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Utilities Commission

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December 13, 2018

Sent via email

Mr. Doug Slater
Director, Regulatory Affairs
FortisBC Energy Inc.
16705 Fraser Highway
Surrey, BC V4N 0E8
gas.regulatory.affairs@fortisbc.com

Re: FortisBC Energy Inc. – Annual Review for 2019 Delivery Rates – Project No. 1598966 – Final Order

Dear Mr. Slater:

With respect to your July 26, 2018 Annual Review for 2019 Delivery Rates Application, enclosed please find British Columbia Utilities Commission Order G-237-18, regarding the above noted matter.

Sincerely,

Original Signed by Ian Jarvis for:

Patrick Wruck
Commission Secretary

/aci

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ORDER NUMBER
G-237-18

IN THE MATTER OF
the *Utilities Commission Act*, RSBC 1996, Chapter 473

and

FortisBC Energy Inc.
Annual Review for 2019 Delivery Rates

BEFORE:
R. I. Mason, Panel Chair/Commissioner
D. J. Enns, Commissioner

on December 13, 2018

ORDER

WHEREAS:

A. On September 15, 2014, the British Columbia Utilities Commission (BCUC) issued its decision and Order G-138-14 for FortisBC Energy Inc. (FEI) approving a Multi-Year Performance Based Ratemaking (PBR) Plan for 2014 through 2019 (PBR Decision). In accordance with the PBR Decision, FEI is to conduct an annual review process to set delivery rates for each year;

B. By letter dated July 26, 2018, FEI proposed a regulatory timetable for its annual review for 2019 delivery rates;

C. By Order G-143-18 dated July 31, 2018, the BCUC established the regulatory timetable for the annual review for FEI's 2019 delivery rates, which included the anticipated date for FEI to file its annual review materials, the deadline for intervener registration, one round of information requests, a workshop, FEI's response to undertakings at the workshop, and written final and reply arguments;

D. On August 3, 2018, FEI submitted its materials for the Annual Review for 2019 Delivery Rates Application (Application). FEI also submitted an evidentiary update to the Application on September 26, 2018 and an amendment to its delivery rate request on October 23, 2018;

E. On October 19, 2018, FEI submitted a request to the BCUC for approval of a 1.1 percent increase to delivery rates on an interim and refundable basis and to set various delivery rate riders on an interim basis, effective January 1, 2019, pending the BCUC's decision regarding FEI's 2019-2022 Demand Side Management (DSM) Expenditures Application filed on June 22, 2018 (DSM Application);

F. Pursuant to section 44.2(2) of the *Utilities Commission Act* (UCA), the BCUC may not consent under section 61 of the UCA to an amendment to a schedule filed under section 61 to the extent that the amendment is for the purpose of, among other things, recovering expenditures on demand side measures the public utility anticipates making during the period addressed by the schedule, unless the amendment is for the purpose of setting an interim rate;

G. By Order G-208-18 dated November 5, 2018, the BCUC approved FEI's request for interim delivery rates and rate riders effective January 1, 2019; and

H. The BCUC has reviewed the Application and evidence filed in the proceeding and considers that approval is warranted.

NOW THEREFORE pursuant to sections 59 to 61 and 89 of the UCA, for the reasons attached as Appendix A to this order, the BCUC orders as follows:

1. FEI's interim rates and rate riders, effective January 1, 2019, which were approved by Order G-208-18, will remain interim and refundable/recoverable, until the completion of the DSM Application proceeding.
2. The following deferral account requests are approved:
    a. Creation of a rate base deferral account for the 2019-2022 DSM Expenditures regulatory proceeding with a four-year amortization period;
    b. Amendment of the existing rate base 2017 Long-Term Resource Plan Application deferral account to also capture the regulatory proceeding costs related to the application, as well as a three-year amortization period commencing in 2019;
    c. A five-year amortization period for the existing 2017 Rate Design Application deferral account, commencing in 2019; and
    d. Creation of a non-rate base deferral account, attracting a Weighted Average Cost of Capital (WACC) return, for the development costs related to the Transmission Integrity Management Capabilities (TIMC) project, with disposition to be proposed by FEI in a future application.
3. FEI is approved to continue debiting the Midstream Cost Reconciliation Account (MCRA) and crediting the delivery margin revenue in the amount of $3.6 million for 2019, as described in Section 5.3.2 of the Application.
4. Z-factor treatment is approved for the 2019 Employer Health Tax and 2018 and 2019 Medical Service Plan (MSP) premium reductions, as described in Section 12.2 of the Application.
5. FEI is directed to comply with all reporting requirements outlined in the Reasons for Decision attached as Appendix A to this order.
6. FEI is directed to file as a compliance filing the finalized financial schedules for the 2019 test period no later than 15 days from the date of the issuance of the BCUC's decision on the DSM Application.

DATED at the City of Vancouver, in the Province of British Columbia, this 13th day of December 2018.

BY ORDER

Original Signed by:

R. I. Mason
Commissioner

Attachment

FortisBC Energy Inc.

Annual Review for 2019 Delivery Rates

Reasons for Decision

December 13, 2018

Before:
R. I. Mason, Panel Chair/Commissioner
D. J. Enns, Commissioner

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1.0 Introduction

1.1 Background

By Order G-138-14 dated September 15, 2014, the British Columbia Utilities Commission (BCUC) approved a Performance Based Ratemaking (PBR) Plan for FortisBC Energy Inc. (FEI) covering a six-year period commencing in 2014. A primary purpose of the PBR Plan is to create an incentive for FEI to seek out sustainable operating and capital savings while maintaining service quality as measured by Service Quality Indicators (SQIs). The PBR Plan provides for an equal sharing of any PBR-related savings between customers and FEI.

