



LETTER No. L-10-03

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March 25, 2003

Mr. Ron Ross, P.Eng.
Emco Engineering Ltd.
186 Columbia Avenue
Castlegar, B.C. V1N 1A9

Dear Mr. Ross:

Re: Pope & Talbot – Grand Forks, BC
Bypass Rate Application - Emco File No. 0277A

On December 18, 2002, Emco Engineering Ltd. submitted a Bypass Rate Application to the Commission on behalf of Pope & Talbot Ltd. Pope & Talbot is applying for permission to build a 60 kV/4.16 kV substation in Grand Forks and move from Aquila Network's Rate Schedule 30 (Large General Service Primary) to Rate Schedule 31 (Large General Service – Transmission). The Application outlines Pope & Talbot's cost of bypass and the associated cost savings expected over the next 20 years, assuming 3 percent annual load growth.

Aquila's five-year distribution plan does not provide for any material expenditure on the existing substation that serves Pope & Talbot. Future expenditures on the substation are likely to be condition related, rather than load related. Moreover, Aquila anticipates very low growth rates in distribution service in the Grand Forks area. Aquila's incremental cost of serving Pope & Talbot under Rate Schedule 30 is not significant.

Aquila does not oppose Pope & Talbot's Application and would serve them under Rate Schedule 31 if they construct the substation. Aquila is concerned that the quality of Pope & Talbot's power supply will be reduced given that the proposed bypass facility would utilize a 38-year old transformer. In the event that this transformer fails, Aquila notes that it is not obligated to supply backup, but would do so on commercial terms only.

Aquila has provided revised cost estimates to the Pope & Talbot Application based on adjustments to a number of underlying assumptions, such as interconnection costs, protection requirements and the cost of capital. Pope & Talbot considers that it would be worthwhile to have Aquila provide them their detailed cost estimates in order to facilitate discussion of significant differences on an item by item basis. A key

outstanding issue for Aquila is that Pope & Talbot does not include an estimate of the expected cost of backup to explicitly account for the risk of the 38-year old transformer failing.

Pope and Talbot's cost of bypass exceeds Aquila's incremental cost of service. Based on this and considering the issue of backup supply that underlies this application, the Commission recommends that Pope & Talbot and Aquila negotiate a Bypass Rate and submit this rate to the Commission for final approval. Negotiation will allow the parties to resolve differences in their respective cost estimates and offer them an opportunity to agree on the expected cost of backup, given the risk of the transformer failing. In this context a negotiated Bypass Rate can be considered a rider to be added to Rate Schedule 31. The Bypass Rate should equal Pope & Talbot's cost of bypass all told and be payable to Aquila over the expected life of the proposed bypass facility, financed at Pope & Talbot's weighted average cost of capital.

The Commission agrees that this Application is essentially a quality of supply issue. Pope & Talbot is seeking to reduce costs by obtaining lower quality service. Aquila does not oppose their application and would serve them under Rate Schedule 31 if the proposed facility was built. The Commission expects that if the proposed bypass facility was built it would not impose costs on Aquila's other customers, provided it does not fail over its expected life. Therefore, the Commission recommends that if the parties cannot agree to a negotiated bypass rate, Pope & Talbot be allowed to construct and operate the proposed bypass facility under the condition that if backup is required, Pope & Talbot be required to pay all of the costs of backup to Aquila under terms agreed to by the parties in advance.

Yours truly,

Original signed by:

Robert J. Pellatt

RG/cms

cc: Mr. George Isherwood
Regulatory Affairs Executive
Aquila Networks Canada (British Columbia) Ltd.

Mr. Andrew Horahan
Sawmill Superintendent
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