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**BRITISH COLUMBIA  
UTILITIES COMMISSION**

**ORDER  
NUMBER** G-64-07

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

**and**

**An Application by British Columbia Transmission Corporation  
for Approval of Allowance for Funds Used During Construction Accounting Treatment and  
Proposed Disposition of the F2008 Forecast Revenue Sufficiency and F2008 Financial Information Filing**

**BEFORE:** L.A. O'Hara, Panel Chair  
and Commissioner

June 12, 2007

**O R D E R**

**WHEREAS:**

- A. On November 9, 2006 Commission Order No. G-139-06 approved the British Columbia Transmission Corporation ("BCTC") F2007 Transmission Revenue Requirement Settlement Agreement; and
- B. In a letter dated February 26, 2007 BCTC informed the Commission of its intended regulatory filings for ratemaking, accounting, and informational purposes for the Fiscal 2008 period; and
- C. On March 20, 2007 BCTC submitted a Financial Information Filing for the period April 1, 2007 to March 31, 2008 ("F2008 Financial Filing"). In the F2008 Financial Filing BCTC stated that it would not seek to change existing rates in F2008 for the BCTC and Asset Management and Maintenance Revenue Requirements, subject to the approval of a change in accounting treatment from Interest During Construction ("IDC") to Allowance for Funds Used During Construction ("AFUDC"); and
- D. On March 21, 2007, BCTC applied for approval of a methodology which recognizes an AFUDC Accounting Treatment and the Proposed Disposition of the F2008 Forecast Revenue Sufficiency, effective April 1, 2007 (the "Application"), pursuant to Section 49(a) of the Utilities Commission Act (the "Act") and Section 6 of Special Direction No. 9; and
- E. The Commission, by Order No. G-37-07 established a written public hearing process and a regulatory timetable to review the Application and the F2008 Financial Filing; and
- F. Commission Order No. G-37-07 also established the current customer rates as interim, effective April 1, 2007; and
- G. The Commission issued information requests to BCTC on April 10, 2007 and BCTC responded on April 24, 2007; and

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- H. The BC Old Age Pensioners Organization et al. (“BCOAPO”) issued information requests to BCTC on April 26, 2007 and BCTC responded on May 10, 2007; and
- I. On May 17, 2007 BCTC filed its Final Argument. BCTC submits that the AFUDC accounting treatment is consistent with Special Direction No. 9 and that crediting the F2008 Forecast Revenue Sufficiency to the Revenue Deferral Account is fair and administratively cost effective; and
- J. On May 22, 2007 BCOAPO filed its Argument. BCOAPO concurred with the submission filed by BCTC and agreed that the orders sought in the Application should be granted; and
- K. On May 23, 2007, the British Columbia Hydro and Power Authority (“BC Hydro”) filed its Argument. BC Hydro was satisfied with the submission of BCTC and agreed that the orders sought in the Application should be granted; and
- L. On May 30, 2007, BCTC submitted its Reply Argument; and
- M. The Commission has reviewed the Application, the evidence adduced in relation thereto and Written Argument and finds that approval is warranted all as set forth in the Reasons attached as Appendix A to this Order.

**NOW THEREFORE** pursuant to Section 49(a) of the Utilities Commission Act and Sections 3 and 6 of Special Direction No. 9, the Commission orders as follows:

1. The Commission approves the methodology for BCTC that recognizes AFUDC accounting treatment and thereby authorizes a change from the current method which recognizes only IDC, effective April 1, 2007.
2. The Commission accepts the F2008 Financial Filing which did not contain F2008 forecast capital additions and therefore, a level of F2008 forecast capital additions has not been approved.
3. The current interim customer rates are confirmed as permanent effective April 1, 2007.
4. The Commission approves the proposed disposition of the forecast \$0.4 million F2008 Forecast Revenue Sufficiency to the Revenue Deferral Account.

**DATED** at the City of Vancouver, in the Province of British Columbia, this 12<sup>th</sup> day of June 2007.

BY ORDER

*Original signed by:*

L.A. O’Hara  
Panel Chair and Commissioner

Attachment

**BRITISH COLUMBIA TRANSMISSION CORPORATION**

**APPLICATION FOR ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION ACCOUNTING  
TREATMENT AND PROPOSED DISPOSITION OF THE F2008 FORECAST REVENUE  
SUFFICIENCY AND F2008 FINANCIAL INFORMATION FILING**

**REASONS FOR DECISION**

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**1.0 INTRODUCTION**

**1.1 The Application**

On March 21, 2007, the British Columbia Transmission Corporation (“BCTC”, the “Company”) applied for British Columbia Utilities Commission (“BCUC”, “Commission”) approval of a methodology which recognizes an Allowance for Funds Used During Construction (“AFUDC”) accounting treatment and the Proposed Disposition of the F2008 Forecast Revenue Sufficiency (“F2008 Sufficiency”), effective April 1, 2007 (the “Application”), pursuant to Section 49(a) of the Utilities Commission Act (the “Act”) and Section 6 of Special Direction No. 9 (“SD9”).