A key element of the PBR Plan is the provision for an annual review. As part of the FEI Application for Approval of a Multi-Year PBR Plan for 2014 through 2019 Decision (PBR Decision), the BCUC set out the following items to be addressed at each annual review:

1. Evaluation of the operation of the PBR Plan in the past year(s) and identification by any party of any deficiencies/concerns with the operation of the PBR Plan that have become apparent.
2. Review of the current year projections and the upcoming year's forecasts.
3. Identification of any efficiency initiatives that FEI has undertaken, or intends to undertake, that require a payback period extending beyond the PBR Plan period and make recommendations to the BCUC with respect to the treatment of such initiatives.
4. Review of any exogenous events that FEI or stakeholders have identified that should be put forward to the BCUC for a decision as to their exclusion from the PBR Plan.
5. Review of FEI's performance with respect to SQIs and make recommendations to the BCUC where there has been a "sustained serious degradation" of service.
6. Assess and make recommendations with respect to any SQIs that should be reviewed in future annual reviews.
7. Assess and make recommendations to the BCUC on the scope for future annual reviews.[1]

1.2 The application and approvals sought

On August 3, 2018, FEI filed its Annual Review for 2019 Delivery Rates Application (Application). As set out in the Application and as updated and amended, FEI seeks the following approvals pursuant to sections 59 to 61 of the *Utilities Commission Act* (UCA):[2]

1. A permanent delivery rate increase of 1.1 percent, before consideration of rate riders, effective January 1, 2019.
2. The following deferral account approvals as described in Sections 7.5 and 12.4 of the Application:
    a. Creation of a rate base deferral account for the 2019-2022 Demand Side Management (DSM) Expenditures regulatory proceeding with a four-year amortization period;

[1] FEI Application for Approval of a Multi-Year Performance Based Ratemaking Plan for 2014 through 2019 (PBR), Decision dated September 15, 2014, pp. 185-186.
[2] FEI Reply Argument, pp. 1-2.

b. Amendment of the existing rate base 2017 Long-Term Resource Plan (LTRP) Application deferral account to also capture the regulatory proceeding costs related to the application, as well as a three-year amortization period commencing in 2019;

c. A five-year amortization period for the existing 2017 Rate Design Application deferral account, commencing in 2019; and

d. Creation of a non-rate base deferral account, attracting a Weighted Average Cost of Capital (WACC) return, for the development costs related to the Transmission Integrity Management Capabilities (TIMC) project, with disposition to be proposed in a future application.

3. The following rate riders, as described in Section 10.2 of the Application:

    a. A Biomethane Variance Account (BVA) Rate Rider for 2019 in the amount of $0.018 per gigajoule (GJ); and

    b. Revenue Stabilization Adjustment Mechanism (RSAM) riders for 2019 in the amount of $(0.045) per GJ as set out in Table 10-10 of the Application.

4. The continued debiting of the Midstream Cost Reconciliation Account (MCRA) and crediting of the delivery margin revenue in the amount of $3.6 million for 2019, as described in Section 5.3.2 of the Application.

5. Z-factor treatment for the 2019 Employer Health Tax (EHT) and 2018 and 2019 Medical Service Plan (MSP) premium reductions, as described in Section 12.2 of the Application.

These approvals are addressed in Section 2 of the Reasons for Decision.

In addition to the approvals sought by FEI, a primary area of focus by interveners during the proceeding was evaluating the PBR Plan and looking ahead to FEI's planned approach to setting rates beyond the PBR Plan term. This is addressed in Section 3 of the Reasons for Decision.

1.3 Application review process

In accordance with the Regulatory Timetable established by Order G-143-18 and amended by BCUC letter dated October 25, 2018, the following review process was undertaken:

- One round of BCUC and intervener Information Requests (IRs);
- A workshop open to all participants held on October 2, 2018 (Workshop);
- An opportunity for FEI to file responses to undertakings arising from the information requested at the Workshop;
- Written final arguments from interveners filed by October 30, 2018; and
- FEI's written reply argument filed by November 6, 2018.

The following interveners registered in the proceeding:

- BC Sustainable Energy Association and the Sierra Club of British Columbia (BCSEA-SCBC);
- British Columbia Old Age Pensioners' Organization *et al.* (BCOAPO);
- Canadian Office and Professional Employees' Union, Local 378 (MoveUP); and
- Commercial Energy Consumers Association of British Columbia (CEC).

1.4 2019 interim and permanent delivery rates

In the Application, FEI forecasts an increase in the delivery rate of 0.5 percent from 2018, but proposes to hold 2019 rates at 2018 levels by amortizing a portion of the existing 2017–2018 Revenue Surplus deferral account balance to offset the 2019 revenue deficiency.[3]

On September 26, 2018, FEI filed an evidentiary update to the Application (Evidentiary Update). FEI explains that the following five items have resulted in changes to the Application and the resulting increase to the revenue deficiency effective January 1, 2019:

1. Implementation of FEI's approved rate design proposals pursuant to Order G-135-18;
2. Update to the Average Weekly Earnings (AWE)-BC index;
3. Update to the termination of FEI's Lease In Lease Out agreement with the City of Kelowna;
4. Update to FEI's projected 2018 capital expenditures; and
5. Update to Prescribed Undertaking 3.6 expenditures.[4]

The combined impact of the above items increases the forecast 2019 revenue deficiency by $4.444 million, resulting in a revised delivery rate increase of 1.1 percent from 2018 delivery rates. FEI continues to propose to hold 2019 rates at 2018 levels by amortizing a portion of the existing 2017–2018 Revenue Surplus deferral account balance to offset the revised 2019 revenue deficiency.[5]

However, on October 19, 2018, FEI submitted a request to the BCUC for approval of a 1.1 percent increase to delivery rates on an interim and refundable basis, effective January 1, 2019 (Interim Rate Application), [6] pending the BCUC's decisions regarding the Application and the 2019–2022 DSM Expenditures Application (DSM Application), filed with the BCUC for acceptance on June 22, 2018. Pursuant to section 44.2(2) of the UCA, the BCUC may not consent under section 61 of the UCA to an amendment to a schedule filed under section 61 to the extent that the amendment is for the purpose of, among other things, recovering expenditures on demand-side measures the public utility anticipates making during the period addressed by the schedule, unless the amendment is for the purpose of setting an interim rate.

