (b) of s. 16(1).* (emphasis added)

67 What the commission did here fails to meet the requirements of the legislation.

DISPOSITION

68 In Pt. 4 of its factum, under the heading "Nature of Order Sought," the appellant seeks an order that:

(a) the decision of the British Columbia Utilities Commission, dated January 30, 1991 be quashed;

(b) that portion of the decision of the British Columbia Utilities Commission, dated October 17, 1990 requiring rates to be phased in and directing a refund be quashed;

(c) the British Columbia Utilities Commission be directed to order HVES to file new tariff schedules permitting it to recover 13% on rate base from July 1, 1990;

(d) monies held by Lawson, Lundell, Lawson & McIntosh pursuant to the order of Mr. Justice Toy of March 7, 1990 be paid to HVES;

(e) costs; and

(f) such further relief as to this Honourable Court may seem just.

69 I think the proper course for this court to adopt is to allow this appeal and to refer the matter back to the commission with the direction that it permit, or require, HVES to file new tariff schedules which will enable it to earn 13 per cent on its determined rate base from July 1, 1990.

70 If the commission considers it necessary or appropriate to ameliorate rate shock by directing the phasing in of such revised rates, it shall do so in a way which meets the requirements of s. 65(4) as set out in these reasons.

71 It will be for the commission to make an order for the appropriate disposition of the funds referred to in para. (d) above.

72 Section 118 of the Act exempts the commission from any liability for the costs of this appeal. I do not think it appropriate to order that the Attorney General, and thereby the general public, bear those costs. However, I note from para. 5.3 of the original decision and from sheet 3 of the Appendix that provision was made for the recovery, through the rates to be charged, of the sum of $35,000 for HVES' rate application costs before the commission.

73 Accordingly, I would direct that, failing agreement between the parties, HVES tax its costs for fees and disbursements of and incidental to this appeal and that the amount so determined be included in the rate application costs in the schedule.

Order accordingly.

HEMLOCK VALLEY ELECTRICAL SERVICES LTD.

UTILITY RATE BASE SCHEDULE 1		TEST YEAR APPLICATION	BCUC ADJUSTMENT	NO.	TEST YEAR ADJUSTED
ASSETS					
Structures and improvements		$5,560			$5,560
Overhead conductors and devices		44,891			44,891
UG Conductors and devices		479,504			479,504
Line transformers		90,693			90,693
PLANT IN SERVICE, opening		$620,648	$0		$620,648
Additions to plant in service		0			0
Disposals		0			0
PLANT IN SERVICE, closing		620,648	0		620,648
Add: Work in progress		0			0
		620,648	0		620,648
Less: Accumulated Depreciation		(178,677)			(178,677)
NET PLANT IN SERVICE		441,971	0		441,971
WORKING CAPITAL ALLOWANCE		0			0
RATE HEARING COSTS		0			0
CONTRIBUTIONS IN AID		(75,460)			(75,460)
UTILITY RATE BASE		$366,511	$0		$366,511
RETURN ON RATE BASE		14.01%	-1.01%		13.00%

HEMLOCK VALLEY ELECTRICAL SERVICES LTD.

UTILITY INCOME & RETURN SCHEDULE 2		TEST YEAR APPLICATION	BCUC ADJUSTMENT	NO.	TEST YEAR ADJUSTED
SALES VOLUME MWh		2,047			2,047
		==========	==========		==========
RATES					
Existing Revenue:¢/kWh		8.65	0.00		8.65
Interim Increase %		42.77%	0.00%		42.77%
Final Increase %		84.62%			43.54%
First year phase-in: ¢/KWh			1.51		1.51
Second year phase-in: ¢/kWh			1.51		1.51
Third year phase-in: ¢/kWh			0.75		0.75
Final Rate: ¢/kWh		15.97	-3.55		12.42
Interim Rate		12.35			
REVENUE					
Existing Rates		$177,066	$0		$177,066
Interim Rates		75,739			75,739
Required Increase		74,101	(72,740)		1,361
Discounts		0			0
Other Income		0			0
		----------	----------		----------
TOTAL REVENUE		326,906	(72,740)		254,166
Less: PURCHASED POWER		125,500	(15,371)	[1]	110,129
		----------	----------		----------
GROSS MARGIN		201,406	(57,369)		144,037
% excluding Other Income		61.61%	-4.94%		56.67%
Administration, Accounting and Office		68,300	(25,300)	[2]	43,000
Repairs, Maintenance and Vehicle		31,000	(11,000)	[3]	20,000

UTILITY INCOME & RETURN SCHEDULE 2		TEST YEAR APPLICATION	BCUC ADJUSTMENT	NO.	TEST YEAR ADJUSTED
Snow Removal		18,000	(18,000)	[4]	0
Depreciation		15,065			15,065
Amortization of Rate Application		10,000	1,667	[6]	11,667
OPERATING EXPENSES		142,365	(52,633)		89,732
Utility income before tax		59,041	(4,735)		54,306
INCOME TAX EXPENSE		7,693	(1,035)		6,658
EARNED RETURN		$51,348	($3,700)		$47,648
RETURN ON RATE BASE		14.01%	-1.01%		13.00%

HEMLOCK VALLEY ELECTRICAL SERVICES LTD.

INCOME TAXES SCHEDULE 3		TEST YEAR APPLICATION	BCUC ADJUSTMENT	NO.	TEST YEAR ADJUSTED
UTILITY INCOME BEFORE TAX		$59,041	($4,735)		$54,306
Deduct – Interest		(23,823)	0		(23,823)
ACCOUNTING INCOME		35,218	(4,735)		30,482
Timing differences					
Depreciation		15,065	0		15,065
Amort. of hearing costs		10,000	1,667	[6]	11,667
Amortization of Line Costs		0			0
Capital cost allowance		(15,065)			(15,065)
Amort. of contributions					0
Overhead capitalized					0
Plant removal costs					0
Rate application costs		(30,000)	(5,000)	[6]	(35,000)
		(20,000)	(3,333)		(23,333)
TAXABLE INCOME		$15,218	($8,069)		$7,149
Income tax rate – deferred		21.84%	0.00%		21.84%
Income tax rate – current		21.84%	0.00%		21.84%
Income tax expense					
– Deferred		$4,369	$728		$5,097
– Current		3,324	(1,762)		1,561
INCOME TAX EXPENSE		$7,693	($1,034)		$6,658

HEMLOCK VALLEY ELECTRICAL SERVICES LTD.

RETURN ON CAPITAL SCHEDULE 4		TEST YEAR APPLICATION	BCUC ADJUSTMENT	NO.	TEST YEAR ADJUSTED
Contribution in Aid		$0	$0		$0
proportion		.00%	0.00%		.00%
Capital Loan		$0	$0		$0
proportion		.00%	0.00%		.00%
embedded cost		.00%	0.00%		.00%
$ return		$0	$0		$0
Current Debt		$0	$0		$0
proportion		.00%	0.00%		.00%
embedded cost		.00%	0.00%		.00%
$ return		$0	$0		$0
Notional debt		$183,256	$0		$183,256
proportion		50.00%	$0		50.00%
embedded cost		13.00%	0.00%		13.00%
$ return		$23,823	$0		$23,823
Preferred shares		$0	$0		$0
proportion		.00%	0.00%		.00%
embedded costs		.00%	0.00%		.00%
$ return		$0	$0		$0
Common equity		$183,256	$0		$183,256
proportion		50.00%	0.00%		50.00%
ROE		15.02%	-2.02%	[5]	13.00%
$ return		$27,525	($3,700)		$23,824
TOTAL CAPITAL		$366,511	$0		$366,511

HEMLOCK VALLEY ELECTRICAL SERVICES LTD.

ADJUSTMENTS				
1. $15,371	Adjust BC Hydro charges for error in Application			
2. $25,300	Adjust Administration, Accounting and Office expenses to approved amount.			
3. $11,00	Adjust Repair and Maintenance expenses to approved amount.			
4. $18,000	Eliminate Snow Removal expenses.			
5. 2.02%	Adjust return on equity to 13%			
6. $5,000	Adjust Rate Hearing costs.			
	Rate Increase Phase-in consists of:	Application	Final	First Year
	Purchased Hydro	6.13	5.38	5.38
	Operating expenses	6.22	3.65	3.65
	Rate Base costs	3.62	3.39	1.13
	Total	15.97	12.42	10.16
			% Increase	17.42

ATTACHMENT B

British Columbia Electric Railway Co. Ltd. v. Public Utilities Commission of BC

BRITISH COLUMBIA ELECTRIC RAILWAY CO. LTD. ..... APPELLANT;

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*May 4, 5, 6
Oct. 4

AND

THE PUBLIC UTILITIES COMMISSION OF BRITISH COLUMBIA, BRITISH COLUMBIA LUMBER MANUFACTURERS' ASSOCIATION, THE CORPORATION OF THE CITY OF VICTORIA, THE CORPORATION OF THE DISTRICT OF OAK BAY, THE CORPORATION OF THE DISTRICT OF SAANICH, CORPORATION OF THE TOWNSHIP OF ESQUIMALT AND CITY OF VANCOUVER ..... RESPONDENTS.

ON APPEAL FROM THE COURT OF APPEAL FOR BRITISH COLUMBIA

Public utilities—Case stated by Public Utilities Commission—Matters to be considered by Commission in changing rates—Order of priority to be given to factors considered—The Public Utilities Act, R.S.B.C. 1948, c. 277, s. 16(1)(a) and (b).

*PRESENT: Kerwin C.J. and Locke, Cartwright, Martland and Ritchie JJ.

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B.C. ELECTRIC RAILWAY CO. LTD. v. PUBLIC UTILITIES COMMISSION OF B.C. *et al.*

The first of a series of questions submitted for the consideration of the Court of Appeal for British Columbia, in a case stated for the opinion of the Court, asked if the Public Utilities Commission of that Province was right in deciding "that no one of the matters and things referred to in clauses (*a*) and (*b*) of subsection (1) of Section 16 of the "Public Utilities Act" should as a matter of law be given priority over any other of those matters or things and that, if a conflict arises among these matters or things, it is the Commission's duty to act to the best of its discretion."

The question was answered in the affirmative. The appellant appealed from that portion of the judgment of the Court of Appeal which comprised this answer.

Held (Kerwin C.J. *dissenting*): The appeal should be allowed.

Per Locke J.: There is an absolute obligation on the part of the Commission on the application of the utility to approve rates which will produce the fair return to which the utility has been found entitled, and the obligation to have due regard to the protection of the public is also to be discharged. It is not a question of considering priorities between "the matters and things referred to in clauses (*a*) and (*b*) of subsection (1) of s. 16", but consideration of these matters is to be given by the Commission in the light of the fact that the obligation to approve rates which will give a fair and reasonable return is absolute.

Per Cartwright, Martland and Ritchie JJ.: The combined effect of the two clauses referred to is that the Commission, when dealing with a rate case, has unlimited discretion as to the matters which it may consider as affecting the rate, but it must when actually setting the rate, meet the requirements specifically mentioned in clause (*b*), i.e., the rate to be imposed should be neither excessive for the service nor insufficient to provide a fair return on the rate base. These two factors should be given priority over any other matters which the Commission may consider.

Although there is no priority directed by the Act as between these two matters, there is a duty imposed on the Commission to have due regard to both of them, and accordingly there must be a balancing of the interests concerned.