As a result of the proposed change from an Interest During Construction (“IDC”) to an AFUDC methodology, BCTC forecasts that the F2008 revenue deficiency of \$2.9 million will change to a revenue sufficiency of \$0.4 million in F2008. The Company proposes to credit the \$0.4 million F2008 Sufficiency to the Revenue Deferral Account (“RDA”) in F2008. BCTC submits that it does not intend to seek a change to existing rates for F2008 if the Application is accepted. If the Application is denied, the Company believes that it will be necessary to apply for a F2008 rate increase. The Application also states that BCTC does not intend to take any further steps regarding F2008 rates until the Commission has made its decision on the Application.

**1.2 Background**

On February 26, 2007, BCTC submitted a letter informing the Commission of its intended regulatory filings for ratemaking, accounting, and informational purposes for the F2008 period. In the letter, BCTC stated that beyond complying with Commission Orders No. G-143-06 and No. G-17-07, regarding the British Columbia Hydro and Power Authority (“BC Hydro”) Owner’s Revenue Requirement, BCTC did not, at this time, intend to seek a change to existing rates for F2008. BCTC also submitted that maintaining rates at existing levels would require a change in BCTC’s current method of accounting from one which recognizes only IDC to one that recognizes AFUDC.

On March 20, 2007 BCTC submitted a Financial Information Filing for the period April 1, 2007 to March 31, 2008 (“F2008 Financial Filing”). The F2008 Financial Filing forecasts a F2008 Revenue Requirement of \$70.5 million which represents a \$2.9 million increase from the F2007 Approved Revenue Requirement of \$67.6 million. The \$2.9 million increase results in a revenue deficiency which would ordinarily require a rate increase. The change to an AFUDC accounting treatment results in a forecast revenue sufficiency which eliminates the need to increase existing rates in F2008.

## **2.0 THE WRITTEN HEARING PROCESS**

In determining the appropriate process to review the Application and the F2008 Financial Filing, the Commission Panel considered the complexity of the Application, the need for public participation and the cost associated with the process selected. The Application is not complex and only two Intervenors and one Interested Party registered to participate in the proceeding. Given the cost of an oral hearing and the small number of Intervenors, the Commission Panel determined that a written process should be used to examine the Application. On March 28, 2007, Commission Order No. G-37-07 established a written public hearing for review of the Application and the F2008 Financial Filing.

## **3.0 CHANGE IN ACCOUNTING TREATMENT**

### **3.1 IDC Accounting Treatment**

Since its inception, BCTC has utilized an IDC accounting treatment. Under the IDC methodology, the capitalization of IDC related to Construction Work in Progress (“CWIP”) begins on the capital project start date and ceases when the capital project is placed in service. The IDC on capital projects is calculated on monthly capital expenditures, inclusive of capital overhead, on a compounding basis. IDC is subtracted from the deemed cost of debt and is not included in the current period’s revenue requirement. The amount of IDC is the lesser of the actual cost of long and short term debt, excluding capital leases and the IDC computed using the CWIP balances. Since the IDC methodology only capitalizes the interest related to CWIP, the Return on Equity (“ROE”) associated with CWIP balances is recovered in current period rates.

### **3.2 AFUDC Accounting Treatment**

The proposed AFUDC methodology recognizes that both debt and equity are used to fund CWIP. Under the AFUDC accounting treatment, the capitalization of the interest expense and the ROE related to CWIP begins on the capital project start date and ceases when the capital project is placed in service. Both the interest expense and the ROE related to CWIP are added to the cost of the asset and not recovered in the current period's rates. The cost of funding CWIP is recovered from future customers through depreciation once the assets are placed in service.

### **3.3 Request to Change Accounting Treatment**

In F2008, BCTC forecasts significant increases in capital expenditures and CWIP due to the System Control Modernization Project ("SCMP"). As a result of the SCMP, the monthly average CWIP balance is forecast to increase from \$72.8 million in April 2007 to \$120.1 million in March 2008. The increase in the CWIP balances results in higher interest expense and ROE related to CWIP. Under the IDC methodology, the interest related to CWIP is capitalized but the ROE related to CWIP is recovered in F2008 rates. BCTC forecasts a revenue deficiency of \$2.9 million in F2008 under the IDC accounting treatment.

