



IN THE MATTER OF  
the Utilities Commission Act, R.S.B.C. 1996, Chapter 473

and

An Application by Kanelk Transmission Company Limited  
for Approval to Dispose of Utility Assets

**BEFORE:** P. Ostergaard, Chair )  
L.R. Barr, Deputy Chair )  
P.G. Bradley, Commissioner ) December 2, 1999  
K.L. Hall, Commissioner )  
B.L. Clemenhagen, Commissioner )

**O R D E R**

**WHEREAS:**

- A. On June 8, 1999, Kanelk Transmission Company Limited ("Kanelk") applied to the Commission, pursuant to Sections 52 and 41 of the Utilities Commission Act ("the Act"), to dispose of its utility assets in British Columbia and assign the associated Certificate of Public Convenience and Necessity ("CPCN") to British Columbia Hydro and Power Authority ("B.C. Hydro"); and
- B. Kanelk's British Columbia facilities were built in 1951. The 138 kV transmission system runs from TransAlta Utilities Corporation's facilities at Pocaterra, Alberta to B.C. Hydro's Natal Substation, then continues east to terminate at Coleman, Alberta. The system is used at present by B.C. Hydro to serve its customers in the Elk Valley; and
- C. Kanelk and B.C. Hydro signed an Asset Purchase Agreement ("the Agreement"), dated December 15, 1998, for the sale of the utility assets for \$4,322,967 subject to Commission approval; and
- D. The closing date of April 30, 1999 in the Agreement was subsequently amended by three letter agreements, with the closing date in the October 27, 1999 letter agreement specified as December 10, 1999; and
- E. The District of Elkford, the District of Sparwood, the Regional District of East Kootenay, the Independent Power Association of British Columbia, and Fording Coal Ltd. expressed their interest and concerns about the sale of Kanelk's utility assets; and

- F. After a Pre hearing Conference, established by Order No. G-71-99 and held in Elkford on July 22, 1999, and after a series of Information Requests and Responses, the Commission informed the parties that they would be given until September 15, 1999 to resolve outstanding issues. In the event that substantive opposition continued to exist, the Commission advised that it may initiate a formal public hearing process to occur in Elkford; and
- G. The Commission, in Letter No. L-54-99 dated October 15, 1999, concluded that an oral hearing would not be required, directed Kanelk to respond to a Fording Coal Ltd. proposal by October 29, 1999, solicited further written submissions from intervenors by November 12, 1999, and a reply by Kanelk, if any, by November 19, 1999.

**NOW THEREFORE** for the Reasons given in Appendix A to this Order, the Commission approves Kanelk's application to dispose of its utility assets in British Columbia and assign the associated Certificate of Public Convenience and Necessity to B.C. Hydro, based on the determinations in the attached Decision.

**DATED** at the City of Vancouver, in the Province of British Columbia, this 2<sup>nd</sup> day of December 1999.

BY ORDER

*Original signed by:*

Peter Ostergaard  
Chair

Attachment



## **REASONS FOR DECISION**

### **KANELK TRANSMISSION COMPANY LIMITED Application for Approval to Dispose of Utility Assets**

#### **THE APPLICATION**

On June 8, 1999, Kanelk Transmission Company Limited ("Kanelk") applied to the Commission to dispose of its utility assets, consisting of a 120 km, 138 kV transmission line located in the Elk Valley, to British Columbia Hydro and Power Authority ("B.C. Hydro") for a purchase price of \$4,322,967. The transmission line serves B.C. Hydro's customers located in the Elk Valley, the District of Elkford, and coal mines at Fording River, Greenhills and Line Creek, pursuant to a Certificate of Public Convenience and Necessity ("CPCN") issued by the British Columbia Public Utilities Commission on October 24, 1949.

The Application states that the quality of service to customers in the Elk Valley will not be affected by the sale of the assets to B.C. Hydro since the transmission line will continue to be interconnected to transmission facilities on the Alberta side of the B.C.-Alberta border. As well, the system support services purchased by Kanelk under Rider A, Special Facilities Credit, to Rate Schedule GIS, and provided to B.C. Hydro by Kanelk under Section 2.2 of the Wholesale Transmission Service and System Support Services Agreement, would continue to be available to B.C. Hydro. The relevant sections of Rider A, Special Facilities Credit, to Rate Schedule GIS have been revised and are directly available to B.C. Hydro.

