



ROBERT J. PELLATT
COMMISSION SECRETARY

SIXTH FLOOR, 900 HOWE STREET, BOX 250
VANCOUVER, B.C. CANADA V6Z 2N3
TELEPHONE: (604) 660-4700
BC TOLL FREE: 1-800-663-1385
FACSIMILE: (604) 660-1102

VIA FACSIMILE

June 29, 1995

Mr. M.J. Filippelli
Manager, Raw Materials & Energy
Sterling Pulp Chemicals Ltd.
2 Gibbs Road
Toronto, Ontario
M9R 1R1

Dear Mr. Filippelli:

Re: Sterling Pulp Chemicals Ltd.
Requested Permission to Extend Power Exchange Operation ("PEO") Service

The Commission has considered your June 7, 1995 request for extension of service from the PEO beyond July 31, 1995 under the pricing arrangements that existed prior to the filing of new PEO access rates by British Columbia Hydro and Power Authority ("B.C. Hydro"). The Commission has reviewed each of the options available to it with respect to PEO access and finds that a level of unfairness exists to some parties under any option. This unfortunate circumstance exists due to the method of formation of the PEO and the determinations which have occurred since its inception in September, 1993. To help you understand our finding with respect to your application one must review the history of the PEO.

The PEO was established under special circumstance whereby the Lieutenant Governor in Council designated the PEO as a regulated project under Section 16 of the Utilities Commission Act ("the Act"). The disposition order pursuant to the Act expressly removed the PEO from Commission regulation during a three year trial period. The operations of the PEO are controlled by the Minister of Energy, Mines and Petroleum Resources on the advice of an oversight committee reporting to the Minister. The Commission has some control over customer migration to the PEO through its approval of amendments to the Electricity Supply Agreements of customers. In February, 1994 the Commission approved an arrangement whereby Sterling was allowed to terminate its Schedule 1821 Electricity Supply Agreement with B.C. Hydro and receive service under Schedule 1211 via an interim ESA. This permitted Sterling to purchase the bulk of its electricity requirements from the PEO until July 31, 1995. You will recall that Sterling had been previously on a trial curtailable load rate which had not worked to the mutual benefit of Sterling and B.C. Hydro. The Commission approved Sterling's participation on the trial curtailable rate option and the PEO in an effort to assist the financial problems then being faced by Sterling.

During 1994 the Commission received various complaints from Quesnel River Pulp, Canadian Occidental and Gibraltar Mines complaining that B.C. Hydro was blocking access by the companies to the B.C. Hydro subsidiary, the PEO. Section 65 of the Act requires that the Commission not allow any utility to charge undue discriminatory or preferential rates or agreements for similar customers. In May,

1994 the Commission acknowledged that access to the PEO required further investigation before the Commission could determine if the B.C. Hydro conditions for amendment to the Electricity Supply Agreements were appropriate.

B.C. Hydro's response to Commission requests was provided at the end of May, 1994. B.C. Hydro identified possible adverse impacts on revenue requirements and impacts on other customers as reasons for blocking access to the PEO. B.C. Hydro also advised that it was developing new tariffs for access to the PEO for customers on Rate Schedules 1821 and 1211. B.C. Hydro advised that it would be prepared to grant interim access to the PEO to any customers, provided that electricity taken from the PEO was in excess of the maximum demand level under any customer's current ESA.

Following a meeting in July, B.C. Hydro identified that it would have to make application to the Ministry of Energy to revise the transfer pricing under the government's disposition order. B.C. Hydro also identified that it would provide a package of tariff proposals, the Industrial Service Options ("ISO"), in the fall. The tariff filing was made in October, 1994 and customers wrote to the Commission expressing concerns with PEO access under the B.C. Hydro proposals. In November, B.C. Hydro made proposals to the oversight committee to revise the enabling agreement between the PEO and prospective customers. That proposal was not implemented.

In December, 1994 the Commission issued Order No. G-96-94. That Order identified that the B.C. Hydro application for PEO access would be considered by the Commission in conjunction with B.C. Hydro's application for other industrial services. The Order denied interim approval for other industrial customers to access the PEO until a public review was held on the application. The Commission confirmed its February, 1994 approval to allow Sterling access to the PEO on an interim basis until such time as the interim contract with B.C. Hydro expires on July 31, 1995.

Most recently the PEO has been the subject of considerable discussion under the Electricity Market Structure Review. In testimony at the hearing, the President of B.C. Hydro stated: "First of all the PEO has not been very successful. There has been one domestic customer of the PEO, and to the best of our calculations that has probably cost three million dollars as opposed to non-PEO in the past year." (T. 2272)

Later in testimony Mr. Sheehan acknowledged that: "There are problems with it (PEO) the way it's currently operating, significant difficulties. We have not thought through how it might best be operated or what the needs are today versus the needs as they were seen back in (1991) when it was first proposed." (T. 2305)

The foregoing chronology of events related to the PEO demonstrates the many problems that have beset the PEO since it was created as an unregulated subsidiary of B.C. Hydro in 1993. The PEO has created prejudice between customers and has failed to attain its stated objectives. At this juncture the need to restructure the PEO is widely acknowledged but the agreement and power to restructure the PEO does not rest with the Commission. The PEO was established under special designation by the government at the insistence of B.C. Hydro. As such, the PEO is not entirely controlled either by its parent, B.C. Hydro or the B.C. Utilities Commission. Changes to the operations of the PEO must be approved by the Minister of Energy. The Commission expects that it will be providing recommendations to the Minister this summer with respect to the PEO as part of its report on the Electricity Market Structure Review as required by the Terms of Reference.

In conclusion, the Commission has had to weigh the cost and fairness with respect to extending the interim agreement between the PEO and Sterling beyond its termination date of July 31, 1995, with the potential unfairness to other customers who have complained that the conditions offered to Sterling are discriminatory unless they are also offered to all customers. At this juncture the Commission is not prepared to extend the PEO service to Sterling under the earlier arrangements which B.C. Hydro has

argued are subsidized by other utility customers. We come to this conclusion reluctantly and we hope that an alternative to the PEO, can be put in place quickly so that the benefits to British Columbia industries, which were hoped to be possible under the PEO, can be realized.

Accordingly, the Commission will be advising B.C. Hydro to terminate your current Rate Schedule 1211 ESA as of July 31, 1995, and allow your return to Schedule 1821, effective August 1, 1995.

Yours truly,



Robert J. Pellatt

WJG/cms

cc: **The Honourable Anne Edwards, Minister**
 Ministry of Energy, Mines and Petroleum Resources
Mr. David A. Harrison
 Senior Vice President and Chief Financial Officer
 British Columbia Hydro and Power Authority
Mr. R.B. Wallace
 Bull, Housser & Tupper
Mr. Brian N. Black
 Manager, Maintenance & Engineering
 Quesnel River Pulp Company
 P.O. Box 9500, Quesnel, B.C. V2J 5C3
CXY Canada Limited Partnership
 #1500, 635 - 8th Avenue S.W.
 Calgary, Alberta, T2P 3Z1
Mr. Barry Weenk, P.Eng.
 Project Manager
 Gibraltar Mines Ltd.
 P.O. Box 130, McLeese Lake, B.C. V0L 1P0