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Via E-file

August 21, 2020

B.C. Utilities Commission
Suite 410, 900 Howe Street
Vancouver, BC V6Z 2N3

File No.: 4.2.7(2020)

Attention: Marija Tresoglavic
Acting Commission Secretary

Dear Ms. Tresoglavic:

**Re: Pacific Northern Gas Ltd.
PNG-West Division
2020-2021 Revenue Requirements Application
Applicant's Supplemental Reply Argument on Shared Corporate Services Costs**

Accompanying, please find the Supplemental Reply Argument of Pacific Northern Gas Ltd. in the referenced proceeding on the matter of Shared Corporate Services Costs.

Please direct any questions regarding the application to my attention.

Yours truly,

Original on file signed by:

Verlon G. Otto

Enclosure

PACIFIC NORTHERN GAS LTD.

**APPLICATION
to the
BRITISH COLUMBIA UTILITIES COMMISSION**

**FOR APPROVAL OF THE PNG-WEST DIVISION
2020-2021 REVENUE REQUIREMENTS**

**APPLICANT'S SUPPLEMENTAL REPLY ARGUMENT
ON THE MATTER OF
SHARED CORPORATE SERVICES COSTS**

August 21, 2020

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1. INTRODUCTION

1. Pacific Northern Gas Ltd. (PNG) hereby provides its Supplemental Reply Argument on the matter of Shared Corporate Services Costs (SCSC) allocated to PNG by its parent, TriSummit Utilities Inc. (TSU, formerly AltaGas Canada Inc.) and in regard to submissions made in the Supplementary Final Argument on SCSC in this proceeding of the British Columbia Old Age Pensioners' Organization, Active Support Against Poverty, Disability Alliance BC, Council of Senior Citizens' Organizations of BC, and the Tenant Resource and Advisory Center, known collectively as BCOAPO et al. (BCOAPO), filed with the British Columbia Utilities Commission (BCUC) on August 18, 2020.

2. REPLY SUBMISSIONS

2. The BCOAPO Supplementary Final Argument on SCSC focused on two areas: (i) Inflating 2011 Directors Fees and Executive Management Salaries for 2020 Comparators; and (ii) Use of Standalone Costs as a Comparator for Shared Costs. The balance of this reply will focus on points made by BCOAPO in regard to each of these matters.

2.1 Inflating 2011 Costs for 2020 Comparators

3. In its Final Argument, BCOAPO has taken exception to the 3% inflation factor applied to the Directors Fees and Executive Management Salaries in arriving at the figures provided in response to BCUC IR 32.4. BCOAPO expressed its view that 3% is not appropriate and that a rate closer to 2%, the Bank of Canada's target inflation rate, would be more appropriate. BCOAPO further submitted that the past practice of applying a rate of 3% is unsupported and cannot be considered prudent, correct or sufficient evidence to justify inflating these costs into the future.

4. In reply and for clarity, PNG's Final Argument on SCSC noted that for the response to BCUC IR 32.4 the BCUC had requested that inflation be applied to 2011 costs in order to come up with an estimate for 2020 costs. PNG reiterates that the KPMG Report did not propose an inflationary approach in the evidence presented, but rather made use of current market-based data, including publicly-reported compensation of TSU executives as the basis for Executive Management costs and a third-party survey (Korn Ferry Report) for Director Fee costs.

5. Further, while PNG had made use of a 3% inflation rate in its analysis, PNG observes

that applying an inflation rate of 2% to these costs reduces the forecast by approximately \$128,000, and applying an inflation rate of 1% to these costs reduces the forecast by a further \$118,000. PNG further observes that the potential reduction in these cost elements from applying a different inflation rate does not reduce the total costs originally forecast of \$2,678,379 to an amount less than the 2020 SCSC allocation to PNG of \$1,835,433.

6. To close on this matter, PNG submits that, similar to the fair value approach taken in the KPMG Report, applying an inflationary approach to the evaluation of SCSC supports the assertion that the value of the shared services received by PNG from TSU is clearly greater than the amount that PNG would pay for these services on its own.

2.2 Use of Standalone Costs as a Comparator for Shared Costs

7. The Final Argument of BCOAPO challenges the use of “estimated, hypothetical” standalone costs as a basis for definitively determining the appropriateness of PNG’s recovery of the SCSC allocation from its parent. BCOAPO has submitted that an estimate of standalone costs represents the highest cost that an entity would incur for the service, and an upper boundary on what any other entity could theoretically charge for this service. Lastly, BCOAPO has submitted that standalone costs are expected to be greater in comparison to allocated costs by virtue of economies of scope and economies of scale inherent in the bundling of corporate services for provision and allocation to multiple entities.

2.2.1 Standalone Cost Estimates

8. PNG submits that the BCOAPO has rightly identified that the estimated standalone costs are the hypothetical cost an entity would incur to self-provide the same service. However, PNG challenges the assertions that such estimates are the highest cost an entity would incur and that they represent an upper boundary on what any other entity could theoretically charge.

9. In the past, the BCUC’s evaluation of SCSC allocations to PNG have made use of standalone cost estimates as a comparator for amounts allocated. As such, this same approach was adopted by PNG in support of the recoveries sought in this Application. PNG observes that the standalone cost estimates were prepared on a line-by-line basis, giving consideration and transparency to the underlying individual cost elements, a methodology PNG submits is aligned with the assessment approach supported by BCOAPO in its Final

Argument.

10. PNG notes that the evidence on record in this proceeding included an estimate of standalone costs derived from a market-based approach, as per the KPMG Report, and, at the BCUC's request, an estimate of standalone costs derived applying an inflationary approach, as per the response to BCUC IR 32.4 and addressed previously in this submission. PNG submits that, while the market-based estimate is greater than the inflationary estimate and both estimates are in excess of the proposed SCSC allocation to PNG, there is no evidence to support the assertion that these estimates represent the "highest cost" or "upper boundary" of amounts that could be charged to PNG. To close on this matter, PNG is hopeful that the application of these two distinct estimation methodologies allays the BCOAPO's concern that the estimate of standalone costs may be inflated to overstate the appropriateness of the proposed SCSC recoveries.

2.2.2 Economies of Scope and Scale

11. PNG concurs with the BCOAPO that economies of scope and economies of scale are inherent when a bundle of corporate services are assembled for provision to number of related entities. This is the very reason why the majority of corporate entities, including TSU, centralize and share certain core services with other entities in the corporate group.

12. PNG submits that, while it is not a standalone entity, the estimated standalone costs are a practical, reasonable and appropriate comparator to the SCSC allocated by its parent. In the absence of TSU corporate group, there would be no other entity with which PNG could share these necessary corporate service costs and there would be no other third-party service provider that could provide these services as efficiently and cost-effectively as PNG could itself.

3. CONCLUSION

13. PNG reiterates that the evidence on record supports that the SCSC allocation methodology is fair, reasonable and consistent with industry practices. PNG submits that the fair value of the shared services received from TSU is clearly greater than the amount that PNG would pay for these services on its own, and that its customers benefit from both shared costs and cost savings due to economies of scale as part of the TSU corporate group.

14. PNG further reiterates that in order to achieve a fair and reasonable result in respect of recovery of necessary costs of services for both customers and its shareholder, full recovery of these prudent and reasonable costs from TSU is appropriate.

ALL OF WHICH IS RESPECTFULLY SUBMITTED.

Dated at Vancouver, British Columbia this 21st day of August 2020.

PACIFIC NORTHERN GAS LTD.

Original on file signed by:

Gordon Doyle

Vice President, Regulatory Affairs, Legal & Gas Supply