#### **THE PURCHASE**

The net book value of the line on December 31, 1998 (based on material supplied by Kanelk as part of the negotiated settlement process that resulted in Order No. G-6-98, which approved the Wholesale Transmission and System Support Service Agreement) is \$3.6148 million. B.C. Hydro proposes to capitalize the Kanelk Line at the full purchase price of \$4.322 million.

B.C. Hydro stated that it is aware it is common practice to include a purchased existing utility plant into the rate base at the net book value of the asset. This practice is followed to prevent shareholders from passing on the risk, associated with the purchase of a utility plant at appreciated capital values, to ratepayers through increased revenue requirements. In this case, B.C. Hydro suggests that capitalizing the Kanelk Line at the full

purchase price is appropriate since ratepayers will benefit through reduced future revenue requirements as a result of B.C. Hydro owning the Kanelk Line. In response to a Commission staff Information Request for precedents on this matter, B.C. Hydro cited a 1984 Decision, where the Commission allowed West Kootenay Power and Light Company, Limited to include the premium of \$11.9 million over book value paid to Cominco Ltd. for generation assets, as a utility asset when determining its revenue requirements. However, that Decision only dealt with the fact that the premium had not been recorded in the correct account within the Uniform System of Accounts. The inclusion of the acquisition premium in rate base was the result of a 1982 Ministerial Order, which exempted Cominco Ltd. from regulation, and approved the sale of Cominco Plants No. 2, 3 and 4 for \$20 million, with the purchase price to be allocated in the books of account between real property, dams and equipment, and buildings.

## **THE REGULATORY PROCESS**

At a Pre-hearing Conference in Elkford on July 22, 1999, intervenors raised a number of issues about the proposed sale. After a series of Information Requests and Responses, the Commission informed the parties that they would be given until September 15, 1999 to resolve outstanding issues. In the event that substantive opposition continued to exist, the Commission advised that it may initiate a formal public hearing process to occur in Elkford.

Subsequently, the Commission concluded that an oral hearing was not required and Letter No. L-54-99 directed Kanelk to respond to a Fording Coal Ltd. ("Fording") proposal by October 29, 1999, with further written submissions from intervenors by November 12, 1999, and with reply by Kanelk, if any, by November 19, 1999.

## **THE ISSUES**

Local governments affected by the proposed sale initially opposed the sale of the transmission line to B.C. Hydro, on the basis that ownership by the Crown corporation resulted in a loss of property tax revenue to them. In mid September 1999, the Regional District of East Kootenay and the District of Sparwood advised the Commission that the Finance, Administration and Engineering Committee of the Regional Board had accepted a mitigation offer from B.C. Hydro, and that these two local governments now supported B.C. Hydro's ownership of the Kanelk line. Therefore, the two remaining parties with substantive concerns were the Independent Power Association of British Columbia ("IPABC") and Fording.

On September 8, 1999, the IPABC stated that it was not possible to make any final determination of its position until it knew the details of any agreement with respect to lost tax revenues. After receiving a response from B.C. Hydro, the IPABC submitted that the transfer of the CPCN to B.C. Hydro is not in the public interest, as B.C. Hydro's justification for the purchase is "woefully inadequate", and the payments to

the local governments raise the issue of undue discrimination. In its June 22, 1999 letter of support, B.C. Hydro noted that the purchase of the Kanelk transmission line would reduce B.C. Hydro's expected present value of future revenue requirements by \$1.407 million. The 8% discount rate used by B.C. Hydro in the determination of the net present value of the asset purchase represents B.C. Hydro's Weighted Average Cost of Capital. The Commission agrees that, on balance, the purchase will have the benefit of reducing B.C. Hydro's future revenue requirements and that the analysis is reasonable.

Fording's concern about the proposed sale focussed on its ability to retain future transmission access at rates that only consider the Kanelk line cost of service. Fording's interest arises from its proposal for a coal-fired thermal generation plant at its Fording River mine.

The issue was first raised in the 1995 public hearing into Kanelk's rates. In its October 17, 1995 Decision the Commission noted:

“At the request of Commission counsel, Kanelk reviewed the utility's CPCN, as amended, and determined that it fully describes the existing services provided by Kanelk and that further modifications were not needed at this time (T. 299). Fording Coal requested that the CPCN dated October 18th, 1967 be varied to remove the requirement for the consent of East Kootenay and B.C. Hydro, or either of them, to wheel power over the Kanelk system, thereby allowing this jurisdiction to revert to the Commission (T. 544). B.C. Hydro argued that this is, in fact, a radical step towards retail wheeling and suggested that the Commission's recent report, The Electricity Market Structure Review, recommended that the government reject retail wheeling at this time (T. 537).