Per Kerwin C.J., *dissenting*: The statute does not require that any weight be given to the matters and things referred to in the two clauses after they have been considered, and therefore the weight to be assigned is a question of fact for the Commission to decide in each instance.

APPEAL from a portion of a judgment of the Court of Appeal for British Columbia[1], comprising the answer to the first of five questions submitted to it by the Public Utilities Commission. Appeal allowed, Kerwin C.J. dissenting.

J. W. de B. Farris, Q.C., A. Bruce Robertson, Q.C., and *R. R. Dodd*, for the appellant;

[1] (1959), 29 W.W.R. 533.

J. A. Clark, Q.C., for The Public Utilities Commission of British Columbia, respondent;

T. P. O'Grady, for The Corporation of The City of Victoria, The Corporation of The District of Oak Bay, The Corporation of the District of Saanich and Corporation of The Township of Esquimalt, respondents;

R. K. Baker, for City of Vancouver, respondent.

THE CHIEF JUSTICE (*dissenting*):—Pursuant to s. 107 of the *Public Utilities Act* of British Columbia, R.S.B.C. 1948, c. 277, the Public Utilities Commission stated a case for the opinion of the Court of Appeal for that Province. The case was stated in respect of five questions but we are concerned only with Question 1 as, by order of this Court, British Columbia Electric Railway Company, Limited was granted leave to appeal only from that portion of the judgment of the Court of Appeal comprising the answer given thereto. That question is as follows:

1. (*a*) Was the Commission right in deciding as appears in the said Reasons for Decision of 14th July, 1958, that no one of the matters and things referred to in clauses (*a*) and (*b*) of subsection (1) of Section 16 of the "Public Utilities Act" should as a matter of law be given priority over any other of those matters or things and that, if a conflict arises among these matters or things, it is the Commission's duty to act to the best of its discretion?

(*b*) If the answer to question (1) (*a*) is "No", what decision should the Commission have reached on the point?

The Court's answer to Question 1 reads:

The Commission was right in deciding as appears in its Reasons for Decision of 14th July, 1958 that no one of the matters and things referred to in clauses (*a*) and (*b*) of subsection (1) of Section 16 of the Public Utilities Act R.S.B.C. 1948, chapter 277 should as a matter of law be given priority over any other of those matters or things and that, if a conflict arises among these matters or things, it is the Commission's duty to act to the best of its discretion.

At the conclusion of the argument the judgment of the Court of Appeal appeared to me to be correct and further consideration has confirmed me in that view. Reasons were given by Sheppard J.A. on behalf of himself and the other four members of the Court who heard the argument on the

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Kerwin C.J.

stated case. I adopt all that he said and would have nothing to add were it not for an argument presented on behalf of the appellant. Section 16(1)(*a*) and (*b*) read as follows:

16. (1) In fixing any rate:—

(*a*) The Commission shall consider all matters which it deems proper as affecting the rate:

(*b*) The Commission shall have due regard, among other things, to the protection of the public from rates that are excessive as being more than a fair and reasonable charge for services of the nature and quality furnished by the public utility; and to giving to the public utility a fair and reasonable return upon the appraised value of the property of the public utility used, or prudently and reasonably acquired, to enable the public utility to furnish the service:

Mr. Farris submitted that the Court of Appeal had not taken into consideration the words in (1)(*b*) "The Commission shall have due regard.....and to giving to the public utility a fair and reasonable return upon the appraised value of the property of the public utility used, or prudently and reasonably acquired, to enable the public utility to furnish the service:". However, I am satisfied upon a review of the reasons of Sheppard J.A., relevant to Question 1, and particularly of the extract transcribed below, which is the substance of his reasoning upon the matter, that he did consider and apply these words. The extract reads:

A further inquiry is what weight should be given to the matters required to be considered by Sec. 16 (1) (*b*) and particularly to the "fair and reasonable return". Under Sec. 16 (1) (*b*), the Commission is required to consider "the protection of the public" and the "giving to the public utility a fair and reasonable return". Although clauses (*a*) and (*b*) of Sec. 16 (1) require certain matters to be considered, they do not state what weight is to be assigned by the Commission. Consequently, the Statute requires only that the Commission consider the matters falling within Sec. 16 (1) (*a*), namely, "all matters which it deems proper as affecting the rate" and those falling within Sec. 16 (1) (*b*), namely, "the protection of the public" and "a fair and reasonable return" to the Utility. But the Statute does not require more, and does not require any weight to be given to these matters after they have been considered. Hence the weight to be assigned is outside any statutory requirement and must be a question of fact for the Commission in each instance.

Furthermore, as Mr. Clark pointed out, the Commission when dealing with the electric rates applications, had, under heading "III.—A Fair Return", discussed that subject; and that in their reasons for decision with reference to the transit fares applications the Commission speaks "of the misunderstanding which arose from the recent decision on

electric rates"; and that later, in the same paragraph, they said: "The 6.5% rate remains the standard of the fair and reasonable return to which the Commission has due regard".

The appeal should be dismissed but there should be no costs.

LOCKE J.:—The sections of the *Public Utilities Act*, R.S.B.C. 1948, c. 277, which must be considered in deciding the first question are quoted in the reasons of my brother Martland which I have had the advantage of reading.

The real question might have been stated more clearly had it asked whether as a matter of law a duty rested upon the Commission to approve rates which would produce for the appellant a fair and reasonable return upon the appraised value of the property used or prudently and reasonably acquired by it to enable it to furnish the service described in the Act when the fact as to what constituted a fair return had previously been determined by the Commission. This is the matter to be determined.

Some assistance in interpreting the sections of the Act is to be obtained by an examination of the earlier legislation dealing with the control of rates charged for electrical power in British Columbia.

The first statutory provision dealing with the matter appears in the *Water Act Amendment Act* of 1929 which appeared as c. 67 of the statutes of that year. This Act provided for the control of such rates and imposed upon a power company producing electrical energy by water power the duty of supplying electrical energy to the public in the manner defined. Power companies were required to file schedules of their tolls with the Water Board constituted under the *Water Act*, R.S.B.C. 1924, c. 271.

"Unjust and unreasonable" as applied to tolls was declared to include injustice and unreasonableness, whether arising from the fact that the tolls were insufficient to yield fair compensation for the service rendered or from the fact that they were excessive as being more than a fair and reasonable charge for service of the nature and quality furnished.

Section 141B authorized the Board upon the complaint of any person interested that a toll charge was unjust, unreasonable or unduly discriminatory to enquire into the matter,

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to disallow any rate found to be excessive, and to fix the tolls to be charged by the power company for its service or respecting the improvement of the service in such manner as the Board considered just and reasonable.

Section 141C read:

> Every power company shall be entitled to a fair return on the value of all property acquired by it and used in providing service to the public of the nature and kind furnished by such power company or reasonably held by such power company for use in such service and the Board in determining any toll shall have due regard to that principle.

Section 141D read in part:

> In considering any complaint and making any order respecting the tolls to be charged by any power company the Board shall have due regard, among other things, to allowing the company a fair return upon the value of the property of the company referred to in Clause 141C and to the protection of the public from tolls that are excessive as being more than a fair and reasonable charge for services of the nature and quality furnished by the company.

These amendments to the *Water Act* appeared as ss. 138 to 157 in the Revision of the Statutes of 1936 and these sections were repealed when the first *Public Utilities Act* was passed by the Legislature, c. 47 of the statutes of 1938.

It will be seen by an examination of the *Public Utilities Act* that in large measure the language of the amendments to the *Water Act* made in 1929 was adopted. The definition of the terms "unjust" and "unreasonable", which appeared in the 1929 amendment as part of s. 2, was reproduced in s. 2 of the Act of 1938. The prohibition against levying any unjust and unreasonable, unduly discriminatory or unduly preferential rate appearing as s. 8 of the *Public Utilities Act* merely expresses in slightly different terms the prohibition contained in s. 141B. The expression "shall have due regard" which appears in s. 16(1)(*b*) of the *Public Utilities Act* was apparently taken from ss. 141C and D.

The *Public Utilities Act,* however, did not, when first enacted, and does not now contain any section which declares in express terms, as did s. 141C of the *Water Act Amendment Act,* that the power company shall be entitled to a fair return on the value of its property. Had the present Act contained such a provision it appears to me to be perfectly clear that the answer to be made to the first question should differ from that given by the Court of Appeal.

Whether its omission affects the matter is to be determined.

As it has been pointed out, the utility in the present matter is required by the Act to maintain its property in such condition as to enable it to supply an adequate service to the public and to furnish that service to all persons who may be reasonably entitled thereto without discrimination and without delay. It may not discontinue its operations without the permission of the Public Utilities Commission. The utility has, so far as we are informed, a monopoly on the sale of electrical energy in the Cities of Vancouver and Victoria and in my opinion at common law the duty thus cast upon it by statute would have entitled it to be paid fair and reasonable charges for the services rendered in the absence of any statutory provision for such payment.

I consider that, in this respect, the position of such a utility would be similar to that of a common carrier upon whom is imposed as a matter of law the duty of transporting goods tendered to him for transport at fair and reasonable rates. This has been so from very early times. In *Bastard v. Bastard*[1], in an action against a common carrier in the Court of King's Bench for the loss of a box delivered to him for carriage, in delivering judgment for the plaintiff it was said that, while there was no particular agreement as to the amount to be paid for the carriage, "then the carrier might have a *quantum meruit* for his hire".

In *Great Western Railway v. Sutton*[2], Blackburn J. said in part:

> The obligation which the common law imposed upon him was to accept and carry all goods delivered to him for carriage according to his profession (unless he had some reasonable excuse for not doing so) on being paid a reasonable compensation for so doing.

The result of the authorities appears to me to be correctly summarized in Browne's Law of Carriers, at p. 42, where it is said:

> We have already seen that the law imposes very onerous duties, and very considerable risks, upon a person who is designated a common carrier. As to his duty, he is bound by law to undertake the carriage of goods. Another man is free from any such duty until he has entered into a special agreement; but the law holds that the common carrier, by the very fact of his trade and business, has, on his side, entered into an agreement with the public to carry goods, which becomes at once a complete and binding contract when any person brings him the goods,

[1] (1679), 2 Show. 81, 89 E.R. 807.
[2] (1869), L.R. 4 H.L. 226 at 237, 38 L.J Ex. 177.

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and makes the request that he should carry them to a certain person or place. To make such a contract binding upon him as a common carrier, it is not necessary that a specific sum of money should be promised or agreed upon; but where that is not the case, there is an implied undertaking upon the part of the bailor that the remuneration shall be reasonable.

The *Water Act Amendment Act* of 1929 appears to have followed closely the form of public utilities legislation in certain of the United States. There had been statutes of this nature in force in various parts of the Union for a considerable time prior to the year 1929.

I do not find that the American statutes generally declared in terms as did s. 141C of the *Water Act Amendment Act* that a power company providing service to the public should be entitled to a fair return on the value of all property acquired by it and used in providing service to the public. This method, however, of establishing a fair and reasonable rate would appear to have been followed universally.

The authorities in the American cases are to be found summarized in Nichols—Ruling Principles of Utility Regulation, at p. 49—where a passage from the judgment of the Supreme Court of the United States in *Bluefield Water Works & Improvement Co. v. West Virginia Public Service Commission*[1] is quoted reading:

> Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the service are unjust, unreasonable, and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment. This is so well settled by numerous decisions of this court that citation of the cases is scarcely necessary.