Given that assets under construction do not provide service to current customers, BCTC submits that the interest charges and the allowed ROE associated with CWIP should not be charged to current customers. BCTC is also of the opinion that the cost of funding CWIP should be recovered from future customers in those years when the assets provide service; therefore, BCTC proposes to change from an IDC to an AFUDC accounting treatment. BCTC states that in addition to addressing the issues regarding the equity between current and future customers, implementing the AFUDC accounting treatment would also bring BCTC's treatment of financing costs associated with capital projects more in line with investor-owned utilities in British Columbia and generally elsewhere in Canada. BCTC also submits that the change to an AFUDC methodology is appropriate and fair.

### **3.4 Return on Equity**

BCTC's ROE is governed by SD9, Section 3 as follows:

#### **Basis for establishing transmission corporation revenue requirements**

In regulating and fixing rates for the transmission corporation, the commission must ensure that those rates allow the transmission corporation to collect sufficient revenue in each financial year to

- (c) generate for the transmission corporation an annual rate of return on deemed equity that is equal to the annual rate of return that is allowed by the commission on the authority's equity as that term is defined in Special Direction HC2.

In response to BCUC Information Request ("IR") No. 1, Question 7.1, BCTC states that "BCTC believes SD9 requires that the Commission allow BCTC the opportunity to earn and collect revenue to cover its debt service and ROE on BCTC's deemed capitalization on an ongoing basis". BCTC also submits that SD9 was not intended to identify a particular accounting treatment, but rather to ensure that BCTC's total cost of capital can be recovered on an ongoing basis. The AFUDC accounting treatment affects the timing of when the ROE related to CWIP is recovered, but it does not affect the Company's opportunity to recover the return on its deemed equity. Therefore, BCTC believes that the change to an AFUDC methodology is consistent with SD9.

The Commission Panel agrees with the BCTC submission that cost of funding CWIP should be recovered from future customers in those years when the assets provide service. The Commission Panel also agrees that the change to the AFUDC accounting treatment is consistent with SD9; therefore, **the Commission Panel approves the BCTC change in accounting treatment from an IDC to an AFUDC methodology, effective April 1, 2007.**

### **4.0 F2008 FINANCIAL INFORMATION FILING**

#### **4.1 Capitalized Overhead**

Capitalized overhead is forecast to increase from the F2007 approved amount of \$9.2 million to \$10.6 million in F2008. Total overhead increased from \$47.2 million in F2007 to \$52.4 million in F2008 and this resulted in higher capitalized overhead (BCUC IR No. 1, Question 4.1). BCTC also states that the Company followed the method described in BCTC F2007 Revenue Requirement Application, Appendix C and subsequently approved by

the BCUC as part of BCTC's F2007 Negotiated Settlement Agreement (BCUC Order G-139-06, Appendix A, paragraph 8).

## **4.2 Labour**

A primary source of the F2008 Revenue Requirement increase is higher labour costs. In the response to BCUC IR No. 1, Question 2.1, BCTC provided a breakdown of the F2008 labour cost increase and employee additions. From F2007-F2008, BCTC plans to increase gross labour costs by \$2.9 million and add 40 new positions, excluding the 10 positions added due the repatriation of functions from the Accenture Business Services of British Columbia Limited Partnership. Of the 40 new positions, 11 positions are temporary increases which BCTC expects to eliminate through retirement over time and 9 positions related to the replacement of temporary or contract staff.

In F2008, BCTC's total headcount forecast is 400 positions; this represents a substantial increase over the 326 Full Time Equivalent positions in the approved BCTC F2005 Revenue Requirement. Given the growth in BCTC's headcount **the Commission Panel directs BCTC to provide a 5-year labour plan, similar in nature to the 5-year capital plan, in its next revenue requirement application.**

## **4.3 F2008 Forecast Capital Structure**

BCTC's deemed capital structure is determined by SD9 and the F2008 Financial Filing includes BCTC's F2008 forecast capital structure. The F2008 forecast average monthly debt and equity reflects the drawing down of temporary investments and increased borrowings to finance BCTC's F2008 capital additions, primarily the SCMP. The F2008 Financial Filing provided F2006 and F2007 capital additions, but did not include F2008 forecast capital additions. For the purposes of the F2008 Financial Filing, the Commission Panel accepts the forecast capital structure and cost of capital for F2008, but has not approved a level of F2008 capital additions.