Subsequent to filing the Interim Rate Application, on October 23, 2018, FEI amended its delivery rate request in the Application to a 1.1 percent increase, effective January 1, 2019, consistent with the Interim Rate Application. FEI states that it is expecting an increase in rates in 2020 due to the Lower Mainland Intermediate Pressure System Upgrade (LMIPSU) project coming into service. In addition, FEI states that by implementing the 1.1 percent delivery rate increase in 2019 and preserving the 2017–2018 Revenue Surplus deferral account balance for rate smoothing, the impact will be overall smoother rates for customers over the next few years.[7]

By Order G-208-18 dated November 5, 2018, the BCUC approved the Interim Rate Application.

[3] Exhibit B-2, p. 1.
[4] Exhibit B-2-1, p. 1.
[5] Exhibit B-2-1, p. 4.
[6] Exhibit B-10.
[7] Exhibit B-11, p. 1.

2.0 Determinations on approvals sought

2.1 2019 delivery rates and the 2017–2018 Revenue Surplus deferral account

As previously described, FEI originally requested in the Application and in the Evidentiary Update to hold the 2019 rates at 2018 levels by amortizing a portion of the existing 2017–2018 Revenue Surplus deferral account to offset the forecast 2019 revenue deficiency. However, subsequent to the Workshop, FEI amended the Application to request a rate increase of 1.1 percent for 2019 and to preserve the balance in the 2017–2018 Revenue Surplus deferral account for future rate smoothing purposes.

FEI's rationale for the 1.1 percent rate increase is to reduce rate volatility, stating that preserving the balance in the 2017–2018 Revenue Surplus deferral account should mitigate the impact of the expected rate increase in 2020 resulting from the LMIPSU project coming into service.[8]

In the Reasons for Decision regarding the Annual Review for 2017 Delivery Rates, FEI received approval to establish the 2017 Revenue Surplus deferral account to capture the 2017 revenue surplus.[9] In the Reasons for Decision regarding the Annual Review for 2018 Rates, FEI received approval to add the 2018 revenue surplus to the 2017 Revenue Surplus deferral account and change the name of the account to the 2017–2018 Revenue Surplus deferral account (Deferral Account).[10]

The primary cause of the revenue surpluses was the delay in the completion of large capital projects, such as the Tilbury Expansion project, which delayed the timing of when these projects entered rate base.[11] During the 2017 and 2018 annual reviews, FEI proposed freezing its rates and preserving the balance in the Deferral Account to smooth future rates in anticipation of large capital projects entering rate base in the upcoming years.[12] As stated above, the BCUC approved this treatment as it would result in less rate volatility (i.e. avoiding a rate decrease followed by a large rate increase) and the surplus could be used to mitigate anticipated future large rate increases caused by large capital projects, such as the Tilbury Expansion project, entering rate base in the upcoming years.[13] The projected after-tax balance in the Deferral Account is approximately $30 million at the end of 2018.[14]

In this Application, FEI forecasts the Tilbury Expansion project and a portion of the LMIPSU project to enter rate base on January 1, 2019. These projects contributed to FEI's forecast rate increase of 1.1 percent for 2019. The anticipated rate impact in 2020 of the remainder of the LMIPSU project coming into service and entering rate base in 2020 is the primary rationale for FEI's revised request to increase 2019 rates by 1.1 percent and preserve the Deferral Account balance.[15]

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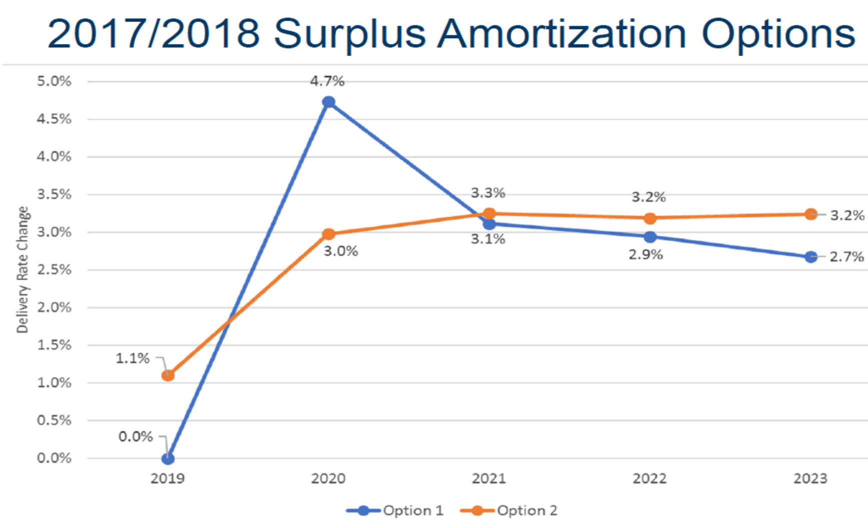
[8] Exhibit B-11, p. 1.
[9] Appendix A to Order G-182-16, p. 9.
[10] Appendix A to Order G-196-17, p. 4.
[11] FEI Annual Review for 2017 Delivery Rates proceeding, Exhibit B-2-1, pp. 1-2; FEI Annual Review for 2018 Delivery Rates proceeding, Exhibit B-2-1, pp. 1-2.
[12] FEI Annual Review for 2017 Delivery Rates proceeding, Exhibit B-11, Undertaking No. 3; FEI Annual Review for 2018 Delivery Rates proceeding, Exhibit B-2, p. 1.
[13] Appendix A to Order G-182-16, p. 9; Appendix A to Order G-196-17, p. 4.
[14] Exhibit B-2, p. 133.
[15] Exhibit B-11, p. 1; Workshop Transcript, p. 46.