In *New Jersey Public Utility Commissioners v. New York Telephone Company*[2], Butler J. said:

> The just compensation safeguarded to the utility by the Fourteenth Amendment is a reasonable return on the value of the property used at the time that it is being used for public service. And rates not sufficient to yield that return are confiscatory.

While without the provision made in s. 141C of the *Water Act Amendment Act* a power company compelled by the amendment to furnish electrical service on demand

[1] (1923), 262 U.S. 679.

[2] (1925), 271 U.S. 23 at 31.

upon the conditions prescribed would in my opinion have been entitled to a fair and reasonable payment for such service, the Legislature, by s. 141C, defined the manner in which fair and reasonable rates should be established.

As I have said, the *Public Utilities Act* does not contain any provision which in terms declares the right of the utility to a fair return on the value of its property. It does, however, by the definition of the terms "unjust" and "unreasonable" adopted from the *Water Act Amendment Act* declare that these expressions include rates that are insufficient to yield fair compensation for the service rendered, and the Public Utilities Commission in the present matter have interpreted this in its context as indicating the yardstick to be used in determining the fair and reasonable return to which the appellant was entitled.

Under the powers given to the Commission by s. 45 of the Act the value of the property of the appellant used, or prudently or reasonably acquired to enable the company to furnish its services was determined as at December 31st, 1942, and since then has been kept up to date. On September 11th, 1952, the Commission, after public hearings, decided that until some change in the financial and market circumstances convinced the Commission that a different rate should be applied, the Commission would apply the rate of 6.5 per cent. on the rate base as a fair and reasonable rate of return for the company.

That decision remains unchanged and is not questioned by anyone in these proceedings.

In interpreting the statute, the position at common law of the utility after the repeal of the sections of the *Water Act* must be considered. Had the statute imposed upon the appellant the obligation to furnish service of the natures defined upon demand, without more, it would have been entitled as a matter of law to recover from a person demanding service reasonable and fair compensation. It will not in my opinion be presumed that it was the intention of the Legislature to deprive a utility of that common law right.

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In *Colonial Sugar Refining Company v. Melbourne Harbour Trust Commissioners*[1], the Judicial Committee said:

> In considering the construction and effect of this Act the Board is guided by the well known principle that a statute should not be held to take away private rights of property without compensation, unless the intention to do so is expressed in clear and unambiguous terms.

In Maxwell on Statutes, 10th ed., at p. 286, the authorities are thus summarized:

> Proprietary rights should not be held to be taken away by Parliament without provision for compensation unless the legislature has so provided in clear terms. It is presumed, where the objects of the Act do not obviously imply such an intention, that the legislature does not desire to confiscate the property or to encroach upon the right of persons, and it is therefore expected that, if such be its intention, it will manifest it plainly, if not in express words at least by clear implication and beyond reasonable doubt.

Subsection 6 of s. 23 of the *Interpretation Act*, R.S.B.C. 1948, c. 1, directs that every Act shall receive such fair, large and liberal construction and interpretation as will best ensure the attainment of the object of the Act. In my opinion the true meaning of the relevant sections of the *Public Utilities Act* is that a utility is given a statutory right to the approval of rates which will afford to it fair compensation for the services rendered and that the quantum of that compensation is to be a fair and reasonable rate of return upon the appraised value of the property of the company referred to in s. 16(1)(*b*).

The appellant in addition to the sale of electrical energy operates a public transportation system and sells gas and by an Order-in-Council made under the provisions of s. 15(1)(*c*) of the Statutes of 1938 it was directed that these three categories of service should be considered as one unit in fixing the rates. In the reasons delivered by the Commission upon the application to increase the rates for electricity, it is said that the appellant has never earned the approved rate of return and that the rates proposed by it, and which were not approved, would not enable it to do so even in respect of the electrical system alone.

[1] [1927] A.C. 343 at 359, 96 L.J.P.C. 74.

Rates that fail to yield fair compensation for the service rendered are declared by s. 2 to be unjust and unreasonable as they were by s. 2 of the *Water Act Amendment Act* of 1929. The Commission is directed by s. 16(1)(*b*) to have due regard to fixing a rate which will give to the utility a fair and reasonable return upon the appraised value of its property used or prudently and reasonably acquired to enable it to furnish the service. It is the inclusion of the expression "shall have due regard" which has led the Commission and the Court of Appeal to conclude that this means that allowing a fair return upon the appraised value is simply one of the matters to be considered by the Commission in fixing the rate. Clearly no such interpretation could have been placed upon this expression under the provisions of the *Water Act* in view of the express provisions of s. 141C, and with great respect I think no such interpretation should be given to it in the present statute.

The fair compensation referred to in s. 2 of the *Water Act Amendment Act* of 1929 referred, and could only refer, to an aggregate produced by tolls sufficient to yield to the power company the fair return on the value of its property to which s. 141C declared it was entitled. The fair compensation referred to in s. 2 of the *Public Utilities Act* is in its context, in my opinion, to be construed in the same manner. The Order of the Commission of September 11th, 1952, determined what that compensation should be. The rates to be put into force to yield such fair compensation, which, at least in the case of electricity, vary in accordance with the use to which it is put and the quantities purchased, are matters to be determined by the Commission. The direction to the Commission in s. 16(1)(*b*) to have due regard to the protection of the public from rates that are excessive as being more than a fair and reasonable charge for the services requires it, in my opinion, to approve rates which are in its judgment fair and reasonable having in mind the purpose for which the electricity is used, the quantities purchased and such other matters as it considers justify the approval of rates which differ for different users.

I can find nothing in this legislation indicating an intention on the part of the Legislature to empower the Commission to deprive the utility of its common law right to be paid fair compensation for the varying services rendered or

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to depart from the declared intention of the Legislature in the *Water Act Amendment Act* that such companies upon whom these obligations are imposed are entitled to have the quantum of such fair compensation determined as a fair return upon the appraised value of the properties required.

I do not think it is possible to define what constitutes a fair return upon the property of utilities in a manner applicable to all cases or that it is expedient to attempt to do so. It is a continuing obligation that rests upon such a utility to provide what the Commission regards as adequate service in supplying not only electricity but transportation and gas, to maintain its properties in a satisfactory state to render adequate service and to provide extensions to these services when, in the opinion of the Commission, such are necessary. In coming to its conclusion as to what constituted a fair return to be allowed to the appellant these matters as well as the undoubted fact that the earnings must be sufficient, if the company was to discharge these statutory duties, to enable it to pay reasonable dividends and attract capital, either by the sale of shares or securities, were of necessity considered. Once that decision was made it was, in my opinion, the duty of the Commission imposed by the statute to approve rates which would enable the company to earn such a return or such lesser return as it might decide to ask. As the reasons delivered by the Commission show, the present appellant did not ask the approval of rates which would yield a return of 6.5 per cent. to which it was entitled under the Order of the Board.

I do not consider that Question (1) can be answered by a simple affirmative or negative. The obligation to approve rates which will produce the fair return to which the utility has been found entitled is, in my opinion, absolute, which does not mean that the obligation of the Commission to have due regard to the protection of the public, as required by s. 16(1)(*b*), is not to be discharged. It is not a question of considering priorities between "the matters and things referred to in Clauses (*a*) and (*b*) of subsection (1) of s. 16". The Commission is directed by s. 16(1)(*a*) to consider all matters which it deems proper as affecting the rate but that consideration is to be given in the light of the fact that the obligation to approve rates which will give a fair and reasonable return is absolute.

In my opinion the answer to be made to Question (1)(*a*) is that the Commission was wrong in deciding that it was not required to approve rates which in the aggregate would produce for the utility the fair return which by its order of September 11, 1952, the Commission found it to be entitled or such lower rates as the utility might submit for approval. The duty of the Commission to have due regard to the protection of the public from excessive rates referred to in the first four lines of s. 16(1)(*b*) refers to the approval of rates according to the use to be made by and the quantities supplied to those to whom the service is rendered.

The second part of Question (1) reads:

> If the answer to (1)(*a*) is "No", what decision should the Commission have reached on the point?

As to this I agree with the answer proposed by my brother Martland.

I would allow this appeal but make no order as to costs.

The judgment of Cartwright, Martland and Ritchie JJ. was delivered by

MARTLAND J.:—Pursuant to the provisions of subs. (1) of s. 107 of the *Public Utilities Act* of British Columbia, R.S.B.C. 1948, c. 277, the Public Utilities Commission of that Province stated a case for the opinion of the Court of Appeal of British Columbia. Five questions were submitted for the consideration of the Court, of which the first was as follows:

> (1) (*a*) Was the Commission right in deciding as appears in the said Reasons for Decision of 14th July, 1958, that no one of the matters and things referred to in clauses (*a*) and (*b*) of subsection (1) of Section 16 of the "Public Utilities Act" should as a matter of law be given priority over any other of those matters or things and that, if a conflict arises among these matters or things, it is the Commission's duty to act to the best of its discretion?
>
> (*b*) If the answer to question (1) (*a*) is "No", what decision should the Commission have reached on the point?

Question (1)(*a*) was answered in the affirmative. The appellant, by special leave of this Court, has appealed from that portion of the judgment of the Court of Appeal which comprises the answer given by it to question (1). The other four questions and the answers given to them are not in issue in this appeal.

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The relevant circumstances involved are contained in the case stated by the Public Utilities Commission and are as follows:

The appellant and British Columbia Electric Company Limited (together called "the Company") are related companies and between them own and operate equipment and facilities for the transportation of persons and property by railway, trolley coach and motor buses and for the production, generation and furnishing of gas and electricity, all for the public for compensation.

The Company is regulated by the Public Utilities Commission of British Columbia (called "the Commission") pursuant to the provisions of the *Public Utilities Act*.

By appraisal the Commission ascertained the value of the property of the Company used, or prudently and reasonably acquired, to enable the Company to furnish its services. The appraisal was made as of December 31, 1942, and since then has been kept up to date. The appraised value is referred to as "the rate base".

By Order-in-Council No. 1627, approved on July 16, 1948, the Commission was directed to consider the classes or categories of the regulated services of the Company as one unit in fixing the rates.

On September 11, 1952, the Commission after public hearing made "Findings as to Rate of Return" and decided that, "until changed financial and market circumstances convince the Commission that a different rate should be applied, the Commission will in its continuing examination of the Company's operations apply the rate of 6.5%" on the rate base as a fair and reasonable rate of return for the Company. This decision remains unchanged.

The Company from time to time amended its rate schedules with the consent of the Commission and filed with the Commission schedules showing the rates so established. On April 23, 1958, it applied for the consent of the Commission, under s. 17 of the *Public Utilities Act,* to file amended schedules containing increased rates for its electric service on the Mainland and on Vancouver Island. On July 28, 1958, it also applied for the consent of the Commission to file amended schedules containing increased transit fares for its transit systems in Vancouver and other Mainland areas and in Victoria and surrounding areas.

Public hearings were held by the Commission and it handed down its decision with respect to the electric applications on July 14, 1958, and with respect to the transit applications on October 30, 1958.