## **4.4 Community Investment Program**

The F2008 Revenue Requirement increase also includes \$0.5 million for the establishment of a community investment program for community-focused sponsorships and scholarships. BCTC states that good community relations will assist in the successful execution of needed infrastructure projects at reasonable costs. The Commission Panel notes that BC Hydro's Corporate Communications and Public Affairs ("CC&PA") business

unit manages corporate and regional outreach activities including corporate donations, regional donations and sponsorships and employee contribution programs (BC Hydro F07/F08 Revenue Requirements Application, p. 6-29) and BCTC should ensure that its community investment program does not duplicate work performed by BC Hydro. Regarding the cost of donations, the Commission Panel concurs with the view from the 1992 Pacific Northern Gas Decision that donations are normal business expenses which provide benefits to the customers and shareholders; therefore, the costs should be shared equally between customers and shareholders (Pacific Northern Gas Ltd. 1992 Revenue Requirements Decision, p. 19). **The Commission Panel accepts the \$0.5 million provision for community-focused sponsorships and scholarships for F2008 Revenue Requirement purposes, but in future revenue requirement applications BCTC is to more fully explain why such expenses should be solely recovered from customers.**

#### **4.5 2007 British Columbia Energy Plan and Federal Energy Regulatory Commission Order No. 890**

BCTC's Final Argument, filed on May 17, 2007, states that the F2008 Financial Filing was made without the benefit of either the 2007 British Columbia Energy Plan or Federal Energy Regulatory Commission Order No. 890. Once BCTC gains a better understanding of these initiatives, the Company may seek Commission approval to devote additional resources to these requirements. At this time, BCTC has not determined whether it will be necessary to seek such approval or, if it is necessary, the nature, timing or scope of such approval and does not expect to be in a position to make this determination until the summer.

**The Commission Panel accepts the F2008 Financial Filing, while reiterating the concerns expressed in Sections 4.2 and 4.4 of these Reasons.**

#### **5.0 DISPOSITION OF F2008 FORECAST REVENUE DEFICIENCY**

In the Application, BCTC applied to the Commission pursuant to Section 6 of SD9 for approval to credit the F2008 Sufficiency of \$0.4 million to the RDA in F2008. BCTC is projecting a debit balance (regulatory asset) of \$15.4 million (subject to audit review) in the RDA as of March 31, 2007 (BCOAPO IR No.1, Questions 1.1 and 1.2). Deferral accounts are governed by SD9, Section 6 as follows:



### **Deferral accounts**

When regulating the transmission corporation, the commission

- (a) must allow the transmission corporation to establish the deferral account or accounts contemplated by paragraph 4.13 (f) of the Master Agreement,
- (b) may allow the transmission corporation to establish one or more other deferral accounts for other purposes, and
- (c) must fix or regulate the transmission corporation's rates in such a way as to allow the deferral account or accounts to be cleared from time to time and within a reasonable period of time.

BCTC is of the opinion that its proposal is similar to the BC Hydro proposal to apply a \$33.7 million reduction in BC Hydro's F2008 allowed return to the balance in its Non-Heritage Deferral Account approved by Commission Order No. G-17-07. Given the modest amount of the F2008 Sufficiency, BCTC considers crediting the F2008 Sufficiency to the RDA in F2008 a fair and administratively cost effective proposal for its customers.

In the Application, BCTC also states that it is not seeking approval from the Commission for disposition and recovery of the remaining receivable balance in the RDA (the March 31, 2007 RDA balance less F2008 Sufficiency of \$0.4 million). If required, the Company proposes to file such an application, when the actual balance of the RDA becomes known in June 2007. In response to BCUC IR No. 1, Question 1.2, BCTC states that it intends to make an application to the Commission to clear any balances in the Revenue, Emergency Maintenance, Regulatory and Cost of Market deferral accounts after its F2007 results are finalized.

The Commission Panel accepts BCTC's proposal to file applications regarding the disposition and recovery of the remaining receivable balance in the RDA in June 2007 and the disposition of any balances in the Revenue, Emergency Maintenance, Regulatory and Cost of Market deferral accounts after BCTC's F2007 results are finalized. In addition, the Commission Panel concurs with the BCTC opinion that crediting the \$0.4 million F2008 Sufficiency to the RDA in F2008 is fair and administratively cost effective; therefore **the Commission Panel approves the BCTC request to credit the \$0.4 million F2008 Sufficiency to the RDA in F2008.**