During the Workshop, FEI presented the following graph, depicting the potential future rate impacts of two amortization options for the Deferral Account:[16]



Option 1 – 0% increase, uneven amortization over 3 yrs
Option 2 – 1.1% increase, uneven amortization over 3 yrs

The graph as set out above is based on the assumption that the remaining balance of the LMIPSU Project will enter rate base in 2020. Option 1 is consistent with FEI's original proposal to amortize approximately $6 million from the Deferral Account in 2019 to offset the revenue deficiency, and then amortize the remaining balance over the next few years to mitigate rate impacts from the LMIPSU Project and other unforeseen items. Option 2 is to increase the 2019 rates by 1.1 percent and preserve the approximately $30 million balance in the Deferral Account to amortize over the next few years. [17]

Position of the parties

In its final argument, BCOAPO notes its concern with FEI's "last minute" amendment to the delivery rate request and FEI's inability to foresee the circumstances that led to the change earlier in the process. However, BCOAPO does not oppose the requested rate increase given that it would result in some smoothing of rates for ratepayers. [18]

FEI responds to BCOAPO by referencing the reasons provided in its October 23, 2018 submission related to rate smoothing and expected cost pressures in 2020 from the LMIPSU project coming into service.[19] FEI also references the PowerPoint slide presented at the Workshop, and reproduced above, which shows the rate smoothing benefits of increasing rates in 2019 by 1.1 percent.[20]

During the Workshop, CEC expressed concerns about the surplus balance in the Deferral Account, as it means that FEI has over-collected from ratepayers in the past, and inquired if FEI has taken steps to avoid this.[21]

[16] Exhibit B-8, slide 11.
[17] Workshop Transcript, pp. 46-47.
[18] BCOAPO Final Argument, pp. 5-6.
[19] FEI Reply Argument, p. 3.
[20] Exhibit B-11, p. 1.
[21] Workshop Transcript, pp. 50-51.

In response, FEI stated that in its view, although ratepayers would like to avoid over-collection, they are not harmed because they are receiving a WACC return on that over-collection. Furthermore, FEI believes that ratepayers would like to avoid rate volatility, and that returning the over-collection now would result in a rate decrease followed by a large rate increase.[22] FEI also stated that it would be preferable to use the surplus in the Deferral Account to smooth rates in the future as needed, rather than to set a fixed amortization amount.[23]

No other interveners raised an issue with FEI's revised request to increase delivery rates by 1.1 percent effective January 1, 2019. BCSEA-SCBC supports the request, stating that it "agrees that as a general principle, rate volatility is undesirable" and that it concurs that the 1.1 percent delivery rate increase in 2019 causes less rate volatility than a rate freeze when considering the expected rate impact in 2020 of the LMIPSU project.[24]

BCUC determination

The Panel agrees with FEI that increasing the delivery rate in 2019 and preserving the Deferral Account balance will likely result in smoother rates for customers over the next few years. However, the Panel is cognizant of the fact that the balance in the Deferral Account has been accumulating over the last two years and represents a significant surplus to be returned to ratepayers. The Panel accepts FEI's proposal to continue to preserve the balance in the Deferral Account in 2019, but with the expectation that FEI will begin amortizing the balance in the near future as major capital projects, such as the LMIPSU project, enters rate base.

Based on the evidence and arguments presented by the parties, the Panel considers it appropriate to increase the 2019 delivery rates by 1.1 percent as proposed by FEI. The Panel agrees with FEI that increasing the delivery rate in 2019 and preserving the Deferral Account balance will result in smoother rates for customers compared to the alternative of amortizing a portion of the Deferral Account balance to offset the 2019 revenue deficiency. **Accordingly, FEI's interim rates, effective January 1, 2019, approved by Order G-208-18, will remain interim and refundable/recoverable, until the completion of the DSM Application.**

2.2 TIMC project and development cost deferral account

FEI requests approval to establish a new non-rate base deferral account to capture the development costs related to the TIMC project. [25]

The TIMC project consists of system modifications to enable the use of crack-detection inline inspection technology or Electro-Magnetic Acoustic Transducers (EMAT). FEI's assessments to-date indicate the need for and feasibility of the adoption of crack-detection capabilities within its in-line inspection program.[26] FEI is undertaking a quantitative risk assessment of its transmission pipeline assets to identify pipelines requiring modifications.[27]

FEI expects to incur development costs for the TIMC project over two phases, commencing in 2018 and continuing into mid-2020. The total development costs are forecast to be $41.6 million.[28] FEI plans to file a

[22] Workshop Transcript, p. 51.
[23] Ibid., p. 47.
[24] BCSEA-SCBC Final Argument, p. 4.
[25] Exhibit B-3, BCUC IR 21.3, 21.7.
[26] Exhibit B-3, BCUC IR 1.5, 8.9.
[27] Exhibit B-2, p. 127.
[28] Exhibit B-2, pp. 127, 129; Exhibit B-3, BCUC IR 21.5.

Certificate of Public Convenience and Necessity (CPCN) application for the TIMC project at the end of Phase 2, which will include a proposal for recovery of the deferral account balance.