Briefly, the decisions of the Commission accepted the proposed rate schedules submitted by the Company, except that it refused to approve the proposed increases in the principal residential electric rates on the Mainland and on Vancouver Island. It directed that those rates be scaled down by approximately 25%. In its decision with respect to electric rates the Commission stated:

> The Commission has therefore consented to the filing to be effective July 15th, 1958, of all the rate schedules submitted by the Company for the Mainland and Vancouver Island, as modified and supplemented by the Company during the course of the hearings on its application, except the residential rate schedules and Mainland Rate 3035 for industrial users.
>
> The Commission has decided that the principal residential rate on the Mainland (Schedule 1109) and the principal residential rate on the Island (Schedule 1110 under which the principal divisions are Billing Codes 1110 and 1112) should be adjusted to yield not more than three-quarters of the additional revenue proposed. The adjustment must be applied primarily to reduce sharp changes in impact and lessen disproportionately large percentage increases in the consumption range of 60 KWH to 280 KWH per month. Comparable adjustments must also be made in some of the related special residential rates of lesser importance. Most of the relief would be given to the small residential user.

At the same time the Commission decided that further increases in the commercial and industrial rates to compensate for this reduction in the proposed residential rates would not be justified.

During the hearings it was contended by counsel for the Company that, the Commission, having determined on a fair and reasonable return to the Company, namely, 6.5%, the Commission should authorize rates which would yield that return, or whatever lesser return the Company's application requested for the time being. The Commission did not accept this contention and the rates which were approved by the Commission would yield approximately $750,000 less per annum than those applied for by the Company would yield. The rates for which the Company sought approval themselves would not have yielded to the Company the full allowed rate of return of 6.5%.

The relevant portions of s. 16(1) of the *Public Utilities Act* provide as follows:

> 16. (1) In fixing any rate:—

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(a) The Commission shall consider all matters which it deems proper as affecting the rate:

(b) The Commission shall have due regard, among other things, to the protection of the public from rates that are excessive as being more than a fair and reasonable charge for services of the nature and quality furnished by the public utility; and to giving to the public utility a fair and reasonable return upon the appraised value of the property of the public utility used, or prudently and reasonably acquired, to enable the public utility to furnish the service:

(c) Where the public utility furnishes more than one class of service, the Commission shall segregate the various kinds of service into distinct classes or categories of service; and for the purpose of fixing the rate to be charged for the service rendered, each distinct class or category of service shall be considered as a self-contained unit, and the rates fixed for each unit shall be such as are considered just and reasonable for that unit without regard to the rates fixed for any other unit. If it is considered by the Lieutenant-Governor in Council that the rates as so determined might be inequitable or contrary to the general public interest, the Lieutenant-Governor in Council may direct that two or more classes or categories of service shall be considered as one unit in fixing the rate:

In the reasons given for its decision the Commission deals with the effect of clauses (*a*) and (*b*) of s. 16(1) and says:

With great respect, the Commission considers that although for this purpose the statutory duty of the Commission to have due regard to all matters which the Commission deems proper as affecting the rate might without any significant inaccuracy be described as the right of the Commission, and its statutory duty to *have due regard to giving* the utility a fair and reasonable return might without significant inaccuracy be described as the Commission's *responsibility for giving* the utility a fair and reasonable return, there is nothing in the Act to relieve the Commission in the case now before it from complying with the language of the Act and giving due regard to all those matters to which the legislature has directed the Commission to give due regard in fixing a rate. No one of those matters should, in the opinion of the Commission, be given as a matter of law priority over any other of those matters and if, as the legislature appears to have thought possible, a conflict arises among those matters, the Commission considers that it is its duty to act to the best of its discretion.

The Court of Appeal concurred in this view. The judgment of the Court[1], delivered by Sheppard J.A., refers to this question in the following words:

A further inquiry is what weight should be given to the matters required to be considered by Sec. 16(1)(*b*) and particularly to the "fair and reasonable return". Under Sec. 16(1)(*b*), the Commission is required

[1] (1959), 29 W.W.R. 533 at 538.

to consider "the protection of the public" and the "giving to the public utility a fair and reasonable return". Although clauses (*a*) and (*b*) of Sec. 16(1) require certain matters to be considered, they do not state what weight is to be assigned by the Commission. Consequently, the Statute requires only that the Commission consider the matters falling within Sec. 16(1)(*a*), namely, "all matters which it deems proper as affecting the rate" and those falling within Sec. 16(1)(*b*), namely, "the protection of the public" and "a fair and reasonable return" to the Utility. But the Statute does not require more, and does not require any weight to be given to these matters after they have been considered. Hence the weight to be assigned is outside any statutory requirement and must be a question of fact for the Commission in each instance.

From this decision the present appeal is brought.

To determine the intent and meaning of clauses (*a*) and (*b*) of s. 16(1) of the Act it is necessary to consider them in relation to the other provisions of the Act, with which they must be read.

Section 5 imposes upon a public utility the duty to maintain its property and equipment in such condition as to enable it to furnish, and to furnish, service to the public in all respects adequate, safe, efficient, just and reasonable. Section 7 prevents a public utility which has been granted a certificate of public convenience and necessity or a franchise from ceasing its operations or any part of them without first obtaining the permission of the Commission.

Section 6 requires every public utility, upon reasonable notice, to furnish to all persons who may apply therefor, and be reasonably entitled thereto, suitable service without discrimination and without delay.

Sections 38, 42 and 43 contain provisions whereby, in the circumstances therein defined, a public utility may be ordered by the Commission to extend its existing services.

These four sections last mentioned involve a statutory obligation on the part of a public utility to make capital outlays for extensions of its service. A public utility which operates in a rapidly expanding community may be required to make substantial expenditures of that nature in order to keep pace with increasing demands. It must, if it is to fulfil those obligations, be able to obtain the necessary

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capital which is required, which it can only do if it is obtaining a fair rate of return upon its rate base. The meaning of a fair return was defined by Lamont J. in *Northwestern Utilities, Limited v. City of Edmonton*[1]:

> By a fair return is meant that the company will be allowed as large a return on the capital invested in its enterprise (which will be net to the company) as it would receive if it were investing the same amount in other securities possessing an attractiveness, stability and certainty equal to that of the company's enterprise.

The necessity for giving a public utility fair compensation for the service which it renders appears in the definition of the words "unjust" and "unreasonable" in s. 2(1), which is as follows:

> "Unjust" and "unreasonable" as applied to rates shall be construed to include respectively injustice and unreasonableness, whether arising from the fact that rates are excessive as being more than a fair and reasonable charge for service of the nature and quality furnished by the public utility, or from the fact that rates are insufficient to yield fair compensation for the service rendered, or arising in any other manner:

The word "service", which appears in this definition, is defined in the Act to include:

> the use and accommodation afforded consumers or patrons, and any product or commodity furnished by a public utility; and also includes, unless the context otherwise requires, the plant, equipment, apparatus, appliances, property, and facilities employed by or in connection with any public utility in performing any service or in furnishing any product or commodity and devoted to the purposes in which the public utility is engaged and to the use and accommodation of the public:

These defined words appear in two sections of the Act which relate to the rates to be charged by a public utility.

Section 8, which is among a group of sections dealing with the duties and restrictions imposed on public utilities, provides:

> 8. (1) No public utility shall make demand or receive any unjust, unreasonable, unduly discriminatory, or unduly preferential rate for any service furnished by it within the Province, or any rate otherwise in violation of law; and no public utility shall, as to rates or service, subject any person or locality, or any particular descripiton of traffic, to any undue prejudice or disadvantage, or extend to any person any form of agreement, or any rule or regulation, or any facility or privilege, except such as are regularly and uniformly extended to all persons under substantially similar circumstances and conditions in respect of service of the same description, and the Commission may by regulations declare what constitute substantially similar circumstances and conditions.

[1] [1929] S.C.R. 186 at 193, 2 D.L.R. 4.

(2) It shall be a question of fact, of which the Commission shall be the sole judge, whether any rate is unjust or unreasonable, or whether in any case there is undue discrimination, preference, prejudice, or disadvantage in respect of any rate or service, or whether service is offered or furnished under substantially similar circumstances and conditions. 1938, c. 47, s. 8; 1939, c 46, s. 5.

Section 20, which empowers the Commission to determine rates, reads as follows:

20. The Commission may upon its own motion or upon complaint that the existing rates in effect and collected or any rates charged or attempted to be charged by any public utility for any service are unjust, unreasonable, insufficient, or discriminatory, or in anywise in violation of law, after a hearing, determine the just, reasonable, and sufficient rates to be thereafter observed and in force, and shall fix the same by order. The public utility affected shall thereupon amend its schedules in conformity with the order and file amended schedules with the Commission.

It will be noted that this section, in addition to the use of the words "unjust" and "unreasonable", also uses the terms "insufficient" and "sufficient" in relation to rates.

Both of these sections contemplate a system of rates which would be fair to the consumer on the one hand and which will yield fair compensation to the public utility on the other hand.

Section 16, the section with which we are concerned in this appeal, also deals with this matter of fairness of rates. In addition, it spells out the method by which a public utility is to obtain fair compensation for its service; i.e., by a fair and reasonable return upon its rate base, which rate base, pursuant to s. 45, the Commission can determine by appraisal.

Section 16 deals with the duties of the Commission in fixing rates. Clause (*a*) of subs. (1) states that the Commission shall consider all matters which it deems proper as affecting the rate. It confers on the Commission a discretion to determine the matters which it deems proper for consideration and it requires the Commission to consider such matters.

Clause (*b*) of subs. (1) does not use the word "consider", which is used in clause (*a*), but directs that the Commission "shall have due regard", among other things, to two specific matters. These are:

(i) The protection of the public from rates that are excessive as being more than a fair and reasonable charge for services of the nature and quality furnished by the public utility; and

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(ii) To giving to the public utility a fair and reasonable return upon the appraised value of its property used or prudently and reasonably acquired to enable the public utility to furnish the service.

As I read them, the combined effect of the two clauses is that the Commission, when dealing with a rate case, has unlimited discretion as to the matters which it may consider as affecting the rate, but that it must, when actually setting the rate, meet the two requirements specifically mentioned in clause (*b*). It would appear, reading ss. 8, 16 and 20 together, that the Act contemplates these two matters to be of primary importance in the fixing of rates.

In my opinion, therefore, these two factors should be given priority over any other matters which the Commission may consider under clause (*a*), or any other things to which it shall have due regard under clause (*b*), when it is fixing any rate.

The second portion of question (1)(*a*) was as to whether, in case of conflict among the matters and things referred to in clauses (*a*) and (*b*) of s. 16(1), it was the Commission's duty to act to the best of its discretion. I have already expressed my view regarding the priority as between those things specifically mentioned in clause (*b*) and the other matters or things referred to in clauses (*a*) and (*b*). This leaves the question as to possible conflict as between the two matters specifically mentioned in clause (*b*).

Clearly, as between these two matters there is no priority directed by the Act, but there is a duty imposed upon the Commission to have due regard to both of them. The rate to be imposed shall be neither excessive for the service nor insufficient to provide a fair return on the rate base. There must be a balancing of interests. In my view, however, if a public utility is providing an adequate and efficient service (as it is required to do by s. 5 of the Act), without incurring unnecessary, unreasonable or excessive costs in so doing, I cannot see how a schedule of rates, which, overall, yields less revenue than would be required to provide that rate of return on its rate base which the Commission has determined to be fair and reasonable, can be considered, overall, as being excessive. It may be that within the schedule certain rates may operate unfairly, relatively, as

between different classes of service or different classes of consumers. If so, the Commission has the duty to prevent such discrimination. But this can be accomplished by adjustments of the relative impact of the various rates in the schedule without having to reduce the total revenues which the whole schedule of rates is designed to produce.