Fording Coal responded that the request was actually focused on the potential to give Fording Coal the ability to view TransAlta as a supplier (T. 548).

The Commission agrees that there is merit to Fording Coal's request to modify the CPCN, but it may be premature until government policy with respect to competitive service in British Columbia is determined. If there is a change to transmission access in the rest of the B.C. Hydro service area, the Commission will review the appropriateness of the Kanelk CPCN at that time and will ensure that Fording Coal is not discriminated against.”

In its November 12, 1999 submission, Fording stated:

“Fording does not oppose the sale of the utility assets, in as much as Kanelk/B.C. Hydro have provided evidence for the Commission to consider which purports to set forth the net benefit to B.C. Hydro. However, Fording submits that it is unfair and unjust to itself and other customers, both existing and reasonably foreseeable, to have to bear the cost, financial burdens as well as potential lost economic opportunities which would not have been the circumstance if Kanelk had remained the owner of the assets.”

The sale of utility assets by Kanelk will terminate the Wholesale Transmission Service and System Support Services Agreement, under which Kanelk provided wheeling and system support services to B.C. Hydro, for serving its loads in the Elk Valley. Fording argued that this Agreement gave third parties a right to seek and receive access to transmission facilities at rates using the cost and other principles as currently embodied in

the Kanelk rates. Alternatively, if it did not have this right, it felt it should have. Fording sought to make this access a condition of the asset transfer.

According to Fording, in the current circumstances, an access rate would be calculated on the basis of Kanelk's costs or alternatively a bypass rate would be negotiated with B.C. Hydro calculated in similar circumstances. However, if the Application is approved by the Commission without the inclusion of mitigation measures (inherited rights), Fording believes that the rate for this same service would be determined on the basis of the lower of the rates proposed in B.C. Hydro's letter of July 29, 1999, or a bypass rate calculated pursuant to Commission principles established in previous decisions. On the basis of information supplied by B.C. Hydro and Kanelk, Fording felt that regulatory approval without inherited rights results in an immediate six to seven-fold increase in the rate.

Kanelk's view is that Fording does not have any rights conferred by the Agreement but agrees that, if Fording were to build a generating plant and apply to become a wholesale customer, Kanelk would likely apply for an amendment to its tariffs which would equitably allocate Kanelk's revenue requirement between B.C. Hydro and Fording. Kanelk felt it is speculative as to what, if any, tariff would ultimately be approved by the Commission in such a circumstance.

Fording responded that its initiatives and activities could be more aptly described as "effective strategic planning (visionary) in a dynamic and rapidly evolving electric market. The market structure in the future will, arguably, not be identical to that which exists today."

Kanelk noted in its November 19, 1999 reply that:

- "1. ...there is no reasonable basis to conclude that potential future wholesale users of the Kanelk facilities would be materially harmed, and in fact they could be better off, if the Kanelk assets were transferred to B.C. Hydro;
2. Kanelk does not offer a competitive alternative to B.C. Hydro for retail customers;
3. Approval of Kanelk's application will not have any impact on a retail customer's opportunity to negotiate an economic bypass rate with B.C. Hydro;"

## **COMMISSION DETERMINATIONS**

The Commission concludes that it is in the public interest for the sale of the Kanelk utility assets to B.C. Hydro to proceed. The Commission is not prepared to accept Fording's argument that it should receive transmission access under B.C. Hydro ownership at rates based on the Kanelk line's cost of service. If Fording's proposed generating plant proceeds further towards financing and construction, Fording has the option under Section 70 ("Use of Transmission Facilities") of the Utilities Commission Act to apply for an

order enabling Fording to use B.C. Hydro's transmission facilities at rates, terms, and conditions considered advisable by the Commission at that time.

**The Commission approves Kanelk's application, under Sections 52 and 41 of the Utilities Commission Act, to dispose of its utility assets and to assign the associated Certificate of Public Convenience and Necessity to B.C. Hydro.**

**The Commission does not accept B.C. Hydro's proposal to capitalize the utility assets of Kanelk at the full purchase price of \$4.323 million. The Commission is of the view that it is more appropriate to record the Kanelk utility assets at net book value.** This is the more normal regulatory accounting treatment which protects customers from utility assets previously paid for by customers being increased by a new utility owner. B.C. Hydro has not established sufficient reasons to increase the capitalization of Kanelk.