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Commentary by Tom Hackney

BC government dictates electricity rates

In a May 22 move, supposed to 'keep electricity rates affordable' for BC families, government dictated electricity rates for the next couple of years to the BC Utilities Commission (BCUC). Cabinet-issued Direction Nº3 has a detailed set of instructions on the decisions BCUC must make in the review of BCHydro's *Revenue Requirements Application*.

In March 2011, BCHydro filed its first fiscal years 2012–2014 *Revenue Requirements Application* for BCUC approval. It was seeking permission to increase electricity rates by 9.73% per year for each of those three years, for a total rate increase of 32%.

The main drivers for the increase were increased capital expenditures to refurbish BCHydro's aging infrastructure plus the new power supply contracts coming into effect at rates much higher than the current cost of BCHydro's 'heritage assets' power (mainly from dams built in the 1960s and 1970s, the costs of which are now amortized).

The BC government responded by feigning surprise and ordering a government staff review of BCHydro, claiming that the rate increase was 'too high.' (By law, BCHydro's rates are set according to its cost of providing electricity service, plus a prescribed 'return on deemed equity'—a proxy for a profit margin—which is returned to its shareholder, the BC government. This rate of return had been set at 12.75%.)

In light of the government's review, BCHydro asked BCUC to adjourn its Review Requirements proceeding.

The government review duly found many instances of alleged over-spending by BCHydro and, last November, BCHydro duly filed a revised *Revenue Requirements Application* with the BCUC, with the proposed rate increases essentially halved, to 8.0%, 3.91% and 3.91%.

BC Sustainable Energy Association believes the reduced rate increases in the revised application do not reflect the actual costs which BCHydro faces, and that the actual rate increase should be close to that for which BCHydro initially applied.

Government's pressure to keep the rate increase low has caused several significant distortions:

1) Real Costs In Deferral Accounts

Current costs like the purchase of energy are being put into 'deferral accounts' where they accumulate as debt that ratepayers (or someone) must pay in the future. There is some justification for cost deferrals when the cost of a capital asset is spread over the years when its benefits will be felt. And there is some justification to smooth out, by deferral, the fluctuating costs and benefits of BCHydro generation in high and low water years. But this must be carefully controlled to avoid the inappropriate deferral of present costs to future ratepayers—known as 'intergenerational inequity.'

BCHydro's deferral of some energy purchases and some smart meter capital costs appear not to be justified.

Meanwhile, given BCHydro's aging infrastructure and current growth in demand, we can expect many expensive capital projects to come forward in the near future. BCHydro forecasts that the total of its deferrals will balloon to $6 billion in the next few years, making the pressure on rates even higher that it is now.

2) Overly Optimistic Estimates

In its second application, BCHydro has been persuaded to make overly optimistic estimates of trade revenue profits, exposing it to increased risk of a larger than expected shortfall of revenue, increasing debt and intergenerational inequity. (Direction Nº 3 mitigates this, setting the expected trade profits lower than in BCHydro's revised application; however, in the current market situation of over-supply, it may still over-estimate revenues.)

3) Scaling Back Conservation

BCHydro has been persuaded to scale back and cut costs on plans to invest in energy conservation measures that could be expected to put off the need for new generation resources and thus reduce costs to BCHydro and ratepayers.

Imposing Government's Might On BCUC

In its November revised *Revenue Requirements Application*, BCHydro made clear its intention to insist on the proposed reduction in rate increases. Normally, the BCUC looks to *cut back* rate increases in order to counter budget-padding and over-spending and protect ratepayers.

The review process is not structured to force a utility to spend more money because the utility is supposed to be given the freedom to manage its own business.

However, BCUC took the unusual move of making an interim ruling to *raise* BCHydro's rate rider from 2.5% to 5%. (The rate rider is an amount charged on a customer's overall electricity bill which is applied to paying down deferral accounts.) This action signals the BCUC'S skepticism that BCHydro's rates will cover its actual costs and indicates the commission's willingness to oppose the government-negotiated reduction on BCHydro's rate increase.

Government Running The Show

Directive Nº3 to BCUC will have the following effects:

- Government has dictated that BCHydro's total rate increase will be approximately 17%, the same total as in BCHydro's revised application, about half what BCHydro had originally applied for in order to cover its costs.
- Government has allowed BCUC's rate rider increase to stand, speeding the rate at which deferral accounts will (hopefully) be cleared, but at the expense of other cuts that BCHydro must make to keep the overall rate increase at 17%.
- Government has consented to relieve some of BCHydro's costs, reducing its return on deemed equity from 12.75% in F2013 and F2014 to 11.73% and 11.84%, respectively. BCHydro calculates that the reduction to the government's dividend will be $75 million.
- Government has dictated some cost cuts and told BCHydro to write off some items at shareholder expense (for example, the 'Procurement Enhancement Initiative,' at some $34 million). The total of cost cuts is buried in the details of Direction Nº3. While reducing BCHydro's costs, these measures will also reduce various useful services that BCHydro was providing.
- Government has effectively killed BCUC's review of BCHydro's application. On May 23, BCHydro wrote to the Commission recommending that the proceeding be ended. There is little left to do but issue the government-dictated decision. There will not be a public examination of BCHydro's costs or an opportunity to test BCHydro's numbers at a hearing.

What Does This Mean For The Future?

In the short term, some may rejoice that electricity rates will be held down until after the provincial general election. But it won't last because the upward cost pressures are too great.

The more government tries to mask the true costs, the more painful it will be when they must finally be paid: costs and debt will continue to increase, increasing pressure on credit ratings and BCHydro's low interest rates.

The long-term picture includes much higher rates, especially with the big increases in industrial load that are forecast: new liquid natural gas processing plants, gas production in the northeast and mines in the northwest are forecast to claim a large part of BC's cheap 'heritage' power, driving up costs for all ratepayers.

In the short term, BCHydro is deprived of scrutiny by interested parties that, while doubtless uncomfortable, is essential to keep costs in check and ensure that BCHydro's plans reflect the needs and priorities of its customers.

Meanwhile, the role of the BCUC to review BCHydro's operations and costs is seriously harmed, and with it, the public transparency and accountability that goes with an open and participatory process. The public interest will be seriously harmed if the Commission is not soon allowed to resume its role of overseeing BCHydro and other utilities.

Tom Hackney is Director of Policy for BC Sustainable Energy Association. ✐