Accordingly, it is my opinion that the answer to question (1)(*a*) should be "No". My answer to question (1)(*b*) would be that the Commission, in priority to any other matters which it may deem proper to consider under clause (*a*) and any of the other things referred to in clause (*b*) of s. 16(1), should have due regard to the two matters specifically mentioned in clause (*b*). In the present case, having decided that certain of the rates proposed by the appellant would impose an unreasonable burden upon certain classes of consumers, the Commission should permit the Company to submit alternative schedules of rates, which, while yielding approximately the same overall revenues, would eliminate the comparatively excessive impact of those classes of rates to which the Commission objected, until a rate schedule is devised which meets the requirements of clause (*b*) of s. 16(1).

In my view the appeal should be allowed, but no costs should be payable.

Appeal allowed, Kerwin C.J. *dissenting.*

Solicitor for the appellant: A. Bruce Robertson, Vancouver.

Solicitors for The Public Utilities Commission of British Columbia, respondent: Clark, Wilson, Clark, White & Maguire, Vancouver.

Solicitors for The Corporation of The City of Victoria, The Corporation of The District of Oak Bay, The Corporation of The District of Saanich and Corporation of The Township of Esquimalt, respondents: Straith, O'Grady, Buchan, Smith & Whitley, Victoria.

Solicitor for City of Vancouver, respondent: R. K. Baker, Vancouver.

ATTACHMENT C

BC Hydro v. Terasen Gas (Vancouver Island) Inc.

COURT OF APPEAL FOR BRITISH COLUMBIA

Citation: ***BC Hydro and Power Authority v. Terasen Gas (Vancouver Island) Inc.,*** 2004 BCCA 346

Date: 20040623
Docket: CA030969; CA030984

In the Matter of the *Utilities Commission Act*, R.S.B.C. 1996, c. 473

And In the Matter of Centra Gas British Columbia Inc. (now Terasen Gas (Vancouver Island) Inc.) 2002 Rate Design Application

And In the Matter of British Columbia Utilities Commission Decision Pronounced June 5, 2003 and Order Number G-42-03 Issued June 5, 2003

Docket: CA030969

Between:

British Columbia Hydro and Power Authority

Appellant

And

Terasen Gas (Vancouver Island) Inc., Howe Sound Pulp & Paper Limited Partnership, Norske Skog Canada Limited, Pope & Talbot Ltd., and Western Pulp Limited Partnership, doing business as the Vancouver Island Gas Joint Venture, Consumers' Association of Canada (B.C. Branch) B.C. Old Age Pensioners' Organization, Council of Senior Citizens' Organizations, Senior Citizens Association of British Columbia, Tenants Rights Action Coalition, Vancouver Island Public Sector Natural Gas Consumers Group, and Her Majesty the Queen in Right of the Province of British Columbia, as represented by the Minister of Energy and Mines

Respondents

- and -

Docket: CA030984

Between:

Howe Sound Pulp & Paper Limited Partnership, Norske Skog Canada Limited, Pope & Talbot Ltd., and Western Pulp Limited Partnership, doing business as the Vancouver Island Gas Joint Venture

Appellants

And

Terasen Gas (Vancouver Island) Inc., British Columbia Hydro and Power Authority, Consumers' Association of Canada (B.C. Branch), B.C. Old Age Pensioners' Organization, Council of Senior Citizens' Organizations, Senior Citizens Association of British Columbia, Tenants Rights Action Coalition, Vancouver Island Public Sector Natural Gas Consumers Group, and Her Majesty the Queen in Right of the Province of British Columbia, as represented by the Minister of Energy and Mines

Respondents

Before: The Honourable Mr. Justice Lambert
The Honourable Mr. Justice Mackenzie
The Honourable Mr. Justice Oppal

R.W. Lusk, Q.C. and B.W. Dixon	Counsel for British Columbia Hydro and Power Authority
D.L. Larson and K.E. Gustafson, Q.C.	Counsel for Vancouver Island Joint Venture
C.B. Johnson	Counsel for Terasen Gas (Vancouver Island) Inc.
J.L. Quail	Counsel for Consumers' Association of Canada (B.C. Branch), B.C. Old Age Pensioners' Organization, Council of Senior Citizens' Organizations, Senior Citizens Association of British Columbia, Tenants Rights Action Coalition, and Vancouver Island Public

	Sector Natural Gas Consumers Group
G.A. Fulton	Counsel for the BC Utilities Commission
Place and Date of Hearing:	Vancouver, British Columbia May 3, 4 & 5, 2004
Place and Date of Judgment:	Vancouver, British Columbia June 23, 2004

Written Reasons by:
The Honourable Mr. Justice Mackenzie

Concurred in by:
The Honourable Mr. Justice Lambert
The Honourable Mr. Justice Oppal

Reasons for Judgment of the Honourable Mr. Justice Mackenzie:

[1] These appeals, with leave, are from an order of the British Columbia Utilities Commission (the “Commission” or “BCUC”) setting rates for the transmission and distribution of natural gas on Vancouver Island. The Commission’s Order No. G-42-03 fixed rates for service effective 1 January 2003 for Centra Gas British Columbia Inc., now Terasen Gas (Vancouver Island) Inc. (“Centra”).

[2] The issues arise out of the Commission's determination to include in the transmission service rates for the appellant, British Columbia Hydro and Power Authority (“BC Hydro”), a contribution to the amortization of an accumulated shortfall between Centra's revenues and its cost of service. This "revenue deficiency", starting in 1996, has grown to a balance of $87.9M as at the end of 2002. This balance is recorded in a Revenue Deficiency Deferral Account (the "Deficiency Account" or “RDDA”). BC Hydro contends that including a contribution to revenue deficiency recovery in its tolls is unlawful, essentially because it conflicts with a Special Direction (the “Special Direction"), issued by the Lieutenant Governor in Council, that the Commission must follow in determining Centra's rates. BC Hydro also contends that the Commission erred by establishing a revenue to cost ratio of

1.25 for the purpose of setting the rates paid by BC Hydro. The 1.25 ratio facilitates the recovery of the revenue deficiency through BC Hydro's rates. The annual contribution to recovery from BC Hydro's tolls is estimated at $4.5M.

[3] The appellants – Howe Sound Pulp & Paper Limited Partnership, Norske Skog Canada Limited, Pope & Talbot Ltd., and Western Pulp Limited Partnership, doing business as the Vancouver Island Gas Joint Venture (the “Joint Venture”) – support BC Hydro and raise other related issues with respect to revenue deficiency recovery in transmission tolls. The Joint Venture is not directly impacted by the Commission's decision because its tolls are set by a formula in a long term transportation service agreement (the "Joint Venture Agreement") that does not include any revenue deficiency recovery. However, the Joint Venture has an interest in BC Hydro's tolls because if they were lower than the tolls in the Joint Venture Agreement, the Joint Venture has the option of terminating the agreements on notice and seeking tolls equivalent to those for BC Hydro.

The Centra Utility Undertaking

[4] There are two parts to the Centra utility undertaking - a high pressure main transmission pipeline (the "Pipeline") that

crosses the Strait of Georgia, and a lower pressure distribution system (the "Distribution System") connected to the Pipeline on Vancouver Island and the Sunshine Coast. The appellants are all connected directly to the Pipeline and purchase natural gas from producers upstream of the Pipeline rather than from Centra. They contract with Centra for transmission service to transport their gas through the Pipeline to their facilities. They do not use any part of the Distribution System.

[5] Residential, commercial, and small industrial customers are connected to the Distribution System. They buy gas from Centra at their point of delivery and their rates include a charge for the commodity cost of the gas in addition to the charge for gas transportation through the Pipeline and the Distribution System. Some Distribution System customers have the option of buying gas from producers and contracting with Centra for transmission service only, but such arrangements are rare.

History of the Natural Gas Service to Vancouver Island

[6] Natural gas transmission and distribution on Vancouver Island and the Sunshine Coast of British Columbia commenced in 1991 when the Vancouver Island Natural Gas Pipeline was

completed. The high pressure transmission Pipeline transports gas from the Lower Mainland to distribution systems serving commercial and residential customers. The Pipeline also transports gas for the Joint Venture and, since 2001, to BC Hydro's electricity co-generation plant at Elk Falls, near Campbell River. Until service to BC Hydro commenced, the Joint Venture and Squamish Gas were the only shippers connected directly to the Pipeline.

[7] Until 1996, the Pipeline was owned and operated separately from the distribution systems by Pacific Coast Energy Corporation, a wholly owned subsidiary of Westcoast Energy Inc. The distribution systems connected to the Pipeline were operated by three wholly owned Westcoast subsidiaries, Centra Gas British Columbia Inc., Centra Gas Victoria Inc., and Centra Gas Vancouver Island Inc. The companies encountered financial difficulties from the inception of their operation.

The 1995 Centra Restructuring

[8] In 1995 the companies were restructured: Pacific Coast Energy Corporation acquired the gas distribution assets of the Centra companies and then changed its name to Centra. The restructuring was documented by the Vancouver Island Natural

Gas Pipeline Agreement (the "Agreement" or "VINGPA") dated 14 December 1995. The parties to the Agreement were the Province, the Centra distribution companies, Pacific Coast Energy Corporation and its then parent company, Westcoast Energy Inc. As part of the restructuring, the provincial government contributed $120M to the capital costs, which reduced the utility rate base by a corresponding amount. The Province also agreed to provide further assistance in the form of gas royalty credits estimated to contribute between $19.7M and $26.8M per year in revenues. These payments will end in 2011.

The Special Direction

[9] The Agreement provided for a Special Direction to be issued to the Commission for rate-making purposes by the Lieutenant Governor in Council, acting under the authority of s. 7 of the ***Vancouver Island Natural Gas Pipeline Act***, R.S.B.C. 1996, c. 474. Section 7 elevates the status of a special direction above any other inconsistent provisions, statutory or otherwise, relating to rate-making by the Commission, and makes plain the importance of a special direction as an instrument of government policy:

> **7** (1) The *Utilities Commission Act* and the *Gas Utility Act* apply to the proponent and a local

distribution utility except to the extent otherwise provided in this section or in a regulation under this section.

(2) The Lieutenant Governor in Council may make regulations as follows:

(a) ordering that prescribed provisions of the *Utilities Commission Act* or of the *Gas Utility Act* do not apply in respect of

(i) the proponent,

(ii) the local distribution utilities, or

(iii) a particular local distribution utility;

(b) prescribing limitations and conditions for the purposes of a regulation under paragraph (a).

