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British Columbia Utilities Commission
Sixth Floor, 900 Howe Street, Box 250
Vancouver, BC, V6Z 2N3
Attn: Patrick Wruck, Commission Secretary
By Email: commission.secretary@bcuc.com

Dear Sir:

Re: British Columbia Utilities Commission Review of British Columbia Hydro and Power Authority's Performance Based Regulation Report
B.C. Sustainable Energy Association (BCSEA), Topics and Questions for Staff Consultant

These are BCSEA's topics and clarifying questions for the Staff Consultant Pacific Economics Group Research, LLC (PEG) regarding PEG's February 28, 2020 report titled *Performance-Based Regulation: Basic Features and Possible Applications to BC Hydro*¹ (PEG Report). These are filed pursuant to the December 12, 2019 regulatory timetable² as clarified in the Commission's letter of March 9, 2020.³

The PEG Report provides a wealth of helpful background information about performance-based ratemaking (PBR) and cost of service ratemaking (COSR) related to energy utilities across North America and over many decades. However, BC Hydro's circumstances appear to be unusual if not unique in many respects that may be relevant to the merits of moving from a COSR system to a PBR system at the present time. BCSEA looks forward to the anticipated workshop on the PEG Report.

In this letter, BCSEA sets out the following topics, along with clarifying questions:

1. Shareholder's lack of a profit motive,
2. Existing "PBR mechanisms" applicable to BC Hydro,
3. PEG's response to BC Hydro's evidence not recommending PBR at this time,
4. Types of PBR mechanisms PEB says are suitable for BC Hydro, and
5. Marketing flexibility under PBR compared to COSR.

¹ Exhibit A2-5.

² Exhibit A-4, Order G-326-19.

³ Exhibit A-5.

1. Shareholder's lack of a profit motive

Would the prospect of enhanced earnings under PBR be an effective motivator for the BC Government (BC Hydro's Shareholder) to cause BC Hydro to contain costs more under PBR than it would under COSR?

Have the authors of the PEG Report considered that the BC Government may be more interested in reducing upward pressure on BC Hydro's rates and in achieving policy objectives such as low-carbon electrification than in increasing the government's earnings from BC Hydro? How does this affect the merits of moving BC Hydro to a PBR framework, in the authors' view?

Please address factors such as the following:

- Currently, the BC Government is transitioning to a more traditional mechanism in which its shareholder's income from BC Hydro is based actual, not deemed, debt/equity and a return on equity to be determined by the BCUC (in a future proceeding). This comes after many years during which the BC Government had complete control over the size of its earnings from BC Hydro. It seems to be understood that the new mechanism will result in less, not more, shareholder's revenue from BC Hydro at least for the foreseeable future. This suggests that BC Hydro's shareholder is motivated primarily by factors other than maximizing its shareholder's return.
- The BC Government recently absorbed a \$1.1 billion write-off of BC Hydro's Rate Smoothing Regulatory Account in order to put BC Hydro's finances on a better footing for limiting future rate increases. Where BC Hydro's shareholder is willing to absorb a \$1.1 billion write-off to reduce rate increases, is it likely that a financial incentive under a PBR framework would be large enough to motivate the shareholder to require BC Hydro to contain costs that BC Hydro would otherwise have incurred?
- The BC Government has numerous levers, such as setting water rentals and payments in lieu of taxes, for adjusting the amount of revenue it receives from BC Hydro, separate from earnings based on a return on equity (whether under PBR or COSR).

2. Existing "PBR mechanisms" applicable to BC Hydro

What does PEG mean when it refers to "the existing PBR provisions in BC Hydro's regulatory system"?⁴

The PEG Report does refer⁵ to the 2006 CPCN to BCTC that included an "incentive/penalty" mechanism dependent on the final cost of the Vancouver Island Transmission Reinforcement Project.⁶ Are there other PBR mechanisms that are or have been applicable to BC Hydro? Does PEG consider decoupling of Demand-Side Management spending to be a PBR mechanism?