In the absence of a deferral account, FEI states that the Phase 1 development costs, estimated at $11.62 million, would likely be classified as operating and maintenance (O&M) expenses and would be recovered from ratepayers in the year (or subsequent year) they are incurred. The Phase 2 development costs, estimated to be $30 million, would be classified as a combination of O&M and capital expenses. FEI states that if the TIMC development costs were not approved to be recorded in a deferral account, the resulting delivery rate increases would be 2.8 percent and 0.7 percent in 2019 and 2020, respectively. [29]

FEI was asked in an IR to provide past examples where it had requested deferral account approval for development costs in an amount comparable to the current request. FEI stated that it incurred approximately $27 million in development costs for the Southern Crossing Pipeline project CPCN in the late 1990s, which would equate to $40 million in today's dollars when applying a 2 percent inflation rate. FEI also stated that deferring development costs for large projects allows the cost of the complete project to be matched against the benefits when they are realized and that the matching of costs and benefits is an accepted basis for deferral accounts, as reflected in the BCUC's Regulatory Account Filing Checklist. This approach also smooths the rate impact of the project and avoids intergenerational inequity.[30]

Although not the subject of FEI's requests in the current Application, FEI provided an estimate in an IR response of the total TIMC project expenditures (excluding development costs). FEI projects an amount of $50 million in 2022 and $250 million in each of 2023 to 2025 and states that estimates beyond 2025 are not yet defined for the TIMC project.[31] FEI submits that these estimates are highly uncertain at this time given that the pipelines requiring modification and the priority and detailed integrity management solutions still need to be determined through the CPCN development process. Given the complexities and timeline, it is possible that FEI may not apply for the full extent of anticipated system modifications in its mid-2020 CPCN application. It is also possible for the TIMC CPCN application to extend to later years.[32]

Position of the parties

None of the interveners objected to FEI's deferral account request. However, during the Workshop, CEC expressed some concerns regarding the TIMC project itself, including the need, the timing of the regulatory review process and the scale of the proposed investment or cost of the project.[33] In particular, CEC inquired as to the possibility of having a regulatory review to assess the quantitative risk of FEI's system prior to bringing forward the EMAT solution in the TIMC project CPCN application.[34]

In response, FEI stated that the majority of pipeline operators in Canada already employ EMAT technology and cites Pacific Northern Gas as an example of a gas utility in British Columbia that runs EMAT tools in its system.[35] Furthermore, FEI stated that it has already assessed the risks and determined that running EMAT tools is the best way to respond to those risks. FEI submitted that the quantitative risk assessment would not determine whether the work needs to happen, but rather only identify the priority of where the work needs to happen. Given that stress corrosion cracking is a time-dependent threat that has already been detected in its system, FEI

[29] Exhibit B-2, p. 130; Exhibit B-3, BCUC IR 21.1.1; Exhibit B-9, Undertaking No. 2.
[30] Exhibit B-3, BCUC IR 21.3.
[31] Exhibit B-3-2, BCUC IR 21.4.
[32] Ibid., BCUC IR 21.4.
[33] Workshop Transcript, p. 87.
[34] Ibid., pp. 82, 84.
[35] Ibid., pp. 87-88.

would like to undertake the work as soon as possible.[36] In FEI's view, due to its highly technical nature, it would be more beneficial to have a regulatory review of the quantitative risk assessment along with the other work that is happening, rather than a review of the quantitative risk assessment on its own.[37]

With respect to the cost of the project, FEI explained that the cost per kilometre to run EMAT tools in its system would be higher compared to utilities that have longer point-to-point pipelines. FEI noted, for example, that its system stops at a number of stations throughout the Lower Mainland, and its system is not comprised of straight pipelines that are point-to-point.[38] FEI also stated that it would be open to conducting a workshop to discuss the project and the impact to its customers and to its system.[39]

BCUC determination

The Panel acknowledges that FEI's request for a development cost deferral account is relatively standard and that such accounts have been approved in the past. However, the Panel considers the magnitude and breadth of both the development costs and especially the TIMC project itself to be atypical. Of particular concern at this time is the lack of certainty around cost amounts beyond the Phase 1 development costs and the lack of certainty about the project timing and scope. For instance, the Panel notes FEI's statement in an IR response that the Phase 2 development costs, estimated to be $30 million, have a "high degree of uncertainty" and are described as a "placeholder until more detailed estimates are developed".[40]

Despite the Panel's concerns regarding the magnitude, breadth and uncertainty of the project costs and scope, the Panel finds FEI's request to establish a non-rate base deferral account to record the development costs related to the TIMC project to be reasonable. The Panel agrees that deferring the development costs will mitigate the rate increases that would occur in the absence of a deferral account. Further, use of a deferral account allows for the matching of development costs with the future benefits of the project, which mitigates intergenerational equity issues.

In consideration of the above, the Panel approves FEI's request to establish a non-rate base deferral account, attracting a WACC return, for the development costs related to the TIMC project.

The Panel is mindful of the concerns raised by CEC at the Workshop and we have previously commented on the magnitude of the estimated project costs. The Panel is also concerned about the potential impact on future rates given the uncertainty of the costs and the fact that it could be at least two years until a full regulatory review of the project is initiated. Accordingly, the Panel appreciates FEI's statement that it would be amenable to holding a workshop to discuss the TIMC project [41] and we encourage FEI to conduct this workshop in due course.

To assist the BCUC with monitoring the progress of the project and the project development costs being incurred, **the Panel directs FEI to file the following information in its next revenue requirement application, which is expected to be filed sometime in 2019:**

[36] Ibid., pp. 82-83; Exhibit B-3, BCUC IR 8.9.
[37] Workshop Transcript, p. 84.
[38] Ibid., p. 86.
[39] Ibid., pp. 84-85.
[40] Exhibit B-3, BCUC IR 21.2.
[41] Workshop Transcript, pp. 84-85.