(3) **Despite Parts 3 and 6 of the *Utilities Commission Act*, the Lieutenant Governor in Council may issue directions to the British Columbia Utilities Commission, specifying one or more of the following:**

(a) the factors, criteria and guidelines that the commission must or must not use in regulating and fixing rates for the proponent or a local distribution utility;

(b) classes of customers of the proponent or of a local distribution utility, according to volume of natural gas taken, location, date of application for natural gas service, type of premises or on any other basis the Lieutenant Governor in Council considers appropriate;

(c) the rates that may be permitted to be charged under the *Utilities Commission Act* by the proponent to

its customers or by a local distribution utility to its customers, and, in specifying rates under this paragraph, the Lieutenant Governor in Council may differentiate among the classes of customers specified under paragraph (b);

(d) limitations or principles that must be applied by the commission in fixing or varying the rates charged by the proponent to its customers or by a local distribution utility to its customers, and, for any specification of limitations or principles under this paragraph, differentiating, or requiring or empowering the commission to differentiate, among the classes of customers specified under paragraph (b);

(e) for all or part of any year since the commencement of operation of the pipeline, one or more of the following:

(i) the cost of service of the proponent or a local distribution utility;

(ii) the manner of determining the proponent's or a local distribution utility's cost of service;

(iii) the components, factors and considerations that must or must not be taken into account in making a determination under subparagraph (ii);

(f) an order that has been made by the British Columbia Utilities Commission and is or may be relevant to the proponent, one or more local

> distribution utilities, or both, and doing either or both of the following:
>
> (i) requiring the commission to apply or to refrain from applying that order or a specified portion or aspect of that order to the proponent, one or more local distribution utilities, or both;
>
> (ii) directing the commission as to the extent or manner in which it must or must not apply that order or a specified portion or aspect of that order to the proponent, one or more local distribution utilities, or both.
>
> (4) **Despite the *Utilities Commission Act* and the *Gas Utility Act*,**
>
> **(a) the British Columbia Utilities Commission must comply with a direction issued under subsection (3) of this section, and**
>
> **(b) if a direction issued under subsection (3) of this section is inconsistent or in conflict with the *Utilities Commission Act* or the *Gas Utility Act*, the direction prevails.** [Emphasis added]

The "proponent" referred to is Pacific Coast Energy Corporation, later Centra.

[10] The Special Direction was issued 13 December 1995 as contemplated by the Agreement. It is divided into five parts.

The first part includes definitions and s. 1.4 which reinforces the pre-eminence of the Special Direction in these terms:

> 1.4 General
>
> The BCUC shall regulate the Utilities and fix the rates charged by the Utilities in accordance with the requirements of this Special Direction, and in accordance with the requirements of the Utilities Commission Act and such regulatory principles that are otherwise applicable to the Utilities from time to time that are not inconsistent with this Special Direction. **In the event of any inconsistency between this Special Direction and any requirement of the Utilities Commission Act or any regulatory principles that would otherwise be applicable to the Utilities, the BCUC shall follow the provisions of this Special Direction.** For greater certainty, the BCUC shall not apply any provisions of the Utilities Commission Act (including, without limitation, Sections 64, 65, 66, and 67) in any manner which has the effect, directly or indirectly, of eliminating or varying any rates that have been specified in, or determined in accordance with, this Special Direction, or eliminating or varying any other determination or matter provided for herein. [Emphasis added]

[11] At the date of the Agreement the assets of the Distribution System and the Pipeline were held by separate companies, as noted above, and Parts 2 and 3 of the Special Direction recognized that separation. Part 2 sets out detailed directions to the Commission with respect to rates for the Distribution System. Part 3 gives direction with respect to rates for the Pipeline. The Special Direction also

recognized the intent of the Agreement to combine all the utility assets in a single entity and Part 4 is entitled “DETERMINATION OF ANNUAL REVENUE DEFICIENCY, RATE BASE, CAPITAL STRUCTURE AND RETURN ON EQUITY WHERE THE PIPELINE AND THE CENTRA DISTRIBUTION SYSTEM ARE OWNED BY A SINGLE ENTITY”. The Pipeline and the Distribution System became a single entity as of 1 January 1996, or very shortly after the Special Direction was issued. The remaining Part 5 of the Special Direction has no application to the issues in these appeals.

[12] "Annual Revenue Deficiency" is a term defined in s. 2.10 of the Special Direction as the amount by which Centra's adjusted cost of service exceeds its actual revenues in any year, and the Commission is directed to determine the balance of the Deficiency Account as the total of accumulated annual deficiencies. Section 2.10 also sets out detailed provisions for the determination of rate base, debt financing, deemed equity and return on equity. Critical to the issues on these appeals are two subsections of the Special Direction: s. 2.10(j), concerning the amortization of the Deficiency Account; and s. 4.1, directing that the calculation for annual deficiencies and the Deficiency Account be made for the single entity after its creation. The relevant portions of the provisions read:

> 2.10 Cost of Service and Revenue Deficiency
>
> **Subject to Part 4 of this Special Direction**, the BCUC shall determine Centra's cost of service and shall make the various associated determinations, all as described in, and in accordance with, the following directions.
>
> . . .
>
> (j) Deemed Redemption or Repayment of Instruments for the Determination of Cost of Service and Setting of Rates
>
> For each year beginning January 1, 2003, **the cost of service of Centra that is approved by the BCUC for the purpose of determining the rates to be charged to Centra's customers shall include an amount** for the deemed redemption of Class "A" Instruments or repayment of Class "B" Instruments **that the BCUC determines to be appropriate in order to amortize the balance of the Revenue Deficiency Deferral Account over the shortest period reasonably possible, having regard for Centra's competitive position relative to alternative energy sources and the desirability of reasonable rates.**
>
> 4.1 Annual Revenue Deficiencies
>
> **The BCUC shall determine Annual Revenue Deficiencies and the balance of the Revenue Deficiency Deferral Account for a Single Entity in the manner set out in Section 2.10 based upon the actual revenue and the cost of service associated with both the Centra Distribution System and the Pipeline** but without taking into account any revenue or costs that relate to any other business conducted, or assets owned, by the Single Entity. [Emphasis added]

[13] The provisions of Part 4, including s. 4.1, prevail over Part 2 to the extent of any inconsistency. Before the creation of the single entity, Centra, as defined, refers to the companies owning the Distribution System; afterward it

refers to the single entity. The reference to Class "A" and Class "B" instruments relates to the manner of financing the revenue deficiency until its amortization and does not require further explanation for the purposes of these reasons.

The Issues

[14] The issues in these appeals largely turn on whether the Commission complied with the Special Direction in setting rates for the appellants.

[15] BC Hydro’s complaint essentially is that the balance in the Deficiency Account represents accumulated deficiencies between revenues and cost of service in the Distribution System and no part of its recovery should be included in the rates charged to BC Hydro and the other large transmission service end users who take delivery of their gas directly from the Pipeline and do not use the facilities of the Distribution System. BC Hydro contends that the Special Direction precludes the Commission from including a contribution to amortization of the Deficiency Account recovery in BC Hydro’s rates.

[16] The Commission's reasons for concluding that it may include a contribution to the revenue deficiency in BC Hydro's rates were as follows:

In resolving the issue of whether or not it was the intention of the Special Direction that the RDDA be collected from [High-Pressure Transmission System ("HPTS")] customers other than the Joint Venture and Squamish Gas, the Commission has to consider the words and provisions of the Special Direction as a whole, as well as related documents such as the VINGPA and the Joint Venture TSA. In other words, the Commission must assess the factual matrix.

After reviewing and considering the evidence and the arguments, the Commission determines that the interpretations of Centra, CAC (BC) et al. and the Public Sector Consumers are more consistent with the applicable documents. The Commission finds that the Special Direction does not prohibit the Commission from allowing Centra to recover some of the RDDA in its transmission tolls from HPTS customers other than the Joint Venture and Squamish Gas, as well as in rates to distribution system customers on the [Centra Distribution System ("CDS")].

An argument advanced to support the position that tolls on the CDS and the HPTS should be treated separately, is based on the use of the word "customers" in Section 2.10(j) of the Special Direction. BC Hydro argues that this excludes parties who only transport gas on the HPTS system, since those parties are referred to as "shippers" in the Joint Venture TSA and the [Pacific Coast Energy Corporation] Terms and Conditions (Schedule H to the Special Direction). The Commission rejects that interpretation. If natural gas service were unbundled on the Centra system, then distribution system customers who chose to purchase gas from a third-party shipper would be able to avoid RDDA recovery in contrast to similar customers who continue to purchase gas from Centra. Also, as pointed out by Centra in argument, the VINGPA uses the term customers in a way that is consistent with the use of the word in Section 2.10(j) of the Special Direction (see, for example, the ninth recital of the VINGPA). Finally, if the distinction raised by BC Hydro was intended, the Commission would expect that "shippers" and "customers" would be defined terms in the Special Direction (as are many other terms), but they are not.

> The Commission agrees with BC Hydro that the terms of the Special Direction only prevail over the provisions of the Act and applicable regulatory principles if they are inconsistent with the Special Direction (BC Hydro Argument, p. 20). The Commission notes that it is directed in Sections 2.8, 2.10(d) and 3.7 of the Special Direction, to apply normal regulatory principles. For reasons discussed later in this Decision, the Commission also concludes that its interpretation is consistent with normal regulatory principles, and with the requirements of the UCA. [Emphasis in original]

[17] There are certain aspects of the Deficiency Account that are clear and non-controversial. Section 4.1, set out above, specifically directs the Commission to determine the annual revenue deficiencies and the balance of the Deficiency Account for a single entity based on the revenue and cost of service of the combined Distribution System and the Pipeline. The Commission is also specifically directed to establish a single rate base, capital structure and return on equity for the combined single entity.

[18] BC Hydro submits that Parts 2 and 3 of the Special Direction established separate rate-making criteria for "customers" of the distribution system and "shippers" connected directly to the Pipeline, and that the separation of the two groups is maintained notwithstanding the combination of the Distribution System and the Pipeline into a single entity. BC Hydro argues that the revenue deficiency results

from a shortfall between revenue and cost of service of the Distribution System and is not attributable to the cost of service of the Pipeline. BC Hydro argues that it is not a "customer" within the Part 2 rate-making methodology and that s. 3.7 excludes BC Hydro and other Pipeline shippers from contributing to amortization of the revenue deficiency.

The Standard of Review

[19] The first question to be answered is the standard of review to be applied in addressing the issues. The Supreme Court of Canada jurisprudence is extensive but the principles may be conveniently summarized. Courts are directed to take a robust and pragmatic approach to review and to consider four factors for determining the appropriate standard. They are: 1) the presence or absence of a privative clause or statutory right of appeal; 2) the expertise of the tribunal relative to that of the reviewing judge on the issue in question; 3) the purposes of the legislation, and of the provision in particular; and 4) the nature of the problem: ***Barrie Public Utilities v. Canadian Cable Television Assn.***, [2003] 1 S.C.R. 476, 225 D.L.R. (4th) 206, 2003 SCC 28 ¶10; see also ***Alberta Union of Provincial Employees v. Lethbridge Community College***, 2004 SCC 28.

[20] Addressing the first factor, s. 101 of the ***Utilities Commission Act*** provides for a right of appeal, with leave, to this Court from orders of the Commission. Section 105(2) bars other forms of judicial review. The ambit of an appeal is limited by s. 79 which states:

> The determination of the commission on a question of fact in its jurisdiction ... is binding and conclusive on all persons and on all courts.

[21] The Commission's exclusive jurisdiction over rates is further expanded by ss. 59(4) and (5):

> (4) It is a question of fact, of which the commission is the sole judge,
>
> (a) whether a rate is unjust or unreasonable,
>
> (b) whether, in any case, there is undue discrimination, preference, prejudice or disadvantage in respect of a rate or service, or
>
> (c) whether a service is offered or provided under substantially similar circumstances and conditions.
>
> (5) In this section, a rate is "unjust" or "unreasonable" if the rate is
>
> (a) more than a fair and reasonable charge for service of the nature and quality provided by the utility,
>
> (b) insufficient to yield a fair and reasonable compensation for the service provided by the utility, or a

> fair and reasonable return on the appraised value of its property, or
>
> (c) unjust and unreasonable for any other reason.