⁴ "Refinements to the existing PBR provisions in BC Hydro's regulatory system merit consideration": Exhibit A2-5, p.112, underline added. "The regulatory system of BC Hydro has included several PBR mechanisms over the years": Exhibit A2-5, p.108, underline added.

⁵ Exhibit A2-5, p.110, footnote 136.

⁶ Decision and Order C-4-06,

<https://www.ordersdecisions.bcuc.com/bcuc/orders/en/115985/1/document.do>.

Is PEG suggesting that the incentive/penalty mechanism in the VITR CPCN was successful in containing costs, or just that the mechanism was approved?

3. PEG's response to BC Hydro's evidence not recommending PBR at this time

PEG's discussion of research regarding PBR and publically-owned utilities appears to indicate few if any positive results.⁷ However, PEG appears to give short shrift to BC Hydro's expert evidence and Chapter 11 of the Application (not recommending PBR at this time).⁸

Is it PEG's view that all of the PBR possibilities canvassed in the BC Hydro evidence are indeed unsuitable but that there are additional PBR possibilities, not considered in the BC Hydro evidence, that might be suitable?

What is PEG's comprehensive response to BC Hydro's evidence?

4. Types of PBR mechanisms PEG says are suitable for BC Hydro

What exactly are the types of PBR that PEG is saying would be feasible and suitable for BC Hydro?

PEG says reliance on an indexed ARM⁹ to escalate allowed revenue is complicated by BC Hydro's system occasionally requiring capex surges to replace aging facilities which will not automatically produce much revenue growth.¹⁰ Consequently, PEG says the revenue adjustment mechanism would not have to be indexed.¹¹ How would a non-indexed revenue adjustment mechanism avoid the complications with an indexed ARM for BC Hydro?

5. Marketing flexibility under MRP compared to COSR

The PEG Report uses the term Multi-Year Rate Plan (MRP) to mean a type of PBR.¹² The PEG Report says that MRPs can facilitate marketing flexibility to help BC Hydro retain and attract large-load customers. It states:

“As a vertically integrated utility serving many large-load customers, the marketing flexibility that MRPs can facilitate can help BC Hydro retain and attract large-load customers. AMI has already been installed and can facilitate

⁷ Exhibit A2-5, pp.65-69.

⁸ Exhibit A2-5, p.109, third paragraph, beginning “In the PBR Report that the Company filed...” And, Exhibit A2-5, p.“...[W]e have shown that PBR options available for regulating the Company extend far beyond the MRPs with indexed ARMs which are discussed in the Company's recent PBR Report and whitepaper.”

⁹ (Revenue) Attrition Relief Mechanism.

¹⁰ Exhibit A2-5, p.111.

¹¹ Exhibit A2-5, p.111.

¹² “Multi-Year Rate Plan (MRP): A common approach to PBR that typically features a multiyear rate case moratorium, an attrition relief mechanism, and several PIMs.”: Exhibit A2-5, p.116.

better rate designs. However, increased marketing flexibility might require an MRP that doesn't have earnings sharing."¹³

What is PEG's explanation of how a Multi-Year Rate Plan PBR framework facilitates marketing flexibility in a vertically integrated utility? How does this compare to a vertically integrated utility's marketing flexibility under a COSR framework?

Why does PEG use the term MRP here, rather than PBR?

When PEG refers to BC Hydro's "AMI" (advanced metering infrastructure) is PEG referring to the metering in place for large-load customers, or the Smart Meters installed for residential and small general service customers?

Why might increased marketing flexibility require an MRP that doesn't have earnings sharing?

Conclusion

BCSEA appreciates this opportunity to raise topics and questions for the upcoming workshop on the PEG Report.

Yours truly,

William J. Andrews



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cc. BC Hydro by email: bhydroregulatorygroup@bhydro.com

¹³ Exhibit A2-5, p.111, underlined added.