1) **Updated actual and forecast project development costs compared to budget with explanations for variances;**
2) **Updated timeline for when FEI anticipates filing the CPCN with explanations for changes; and**
3) **Details on project scope and deliverables, including any changes thereto from what was provided in the current annual review proceeding.**

2.3 Other approvals sought

In addition to the approvals sought discussed in Sections 2.1 and 2.2 of these Reasons for Decision, FEI seeks approvals related to a number of deferral accounts and rate riders, as well as approvals related to the treatment of the MCRA and two items it has identified as qualifying for exogenous, or Z-factor, treatment. These requests are described in Section 1.2 of these Reasons for Decision.

No issues or objections were raised by interveners with respect to the aforementioned requests.

BCUC determination

The Panel finds the deferral account and rate rider requests reasonable as they are consistent with previous treatment of regulatory proceeding costs and with the previous treatment of rate riders, and there are no circumstances currently that would compel a different treatment. **Therefore, the Panel approves the following:**

- **Creation of a rate base deferral account for the 2019–2022 DSM Expenditures regulatory proceeding with a four-year amortization period;**
- **Amendment of the existing 2017 LTRP Application deferral account to also capture the regulatory proceeding costs related to the LTRP application, and a three-year amortization period commencing in 2019;**
- **A five-year amortization period for the existing 2017 Rate Design Application deferral account commencing in 2019; and**
- **The continued debiting of the MCRA and crediting of the delivery margin revenue as described in Section 5.3.2 of the Application.**

The Panel notes that the BVA Rate Rider and RSAM riders were approved effective January 1, 2019 on an interim basis by Order G-208-18. **The BVA Rate Rider and RSAM riders will remain interim until the completion of the DSM Application.**

With regard to FEI's request for Z-factor treatment for the 2019 EHT and the 2018 and 2019 MSP premium reductions, the Panel notes that in the PBR Decision, the BCUC approved five criteria that an event must meet in order to receive exogenous factor or "Z-factor" treatment. In Section 12.2 of the Application, FEI provides the exogenous factor criteria approved in the PBR Decision and explains how the 2019 EHT and the 2018 and 2019 MSP premium reductions qualify for Z-factor treatment.[42]

FEI explains that the EHT was announced by the provincial government in February of 2018, and is a tax levied on businesses' payrolls that comes into effect on January 1, 2019. Similarly, the MSP premiums reduction was

[42] Exhibit B-2, p. 121.

announced by the provincial government in December of 2017, which is a 50 percent reduction, effective January 1, 2018. In February of 2018, the provincial government announced the elimination of MSP premiums by January 1, 2020.[43]

The Panel finds the 2019 EHT and the 2018 and 2019 MSP premium reductions meet the criteria for exogenous factor treatment. **Therefore, the Panel approves Z-factor treatment for the 2019 EHT and the 2018 and 2019 MSP premium reductions.**

3.0 PBR evaluation and future considerations

During the Workshop and in final arguments, many of the interveners raised issues regarding the overall PBR Plan, including expressing views on what actions should be taken at the conclusion of the current PBR Plan. As mentioned in Section 1.1 of these Reasons for Decision, a primary purpose of the PBR Plan is to create an incentive for FEI to seek out sustainable operating and capital savings while maintaining service quality as measured by the SQIs. As such, the BCUC set out seven items to be addressed at each annual review. As this is the last annual review for this PBR term, some of these items are no longer applicable. The items that are applicable and are not addressed elsewhere in these Reasons for Decision, are discussed below along with the issues and views raised by the parties in the proceeding.

3.1 PBR evaluation

As directed in the PBR Decision, an evaluation of the operation of the PBR Plan is to be undertaken as part of the annual review process. This evaluation is provided below in the context of FEI’s O&M, capital spending and SQIs during the PBR term.

O&M

FEI states that under the PBR Plan it has achieved approximately $43 million in O&M savings that is shared with its customers.[44]

While FEI has achieved O&M savings in each of the years of the PBR Plan term thus far, the following table shows a decline in O&M savings in the latter years: [45]

[43] Exhibit B-2, pp. 121-122.
[44] Exhibit B-2, p. 5.
[45] Ibid., Table 1-2, p. 5.

Table 1-2: Formula O&M Savings 2014 to 2018 ($ millions)

	Actual	Formula	Variance	1.1% PIF
2014	$ 191.0	$ 198.5	$ 7.5	$ 2.2
2015	$ 225.4	$ 235.6	$ 10.2	$ 2.6
2016	$ 225.9	$ 238.1	$ 12.1	$ 2.6
2017	$ 232.5	$ 240.4	$ 7.9	$ 2.6
* 2018	$ 238.6	$ 243.6	$ 5.0	$ 2.7
Cumulative Savings			$ 42.8	$ 12.7

* 2018 is projected.

Corresponding with the trend in O&M savings, staffing levels have increased in the latter years of the PBR term, as shown in the following table: [46]

Table 1-3: Employees at Year-End[6]

	Headcount	FTEs
2013 Actual	1,764	1,679
2014 Actual	1,704	1,650
2015 Actual	1,656	1,573
2016 Actual	1,667	1,581
2017 Actual	1,735	1,648
2018 Projected	1,816	1,727

With respect to O&M savings during the PBR term, FEI states that it "continues to be faced with the increasingly difficult challenge of finding new productivity opportunities to meet the annual savings embedded in the formula, and to sustain the level of incremental O&M savings achieved in recent years."[47] FEI also states that in the earlier years of the PBR term, Full Time Equivalents (FTEs) were reduced as a result of management reorganization and initiatives undertaken, such as Project Blue Pencil, which resulted in reductions to Customer Service. FEI expects staffing levels to continue to increase in 2018 "to meet customer growth and other capital requirements."[48]

For 2018, FEI states the following factors contribute to the decrease in formula O&M savings:

- The Productivity Improvement Factor;
- Difficulty in finding new productivity opportunities; and
- Cost pressures.[49]

[46] Exhibit B-2, Table 1-3, p. 6.
[47] Ibid., p. 5.
[48] Ibid., p. 6.
[49] Exhibit B-3, BCUC IR 1.1.