[22] The legislative scheme also includes power for the provincial government to give special directions to the Commission under two sections, both of which are similar: s. 3(1) of the ***Utilities Commission Act*** and ss. 7(1) to (4) of the ***Vancouver Island Natural Gas Pipeline Act***, set out above.

[23] I have set out the statutory provisions at length because they express the determination of the Legislature to insulate the Commission from judicial review of its specialized rate-making jurisdiction and they establish a close policy connection between the government and the Commission through the mechanism of special directions which take precedence over inconsistent provisions of the Commission's governing statutes or regulatory principles otherwise applicable. This implies a high degree of judicial deference within the terms of a special direction but less deference in the interpretation of terms that are mandatory and do not import an element of discretion.

[24] Moving on to the second and third factors to be considered in determining the standard of review, the

legislative scheme emphasizes the expertise of the Commission within its rate-making mandate, including the statutory declarations that just and reasonable rates are questions of fact and Commission findings of fact within its jurisdiction are conclusive. The statutory recognition of the Commission's expertise in determining rates reinforces curial deference. The Commission is required to resolve and balance the economic interests of various constituencies, well illustrated by the parties to these proceedings, which gives its jurisdiction a polycentric quality, as termed by the Supreme Court of Canada in ***Pushpanathan v. Canada (Minister of Citizenship and Immigration)***, [1998] 1 S.C.R. 982, 160 D.L.R. (4th) 193, 226 N.R. 201 ¶36. The Commission's function is pragmatic and often robust.

[25] The final factor is the nature of the problem or question. Here the appellants have raised several questions and, as the Supreme Court of Canada has observed, the standard of review may be different for different questions.

BC Hydro's First Issue

[26] The first question raised by BC Hydro was defined by the Commission's conclusion, set out above, that the Special Direction does not prohibit the Commission from allowing

Centra to recover some of the revenue deficiency from transmission tolls of BC Hydro.

[27] BC Hydro is the only high pressure transmission service customer apart from the Joint Venture and Squamish Gas, and it disputes its designation as a "customer", for reasons discussed below. BC Hydro submits that this question goes to the delineation of the Commission's mandate and the standard of review is correctness. The Commission agrees that it must be correct in answering that question. Centra also agrees that at the broad jurisdictional level, the appropriate standard is correctness on the question of whether the Special Direction prohibits the Commission from setting rates for BC Hydro that include a contribution for amortization of the Deficiency Account balance. I propose to apply the standard of correctness to the first issue as so defined.

[28] Centra and Centra Distribution System are both defined terms in the Special Direction. The Centra Distribution System is defined as the physical assets comprising the distribution system and not the entity holding those assets. Centra has a dual meaning. When the Distribution System assets and the Pipeline are held by separate entities, Centra means the entities holding the Distribution System assets only. After the assets are combined in a single entity, Centra means that

entity, which includes both the Distribution System and Pipeline assets. Therefore there is no definitional impediment to construing references to Centra in Part 2, post combination, as including the Pipeline, to the extent that Part 4 applies the terms of Part 2 to the single entity.

i) The "customer" argument

[29] BC Hydro contends that "customer" in Part 2 is limited to Distribution System customers who pay Centra a bundled rate for transportation and the commodity cost of gas delivered, as opposed to shippers who are charged a toll for transportation only and purchase the gas separately from gas producers. The Commission, in its reasons quoted above, rejected that submission, noting that if natural gas service were unbundled on the Centra system, then Distribution System customers who chose to purchase gas from a third-party shipper would be able to avoid Deficiency Account recovery, in contrast to customers who continue to purchase gas from Centra. The Commission further noted that the use of “customer” for which Centra contends is consistent with its use in s. 2.10(j) of the Special Direction – the Special Direction does not define “customer” and generically the term is capable of including end users of transportation service as well as purchasers of both transportation service and the gas commodity from Centra.

BC Hydro refers to the definition of "Shipper" as any person who enters into a "Service Agreement" – defined as a gas transportation service agreement with Pacific Coast Energy Corporation, as set out in the general conditions for gas transportation service approved and attached as a schedule by s. 3.5 of the Special Direction – as applicable to all transportation service agreements. BC Hydro also relies on the division of customers in s. 2.2 of the Special Direction into “Pioneer Customers” and “New Customers”.

[30] The Commission rejected BC Hydro's submission that shippers under transportation service agreements could not be customers for the reasons quoted above. Centra supported the Commission's conclusion by noting that the distinction between Pioneer and New Customers, with one limited exception, had no application after 31 December 2002, the effective commencement date for the single entity. The distinction was not intended to be exclusive because it referred to other customers who were neither Pioneer nor New Customers. The reference to persons entering into transportation service agreements as “shippers”, for the purposes of the terms and conditions of those transportation agreements, does not preclude them from being customers generically; they are customers in the ordinary sense of the word as they purchase a service from

Centra. "Shipper" is not a defined term in the Special Direction other than its reference to the transportation service agreements' general terms and conditions, and Centra contended that the absence of any restrictive definition to limit the generic meaning of customer supports the conclusion that shippers were included within customers of the single entity for the purposes of s. 2.10(j).

ii) The section 3.7 argument

[31] BC Hydro contended that its position was supported by s. 3.7 of the Special Direction which makes reference to the Deficiency Account. It states:

> 3.7 Rates and Transportation Tolls Otherwise Applicable to the Joint Venture, Squamish Gas, and Centra
>
> For the purpose of fixing transportation tolls to be charged by [Pacific Coast Energy Corporation] other than as directed in Sections 3.2, 3.3 and 3.4, the BCUC shall, subject to the exception set out below, apply such regulatory principles that are generally applied by the BCUC from time to time to gas utilities operating within British Columbia. In no event whatsoever shall the rates or transportation tolls that are approved for the Joint Venture or Squamish Gas pursuant to this Section 3.7 include any amount for the recovery in whole or in part, directly or indirectly, of dividends or interest as described in paragraph 2.10(h), or for the amortization, reduction, or recovery of the Revenue Deficiency Deferral Account balance.

This provision clearly excludes the tolls of the Joint Venture (and Squamish Gas) from any contribution to revenue deficiency recovery. BC Hydro contended that the intent of s. 3.7 was to exclude all persons with transportation service contracts from contributing to the deficiency recovery and the specific reference to the Joint Venture and Squamish Gas was only for greater certainty, out of an abundance of caution. BC Hydro notes that the Joint Venture and Squamish Gas were the only parties with transportation service contracts when the Special Direction was issued.

[32] BC Hydro's argument contains an implicit admission that without the specific reference, s. 3.7 is otherwise potentially ambiguous. Centra argued that s. 3.7 makes specific reference to exemptions for the Joint Venture and Squamish Gas and is not a general exemption for those with transportation service agreements. Centra relied on the implied exclusion argument that:

> Whenever there is reason to believe that if the legislature had meant to include a particular thing within its legislation, it would have referred to that thing expressly. Because of this expectation, the legislature's failure to mention the thing becomes grounds for inferring that it was deliberately excluded: R. Sullivan, *Sullivan and Driedger on the Construction of Statutes*, 4th ed. (Markham: Butterworths, 2002) at 186; see also ***65302 British Columbia Ltd. v. Canada***, [1999] 3 S.C.R. 804, 179 D.L.R. (4th) 577, 69 B.C.L.R. (3d) 201 ¶65.

Centra contended that s. 3.7 supports the Commission's conclusion that persons with transportation service agreements other than those specifically exempted were not intended to be excluded from revenue deficiency recovery.

iii) The revenue deficiency source argument

[33] BC Hydro argued that the revenue deficiencies resulted entirely from revenue deficits on the Distribution System and that the Pipeline transportation users were paying their full cost of service on the Pipeline and not contributing to the deficiency. The Commission was unable to determine that the entire revenue deficiency arose solely as a result of costs exceeding revenues on the Distribution System and it concluded that: "The Pipeline would not have been viable without the combined loads and the government support provided to deliver gas to Vancouver Island" and "the transmission facilities would not have been constructed if the expectation had been to only serve large volume customers taking transmission service." The Pipeline and the Distribution System were interrelated from the inception of the project. The government's interest is reflected in the $120M contributed under the Vancouver Island Natural Gas Pipeline Agreement, conditional on the creation of the merger of the Pipeline and the Distribution System under that agreement, and supports the

government's policy interest in combining the two for the economic viability of the system as a whole.

[34] The Commission recognized that the availability of fuel oil and electricity as competitive alternative fuels for residential and commercial customers limited the rates for natural gas to those customers. The Commission established a "soft cap" mechanism which limited rates to those customers to the maximum that the residential and commercial customers could be expected to pay given the price of alternative fuels. BC Hydro and the Joint Venture did not challenge the rationale or methodology of the soft cap mechanism before the Commission, and a BC Hydro witness agreed that setting rates for residential and commercial customers relative to the price of oil and electricity was not unreasonable. The rates set under the soft cap mechanism were projected to amortize only a portion of the Deficiency Account by 2011.

[35] The ability of Centra to earn a fair return on its utility rate base is an imperative of the Special Direction and the regulatory scheme. General regulatory principles require the Commission to grant a utility the opportunity to earn a fair return: ***Hemlock Valley Electrical Services Ltd. v. British Columbia (Utilities Commission)*** (1992), 66 B.C.L.R. (2d) 1, 12 B.C.A.C. 1 ¶57. The "soft cap" on rates paid by

Distribution System customers because of the competition from alternative energy sources imposed a pragmatic limit on the revenue that could be obtained from those customers. The rates for the Joint Venture and Squamish Gas were fixed by formulas in their transportation service agreements and confirmed by the Special Direction. While the rates set for Distribution System customers are projected to make some contribution to the amortization of the accumulated revenue deficiency, they will still leave a substantial portion outstanding in 2011, when the royalty credits will end, with a corresponding increase in the cost of service. The alternatives facing the Commission were to set rates for BC Hydro that provided for a contribution to the amortization or defer substantial recovery to an uncertain future after 2011. The submission of Mr. Quail, on behalf of the Consumers' Association of Canada (BC Branch) and other residential consumer groups, emphasized the continued financial vulnerability of the utility if amortization of the Deficiency Account were deferred to an indefinite, uncertain future. The Special Direction instructs the Commission to set rates that will amortize the Deficiency Account balance "over the shortest period reasonably possible" (s. 2.10(j)). The legislative scheme, the Special Direction and economic exigencies of the single entity utility all look to BC Hydro

(and any new transportation service contracts) to contribute substantially to the amortization of the accumulated deficiency.

[36] I am satisfied that the Commission was correct in concluding that the term "customer" in Part 2 of the Special Direction included transmission shippers following the establishment of the Single Entity and the coming into effect of the Part 4 provisions. I agree with Centra's submission that the meaning of "customers" of the single entity extends to include transportation shippers and 2.10(j) applies to BC Hydro's rates. I think that the limited exemption of the Joint Venture and Squamish Gas in s. 3.7 reinforces the conclusion that other transportation service contracts were not exempted. In my view, there is nothing in the Special Direction or otherwise in the regulatory scheme that precluded the Commission from setting rates for BC Hydro that included amortization of the Deficiency Account balance. Accordingly, I would reject BC Hydro's first ground of appeal.

