Reprint
Island Tides

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Reprint from Volume 21 Number 25 Dec 17, 2009

Goodbye to dividends from BC Hydro

The people of BC will not get their usual $300 million dividend from BC Hydro this year. Or maybe any future year.

Hydro's 2009 Annual Report, released in midsummer, revealed that its debt to equity ratio had risen to the point that it could no longer pay a dividend to its owners, the Government of BC. Hydro's second quarter report, released at the end of November, illustrated many of the factors that contribute to Hydro's ups and downs. And a number of critics point to the long-term financial commitments Hydro is making to independent power producers (IPPs) for future 'green' power. Much of this power will be sold in the US, at prices yet to be determined.

BC Hydro, in negotiating contracts for up to forty years into the future to purchase power from run-of-river, wind, and biomass projects, is taking the market risk for these private companies. This enables the companies to finance the capital costs of their projects using, in effect, Hydro's excellent credit rating and asset base. The companies are then left with the climate change and engineering risks inherent in the location and design of their project—risks that are easier to quantify and have demonstrable limits.

The result is to change Hydro from a corporation that has produced predictable financial results and low consumer rates for BC residents and industries over many years, to a marketing and financing structure for private investment in 'green' power projects to be built in BC.

From an industrial development point of view, this may be a viable strategy, but while the risk is taken by Hydro and its BC owners, the profits from these projects are guaranteed to corporations largely based outside the province, and the power goes to support economic growth outside the province.

Considering the magnitude of the investments involved, few continuing jobs are created beyond the construction phase. This reinforces the province as a hewer of wood and a drawer of water (literally) and does nothing for the knowledge sector jobs which might ensure BC's future as a place for skilled people.

Dividends

First, the dividend provisions: BC Hydro is required to make a dividend payment to the Province provided that its debt/equity ratio does not exceed 80/20. In the 2009 Annual Report, page 63, this is explained: 'Under a Special Directive from the Province, BC Hydro is required to make an annual Payment (the Payment) on or before June 30 of each year. The Payment is equal to 85 per cent of BC Hydro's distributable surplus for the most recently completed fiscal year assuming that the debt to equity ratio, as defined by the Province, after deducting the payment, is not greater than 80:20. If the Payment would result in a debt to equity ratio exceeding 80:20, the Payment will be based on the greatest amount that can be paid without causing the debt to equity ratio to exceed 80:20. Due to the 80:20 cap, no payment is payable for fiscal 2009.'

According to the Annual Report, the debt/equity ratio in fiscal 2009 was 81:19, up from 70:30 in 2008. Therefore no 'dividend' is payable to the Province.

'Net Income' for 2007 was $407 million; for 2008, $369 million, and for 2009, $358 million. A $288 million dividend was paid in 2008. BC's Provincial budget appeared to anticipate a $300 million dividend for $2009. It won't be paid; just another reason for the massive errors in the Provincial budget this year.

Debt:Equity Ratio Factors

These factors include everything that affects profits, and everything that affects capital spending. According to BC Hydro's second quarter results, domestic revenues from power sales were $683 million, $60 million higher than the previous year; they credit 'higher average customer rates' , but say these were 'partially offset by decreased revenue from the industrial sector'.

'Energy trading results were significantly lower than in the previous year due to falling prices, lower price spreads between the Northwest and California and between BC and Alberta and weakening of the US Dollar.' This is an excellent description of the risks BC Hydro is taking on behalf of the IPPs.

It was a low water year; there was a 17% decrease in hydro generation because of low winter snowpacks and low spring and summer precipitation. BC Hydro had to buy energy, but prices were lower, and industrial demand was lower, as previously explained.

But capital expenditures were $55 million higher than the previous year. The money was spent on the replacement and expansion of generation facilities and expansion of the distribution system.

Island Tides, Box 55, Pender Island, BC, Canada. Phone: 250-629-3660. Fax: 250-629-3838.
Email: islandtides@islandtides.com. Website: http://www.islandtides.com

The Future

It seems clear that BC Hydro will have to increase its profits if the debt:equity ratio is to once more permit dividends to be paid. This will require some combination of increased revenues from BC customers (which probably means increased rates), increased hydropower generation, more sales to the US at higher prices, and lower investment. On the other hand, the increasing cost of 'take-or-pay' contract commitments with 'green' IPPs will make it more difficult to make profits and build equity.

This is the cost of a strategy that uses the historically sound financial position of BC Hydro to cover the market risks for IPPs. If there are to be dividends, the price of power to BC's consumers, domestic and industrial, must go up. ✐

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