FEI provides the following examples of cost pressures that it is experiencing and states that it expects many of these cost pressures to continue into the future:

- The evolving risks of changing cyber security landscape;
- The growth and aging of FEI's pipeline and distribution system;
- Rising vehicle fuel and insurance costs and municipal fees; and
- Remediation activities related to erosion, landslides and fires in the Interior regions of the province.[50]

FEI explains that under the PBR Plan there is a natural decline in formula O&M savings due in part to fewer "financially attractive and achievable opportunities to undertake" as the PBR Plan progresses because the PBR Plan incents FEI to implement initiatives earlier on in the PBR term to allow a longer evaluation period for efficiencies and savings. FEI submits that it will be continually difficult to find new productivity opportunities if there is a renewal or continuation of the PBR Plan.[51]

Capital spending

FEI's capital spending has been above the PBR formula amount in each year of the PBR term and FEI expects this trend to continue.[52] FEI projects that as of the end of the fifth year of the PBR Plan term (i.e. the end of 2018), actual total capital spending (excluding non-formula capital expenditures) will be $157 million, or 21.8 percent, higher than formula.[53]

In the PBR Decision, the BCUC established both a one-year 10 percent capital dead-band, and a two-year 15 percent cumulative capital dead-band with regard to FEI's formula-driven capital spending.[54] FEI has exceeded the cumulative capital dead-band in each of the last three years of the PBR Plan (i.e. 2016, 2017 and 2018).[55]

Consistent with previous years' treatment of the capital expenditures in excess of the dead-band, FEI has removed the amount of formula capital in excess of the cumulative dead-band from the earnings sharing calculation for 2018 and added it to its opening 2019 plant additions balance.[56]

SQIs

FEI has performed better than the threshold results in all years of the PBR term, and has performed better than the benchmark results in almost all years for all nine of the applicable SQIs. For the four SQIs that are informational only, FEI's performance was consistent with prior years.[57]

Position of the parties

Interveners' comments on FEI's performance during the PBR term and FEI's reply are summarized below.

[50] Ibid., BCUC IR 1.1.
[51] Exhibit B-6, MoveUP IR 2.9, 2.10, 2.12.
[52] Exhibit B-2, pp. 10-11.
[53] Exhibit B-2-1, Table 1-4, p. 11.
[54] FEI PBR Decision, p. 81.
[55] Exhibit B-2-1, Table 1-4, p. 11.
[56] Exhibit B-2, p. 14; Exhibit B-3, BCUC IR 11.1.
[57] Up to June 2018 year-to-date results: Exhibit B-2, Tables 13-1-13-15, pp. 138-150.

O&M

In MoveUP's view, the funds available for earnings sharing have been "trivial" and it is difficult to find "specific and concrete gains that would not have been just as available under a more traditional regulatory cycle."[58]

Similarly, CEC questions whether "the O&M 'savings' could and/or should have been achievable under Cost of Service regulation."[59]

FEI submits that although it would not be possible to know what would have resulted under a forecast cost of service ratemaking mechanism, in its view, "the savings and efficiencies achieved to date have been driven in full or in part by the incentive mechanisms and other features of the PBR Plan…."[60] FEI further submits that its "total O&M has trended down over the PBR term," its "delivery rates are trending below inflation" and it has "surplus revenue in the 2017–2018 Revenue Surplus account available to offset future rate increase."[61]

Capital spending

With respect to FEI's capital spending, BCOAPO questions the usefulness of the capital expenditure formula given that the actual capital expenditures have substantially exceeded the formula in almost all years of the PBR Term.[62]

CEC submits that the calculation of the dead-band adjustment is mathematically flawed and should be corrected in this and any future PBRs.[63]

FEI submits that the PBR Plan has provided more certainty and flexibility for its capital planning and enabled it to achieve savings it otherwise would not have.[64] FEI also notes that its "shareholder does not earn [a return] on half of all capital expenditures within the dead band, and the shareholder's return on all capital above the dead band is delayed until the following year."[65]

With respect to the calculation of the dead-band, FEI states that the cumulative two-year variance was calculated in accordance with the PBR Decision. Further, FEI sees no value in adjusting the calculation in the final year of the PBR Plan and notes that it will not be proposing a two-year dead band in the future.[66]

SQIs

None of the interveners have raised any issues regarding FEI's performance with respect to the SQIs approved by the BCUC in the PBR Decision.

BCUC determination

The Panel acknowledges the interveners' views regarding FEI's O&M savings. Although it cannot be known with any level of certainty what efficiencies could have been achieved under a different ratemaking mechanism, the

[58] MoveUP Final Argument, pp. 1-2.
[59] CEC Final Argument, p. 25.
[60] Exhibit B-6, MoveUP IR 2.2.
[61] FEI Reply Argument, pp. 7-8.
[62] BCOAPO Final Argument, p. 10.
[63] CEC Final Argument, pp. 3, 7.
[64] FEI Reply Argument, p. 7.
[65] Ibid., p. 7.
[66] Ibid., pp. 4-5.

Panel finds that O&M savings have been achieved and have been shared with FEI's customers during the PBR term. The Panel also finds that FEI has either maintained or increased its level of service quality as measured by the SQIs.