BC Hydro's Second Issue

[37] BC Hydro submits that the Commission erred in establishing tolls for BC Hydro at a revenue to cost ratio of 1.25, that is forecast revenues from BC Hydro’s tolls that

exceed its allocated cost of service by 25 per cent. BC Hydro's statement of this issue acknowledges that the 1.25 ratio is linked to BC Hydro’s contribution to the amortization of the Deficiency Account. In that respect, the second issue is a variant of BC Hydro's first issue. I have concluded above that a contribution to amortization is within the Commission's rate setting mandate under the Special Direction. The only additional element posed by the second issue is whether a 1.25 revenue to cost ratio is an erroneous exercise of its mandate. The legislative provisions quoted above state that whether a rate is unjust or unreasonable is a question of fact and that the Commission's determination of a question of fact is binding and conclusive. The ambit of judicial review is therefore very limited.

[38] Centra is entitled to rates designed to recover the revenue requirement approved by the Commission. The maximum revenues that can be recovered from the distribution customers are constrained by the competitive alternatives reflected in the soft cap mechanism. The rates for the Joint Venture and Squamish Gas are fixed by formulas in their transportation service contracts. The revenue requirement allocated to BC Hydro's tolls, as the only other user of the system, is the residual amount of the revenue requirement remaining after the

revenues produced from the distribution service rates and the fixed transportation contract formulas have been determined. It simply reflects the tolls BC Hydro is required to pay if Centra is to have a reasonable opportunity to recover its revenue requirement, including a contribution to the revenue deficiency, the determination of which, following the resolution of the first issue, is within the Commission's mandate. The 1.25 ratio is within the range of revenue to cost ratios of rates for particular classes of Distribution System customers, which vary from 0.84 to 1.42.

[39] As I understand BC Hydro's submission, it does not challenge the rate as reviewable under the Commission’s general mandate. Rather it contended that the Special Direction prevails over the statutory provisions otherwise applicable and the 1.25 ratio conflicts with the Special Direction. BC Hydro argued that s. 3.1 of the Special Direction requires that its cost of service be determined on a separate rate base for the Pipeline as provided in that section. However, s. 3.1 is expressly stated to be "Subject to Part 4 of this Special Direction". Part 4 includes, in s. 4.2, a direction to determine a single rate base, capital structure and return on equity for the Single Entity. Section 4.1 requires that the Commission determine annual revenue

deficiencies and the balance of the Deficiency Account for the single entity. In my view, Part 4 of the Special Direction was clearly intended to combine the rate base of the Pipeline and the Distribution System once the assets were merged in the single entity, and the Deficiency Account is explicitly stated to be one account for the single entity. In my opinion, the Special Direction did not preclude the Commission from setting tolls for BC Hydro that provided for a contribution to amortization of the Deficiency Account that resulted in a 1.25 ratio. The rate set was not otherwise outside the Commission's rate-setting mandate in the exercise of its general jurisdiction.

[40] Accordingly, I do not think that there is merit in BC Hydro's second ground of appeal.

The Joint Venture Appeal

[41] The Joint Venture is not directly affected by the Commission's order because its tolls are determined independently by formulas in the Joint Venture Transportation Service Agreement dated 14 December 1995 which the Commission was directed to approve under s. 3.2 of the Special Direction. The Joint Venture may elect to terminate the Joint Venture Agreement on one year's notice and move to tolls otherwise

determined by the Commission, which presumably would be comparable to tolls set by the Commission for BC Hydro. The Joint Venture thus has a prospective interest in lower tolls for BC Hydro and therefore supported BC Hydro's appeal. It also raised other issues arising from the Special Direction and the terms of the Joint Venture Agreement.

[42] The Joint Venture submitted that the Commission erred in failing to distinguish between the Pipeline and the Distribution System, as required by s. 4.5 of the Special Direction and s. 60(1)(c) of the ***Utilities Commission Act***. The Joint Venture also contended that the Commission has abandoned cost-based rate design principles required by article 11.01(b) of the Joint Venture Agreement and that the tolls set for BC Hydro are discriminatory within the meaning of s. 59(1)(a) of the ***Utilities Commission Act*** and contrary to article 11.01(c) of the Joint Venture Agreement.

i) The cost-based rates issue

[43] The Joint Venture contended that Centra and the Commission failed to comply with the separate records requirement of s. 4.5 of the Special Direction as follows:

> 4.5 Separate Records
>
> The BCUC shall require that the Single Entity keep separate records relating to the Pipeline and the Centra Distribution System sufficient at all times to differentiate, where appropriate, between all activities related to the construction and operation of the Pipeline and the Centra Distribution System.

Centra's position is that it kept separate records for the pipeline and the distribution system in compliance with s. 4.5 of the Special Direction and the adequacy of those records was a matter that the Commission settled in favour of Centra. In my view, that was a matter within its specialized expertise and there was no reviewable error.

(ii) The Pipeline/Distribution System Distinction

[44] The Joint Venture's second issue is founded on article 11.01(b) of the Joint Venture Agreement that reads:

> 11.01 Covenants. Pacific Coast covenants with and in favour of Shipper that Pacific Coast:
>
> . . .
>
> (b) shall, in respect of the tolls to be charged to any new Third Party Shipper of gas through the Pacific Coast System, apply to the BCUC for approval of tolls which are determined in accordance with the full fixed-variable cost of service methodology and which, in the case of the mainline sections of the Pacific Coast System, are determined on a rolled-in basis as opposed to an incremental basis; and . . .

Article 11.01(b) is a covenant of Pacific Coast Energy, later Centra, which the Joint Venture contended was a condition of Centra's application for rates that the Commission was obliged to respect. The Joint Venture submitted that BC Hydro was a "Third Party Shipper" within article 11.01(b) and both Centra's application and the Commission's decision were not in accordance with "the full fixed-variable cost of service methodology" required.

[45] The Joint Venture's submission is in part a restatement of the customer/shipper distinction advanced by BC Hydro. In my view, it fails for the same reason, namely that "customer" is not a defined term in the Special Direction. Its meaning can extend to include "shippers" on the pipeline for the purposes of s. 2.10(j) with respect to the Deficiency Account because of the application of Part 4 of the Special Direction to the single entity. The amortization of the Deficiency Account consequently becomes a part of the cost of service for Distribution System customers and Pipeline shippers (apart from the Joint Venture and Squamish Gas specifically exempted by s. 3.7) and therefore included in any "full fixed-variable cost of service methodology". According to the Commission's reasons, quoted in paragraph 16 above, the inclusion of

revenue deficiency amortization in the cost of service is consistent with regulatory principles.

[46] In my view, determination of cost of service and allocation of that cost among users of the utility services for rate-making purchases is at the heart of the Commission's specialized expertise. Curial deference to that expertise is underlined by the statutory provisions that declare just and reasonable rates to be factual questions on which the Commission's determination is conclusive.

[47] Centra submitted in its factum that:

> A full fixed-variable cost of service methodology is one in which the fixed costs are allocated by way of a demand determinant and the variable costs are allocated by way of a commodity or variable determinant. Centra's Rate Design Application as it related to the firm transportation rate for service on the transmission facilities conformed with a full fixed-variable cost of service methodology.

The Commission rejected the Joint Venture's argument that Centra's application and the Commission's approach breached article 11.01(b). The Commission concluded:

> The Joint Venture's concerns about potential breach[es] of Section 11.01(b) seem to hinge on collection of [Revenue Deficiency Deferral Account] in the rates of other [High Pressure Transmission System] shippers. That has been dealt with elsewhere in the Special Direction.

In my view, the Commission recognized that the rate-making treatment of the Deficiency Account was the real complaint and, as concluded above, its treatment of that account accorded with its Special Direction mandate. To the extent that the Special Direction departed from general regulatory principles otherwise applicable, the Special Direction governed. The Commission concluded that the Special Direction and general regulatory principles were not inconsistent and there was no breach of article 11.01(b). Once the conclusion is reached that the Commission was correct in interpreting its Special Direction mandate, the Commission's determination was within its rate-making jurisdiction and does not contain any reviewable error. In my view, there is no basis for this Court to disturb the order of the Commission on this ground of appeal.

iii) Discrimination

[48] The Joint Venture also contends that the Commission has set discriminatory rates contrary to 11.01(c) of the Joint Venture Agreement that reads:

> (c) Pacific Coast will operate the Pacific Coast System so as to provide Firm Transportation Service and Interruptible Transportation Service under the General Terms and Conditions for Gas Transportation Service on a non-discriminatory basis in respect of gas to be transported and delivered to Shipper,

> Third Party Shippers and to the Centra Distribution System.

[49] The Commission determined that the transmission tolls set for BC Hydro were non-discriminatory. The tolls for the Joint Venture are negotiated charges defined by the Joint Venture Agreement and confirmed by the Special Direction. BC Hydro's tolls inevitably were going to be different unless the Commission simply imposed the Joint Venture Agreement formulas, which was not advocated by the Joint Venture or any other party. Indeed, imposing formula rates would defeat the Joint Venture's objective of rates for BC Hydro that were lower than those rates. In my opinion, there was no error in the Commission's conclusion that the tolls set for BC Hydro were non-discriminatory.

[50] The Joint Venture also raises a difference between curtailment rights applicable to the Joint Venture and to other industrial customers connected to the Distribution System. The curtailment rights with respect to the Joint Venture are negotiated terms agreed in a peaking gas management agreement between the parties and reflect the fact that the Joint Venture pulp and paper mills each have alternative heavy fuel oil burning capability. It was not unreasonable for the Commission to conclude that it was not

discrimination to accept different curtailment rights for other customers who may not have had similar standby capability.

[51] I am satisfied that none of the issues raised by the Joint Venture involve a reviewable error by the Commission.

Conclusion

[52] The economic viability of a utility, and service to its customers, depends upon its ability to meet its revenue requirement through tolls set by its regulator for its customers. No party to these appeals has questioned the revenue requirement determined by the Commission for Centra. Recovery of the Deficiency Account balance is part of the revenue requirement as mandated by the Special Direction. The share of Centra's revenue requirement that can be recovered from Distribution System customers is limited by competition from alternative fuels, reflected in the soft cap mechanism which all parties accept is a reasonable response to the competitive exigencies. The Joint Venture tolls are fixed by the Joint Venture Agreement and the Special Direction expressly excludes recovery of any part of the revenue deficiency from the Joint Venture. The only remaining source of customer revenue available for contribution to amortization

of the revenue deficiency is BC Hydro. The Commission was faced with the choice of setting tolls for BC Hydro that included contribution to the amortization or deferring amortization into an indefinite future, likely after 2011 when Centra will lose the contribution to revenue from gas royalty credits, and its ability to meet its revenue requirement may become more precarious. The Special Direction instructed the Commission to set rates that would amortize the accumulated deficiency "over the shortest period reasonably possible". The Special Direction does not preclude the Commission from including a contribution to amortization in BC Hydro's tolls. In light of the other constraints on the sources of revenue available to meet the revenue requirement, setting tolls for BC Hydro that includes a contribution to amortization simply recognizes the economic realities of the Centra utility. In my opinion, it was not an unreasonable determination by the Commission in the exercise of its jurisdiction and there was no reviewable error in the Commission’s order.

[53] I would dismiss both appeals.

"The Honourable Mr. Justice Mackenzie"

I AGREE:

"The Honourable Mr. Justice Lambert"

I AGREE:

"The Honourable Mr. Justice Oppal"