

**F2012 to F2014 Revenue Requirements Application, Project No. 3698622**

**Association of Major Power Customers of BC (AMPC)**

**Response to BCOAPO Information Request No.1**

**May 15, 2012**

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**1.0 Topic: Outsourcing Opportunities**  
**Reference: Exhibit C18-9, page 9, Footnote 22**

1.1 AMPC indicates that it believes restructuring costs are the responsibility of BC Hydro, not the ratepayer. Does AMPC believe that severance costs should be excluded from this application?

**Response:**

AMPC believes that BC Hydro should structure its staffing and compensation levels at a level appropriate for the basic functions that are required of an electric utility. Where these levels are imprudent they should be disallowed. Severance costs associated with imprudent decisions should not be borne by the ratepayers. There is little incentive for prudent behavior if the shareholder is not held responsible for corrective costs, including severance packages that may be required and unnecessary facilities and equipment.

**2.0 Topic: PEI Costs**  
**Reference: Exhibit C18-9, page 14**

2.1 The Review Panel report suggests that BC Hydro has been unable to implement technological changes effectively. PEI has been identified as a project that suffers from this failure. Please explain why AMPC believes the disallowance of some PEI costs will incent BC Hydro to improve in this area.

**Response:**

The “gold standard” culture noted by the government panel cannot survive where the costs of projects that may not represent the least cost or most effective solutions to a clearly identified need are substantially disallowed. Disallowance is the only effective incentive available to the regulator.

2.2 As an alternative to disallowing costs, have the benefits identified in the business case tracked and included in future revenue requirement applications. Ratepayers are assured a benefit and the shareholder could

benefit to the extent that actual benefits exceed those identified in the business case. Please comment.

**Response:**

Benefits of this nature are often speculative and difficult to confirm, as the costs of the prior approach or alternatives are no longer available for comparison. The proposal to credit future ratepayers with the benefits would face validation difficulties and controversy unless the formula was predetermined. However, for large investments the approach may be appropriate and worthwhile.

**3.0 Topic: Recommendation on OMA**  
**Reference: Exhibit C18-9, page 15**

3.1 Could AMPC provide an estimate of the revenue requirement reduction that would result if the Recommendation on OMA was adopted?

**Response:**

AMPC anticipates that employee reductions and supporting costs will affect OM&A, deferral accounts and capital and related return and does not have the information at this time to determine the impact on revenue requirements. The following is illustrative only and information will have to be provided by BC Hydro or assumptions made.

- For example only, a reduction in the work force of an additional 600 employees (\$150,000 per employee), assuming 75% are OM&A would lower OM&A \$67.5 million and assuming 60% are OM&A would lower OM&A \$54 million. This would be a permanent decrease in costs.
- Restructuring costs, whether deferred or in OM&A are not or may not be all identified. Outsourcing implementation is \$33.5 million (Ex. B-1-3, App A, Sch 2.2). Other costs included in OM&A are not known. For illustrative purposes only, an amount of \$12 million is assumed. This would be a one-time reduction in deferrals and revenue requirements.
- Facilities, equipment and other costs related to excess employees are not known at this time. For illustrative purposes only, an amount of \$50,000 per employee or \$60 million is assumed. At 15% cost of capital and depreciation, the annual revenue requirements impact would be \$9 million. This decrease in revenue requirements, deferrals accounts and capital would persist until the facilities and equipment are eliminated or required for normal growth.
- The BC Hydro Review Panel noted that Performance Pay in F2010 was \$42.3 million (p. 6). 50% would be \$21.2 million.

- For illustrative purposes, if the cost of Consultants & Contractors of \$252.3 million was reduced by 50%, the impact on the revenue requirement would be \$126.2 million, subject to any deferrals. A 25% OM&A reduction would be \$63.1 million.<sup>1</sup>
- Disallowing 75% of PEI costs would reduce the amortization by \$4 million and should also reduce the related financing costs on approximately \$28.9 million (\$1.2 million).
- Disallowance of \$43.2 million in GMS 3 costs would reduce the HDA accounts and future recoveries through the DARR but would not have an immediate effect on rates.

The above reductions are illustrative only and important information is required from BC Hydro in order to make a reasonable determination. The total reduction in Revenue Requirements based on the assumptions made above would be \$164.5 million (\$54.0 + \$12.0 + \$9.0 + \$21.2 + \$63.1 + \$4.0 + \$1.2 million).

**4.0 Topic: IT Costs**  
**Reference: Exhibit C18-9, page 17-18.**

4.1 What weight if any should be given to soft costs in justifying IT projects?

**Response:**

The reference discusses soft benefits only. In economic evaluations such as in a business case, soft benefits should be given weight only when projects are at the margin and there are real advantages that can be identified and measured in the future.

**5.0 Topic: DSM Costs**  
**Reference: Exhibit C18-9, page 23- 25**

5.1 Does AMPC support the expensing of DSM administration costs?

**Response:**

Yes. The cost of administering DSM programs should be expensed in the period they are incurred.

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<sup>1</sup> Consultant and Contractor costs are set out on page 13 of the AMPC evidence and for F2013 are \$252.3 million which is less than the cost of Services of \$367.7 million shown in Ex B-1-3, App A, Sch 5.0.

5.2 Does AMPC have a timeline in mind for the review of DSM?

**Response:**

DSM expenditures should be curtailed or at least not increased until a thorough review of DSM investments and demand responses is concluded.

**6.0 Topic: Conclusion**  
**Reference: Exhibit C18-9, page 31, lines17-19**

6.1 Please prioritize your costs reduction steps.

**Response:**

Prioritized cost reduction steps follow:

1. Identify the essential functions of an electric utility that customers broadly expect BC Hydro to perform and customers are willing to support through electricity rates.
2. Transparently identify functions currently performed by BC Hydro (as a result of legislative or Ministerial direction or otherwise) that would be more appropriately performed by a government agency and funded through taxation.
3. Identify functions currently performed by BC Hydro that can be more effectively delivered by a functioning marketplace for goods and services and competitive-organizations operating in that marketplace.
4. Design an efficient organizational structure without duplication and with appropriate authorities and accountability that will best deliver only the functions described in step #1.
5. Staff the organization designed in step #4 appropriately with regard for economic regulation where shareholder's profit is what remains after all costs have been serviced under a revenue cap set by the regulator simulating market forces.

6.2 Does AMPC want the Commission's identification of Government Policy impact on BC Hydro rates to be part of this revenue requirement application?

**Response:**

Yes. BC Hydro should identify the rate impact of all policy decisions that result in significant expenditures, regardless of policy origin or precedent. Where BC Hydro's policy is the result of government direction (such as limitations on the use of natural gas, or mandatory metering technology) then public interest and future policy development is better served if the costs and benefits of alternative approaches are fully understood. Setting

just and reasonable rates includes, in AMPC's view, transparent rate-making and clear identification of alternatives and cost drivers.