However, the Panel is concerned with the sustainability of the savings achieved as it appears that the savings are diminishing as the PBR term concludes. The Panel is also concerned with FEI's ability to find new productivity measures and savings in light of the cost pressures FEI is experiencing.

With respect to FEI's capital spending, the Panel shares the same concerns as were raised by the BCUC in the FEI Annual Review for 2017 Delivery Rates Reasons for Decision. These concerns include: (i) the continuing trend of capital expenditures exceeding the dead-band; (ii) the magnitude of the capital over-spending; and (iii) the impact on the incentive properties of the PBR Plan under FEI's approach of adding the capital expenditures in excess of the dead-band to the next year's opening plant in service.[67] However, the Panel recognizes that this being the final year of the PBR term there would be no value in rebasing the capital formula, and therefore agrees with FEI that its approach is appropriate under the circumstances. **Accordingly, the Panel approves FEI's proposal to remove the amount of formula capital which has exceeded the cumulative dead-band from the earnings sharing calculation, and to add the amount of capital in excess of the dead-band to FEI's opening 2019 plant additions balance.**

The Panel notes that FEI has been providing information annually on various O&M and capital issues, including the following: (i) information on major productivity initiatives; (ii) annual changes to headcount and FTEs; and (iii) cost breakdowns and explanations for sustainment/other and growth capital spending. This information is provided in compliance with BCUC directives in past annual reviews.

The Panel further notes the BCUC's statements in the FEI Annual Review of 2015 Delivery Rates Decision (2015 Annual Review Decision):

> …the Panel considers it essential during the PBR term for certain information to be gathered on efficiency initiatives, particularly with regards to how these initiatives impact the organizational structure of the Company and the expected savings and/or costs which result from these efficiency initiatives. The purpose of obtaining this information…is to gain an understanding of how savings are being achieved and to acquire some quantifiable data on these savings and initiatives throughout the PBR term.[68]

The Panel agrees with the BCUC's statements above that the information collected through the annual reviews is important to gain an overall understanding of the functioning of the PBR Plan, as the information provides some quantifiable data on O&M and capital spending at a more granular level. This information may then be used by parties to assist with the evaluation of the PBR Plan as a whole. Regardless of whether FEI's proposed rate-setting approach beyond the current PBR Plan term is cost of service or some form of PBR, the Panel expects that the application would include an evaluation of the current PBR Plan.

In consideration of the above, the Panel directs FEI to file the information contained in Appendices C2, C3 and C4 of the Application, as well as Table 1-4 of the Application, as part of FEI's upcoming revenue requirement application. The Panel expects that this information will be updated to include the actual 2018 results, if available, and projected 2019 results.

[67] Appendix A to Order G-182-16, pp. 16-17.
[68] 2015 Annual Review Decision, p. 34.

The Panel acknowledges CEC's concerns regarding the calculation of the cumulative capital dead-band adjustment. However, the Panel finds that changing this calculation in the last year of the PBR Plan term would be inappropriate as the results would be inconsistent with the previous years' results. Further, the two-year cumulative capital dead-band was directed by the BCUC as part of the PBR Decision and FEI has been performing this calculation in the same manner in each annual review. The Panel considers FEI's calculation to be a reasonable interpretation of the BCUC's determination in the PBR Decision and declines to deviate or re-interpret the directive provided in the PBR Decision.

3.2 Future considerations

During the Workshop and in final argument, FEI and the interveners made submissions regarding the next steps that should be considered once this PBR term concludes.

During the Workshop, FEI provided an overview of what it is considering for the next PBR plan. FEI states that the next PBR plan would be similar to the general structure of the current plan. A majority of the O&M and capital would be set by formula and the non-formula items would be forecast annually on a cost of service basis. Also, FEI referred to re-basing O&M and capital and adjusting some of the formulas for growth capital as examples of changes from the current PBR Plan.[69]

MoveUP questions whether a PBR mechanism is an appropriate mode of regulation for FEI.[70]

BCOAPO supports the consideration of alternative forms of rate regulation for the next regulatory cycle, such as:

- A one-year or multi-year cost of service; or
- A modified and more limited PBR plan that indexes only O&M revenues (with capital spending determined/approved in a mini-hearing).[71]

CEC recommends that prior to advancing a new PBR plan, the BCUC should hold a separate proceeding to evaluate the current PBR Plan and whether the O&M savings could have been achieved under a cost of service regulation.[72]

FEI submits that it has been "successful in achieving benefits for customers under the PBR Plan" and states that it plans to submit a proposal for a new PBR Plan in due course.[73] FEI also states that PBR has been implemented in multiple jurisdictions in Canada over many years and has been proven consistent with the regulatory compact and the obligations and entitlements under utilities regulation legislation. FEI further notes that it has been under a form of PBR for most of the past 20 years.[74]

In response to CEC, FEI submits that having a separate proceeding would be extremely inefficient from a regulatory perspective because an evaluation of the PBR Plan would likely be discussed during the next PBR application proceeding anyway.[75]

[69] Workshop Transcript, pp. 17-18.
[70] MoveUP Final Argument, p. 7.
[71] BCOAPO Final Argument, p. 11.
[72] CEC Final Argument, pp. 3, 25.
[73] FEI Reply Argument, pp. 5, 9.
[74] Ibid., p. 6.
[75] Ibid., p. 8.

Panel discussion

Similar to previous BCUC decisions on FEI's annual reviews during this PBR Plan, the Panel acknowledges the interveners' comments on the current PBR Plan and its views for moving forward at the conclusion of the current PBR term. However, these comments and views fall outside the scope of the current proceeding, and as such, the Panel makes no comments or determinations on the form of regulation that should take place at the conclusion of the PBR Plan term.