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ORDER NUMBER
G-196-17

IN THE MATTER OF
the *Utilities Commission Act*, RSBC 1996, Chapter 473

and

FortisBC Energy Inc.
Annual Review for 2018 Delivery Rates

BEFORE:
D. J. Enns, Panel Chair/Commissioner
B. A. Magnan, Commissioner
R. D. Revel, Commissioner

on December 21, 2017

ORDER

WHEREAS:

A. On September 15, 2014, the British Columbia Utilities Commission (Commission) issued its decision and Order G-138-14 for FortisBC Energy Inc. (FEI) approving a Multi-Year Performance Based Ratemaking (PBR) Plan for 2014 through 2019 (PBR Decision). In accordance with the PBR Decision, FEI is to conduct an annual review process to set delivery rates for each year;

B. By letter dated July 17, 2017 and revised letter dated July 24, 2017, FEI proposed a regulatory timetable for its annual review for 2018 delivery rates;

C. By Order G-115-17 dated July 27, 2017, the Commission established the regulatory timetable for the annual review for 2018 delivery rates which included the anticipated date for FEI to file its annual review materials, the deadline for intervener registration, one round of information requests, a workshop, FEI's response to undertakings at the workshop, and written final and reply arguments;

D. On August 4, 2017, FEI submitted its Annual Review for 2018 Delivery Rates Application materials (Application). FEI also submitted an evidentiary update to the Application on September 26, 2017;

E. By Order G-177-17 dated December 4, 2017, the Commission approved FEI's request for interim delivery rates and rate riders effective January 1, 2018; and

F. The Commission has reviewed the Application and evidence filed in the proceeding and considers that approval is warranted.

NOW THEREFORE pursuant to sections 59 to 61 of the *Utilities Commission Act*, for the reasons attached as Appendix A to this order, the Commission orders as follows:

1. FEI is approved to maintain delivery rates for 2018 at approved 2017 levels, holding the delivery charge and basic charge at existing 2017 levels, on a permanent basis effective January 1, 2018.
2. The following deferral account requests are approved:
    a. Creation of a rate base deferral account for the 2020 Revenue Requirement regulatory proceeding with an amortization period to be proposed when that application is filed;
    b. Creation of a rate base deferral account for the Surrey Operating Agreement regulatory proceeding with a three-year amortization period;
    c. A three-year amortization period for the existing 2016 Cost of Capital Application deferral account, commencing in 2018; and
    d. A name change of the 2017 Revenue Surplus deferral account to the 2017–2018 Revenue Surplus deferral account, and an addition of the 2018 surplus of $7.960 million to the 2017–2018 Revenue Surplus deferral account.
3. The Biomethane Variance Account Rate Rider for 2018 in the amount of $0.026 per gigajoule (GJ) is approved on a permanent basis, effective January 1, 2018.
4. Revenue Stabilization Adjustment Mechanism riders for 2018 in the amount of $(0.041) per GJ are approved on a permanent basis, effective January 1, 2018.
5. The Phase-in Rider Balancing Account Rate Rider and Rate Stabilization Deferral Account Rate Rider for 2018 in the amount of zero per GJ are approved on a permanent basis, effective January 1, 2018.
6. FEI is approved to transfer the ending 2017 balances in the Rate Stabilization Deferral Account, Phase-in Rider Balancing Account, and Amalgamation Regulatory Account to the Residual Delivery Rate Riders deferral account.
7. FEI is directed to comply with all reporting requirements outlined in the Reasons for Decision attached as Appendix A to this order.
8. FEI is directed to file as a compliance filing the finalized financial schedules for the 2018 test period no later than 30 days from the date of this order.

DATED at the City of Vancouver, in the Province of British Columbia, this 21st day of December 2017.

BY ORDER

Original signed by:

D.J. Enns
Commissioner

Attachment

FortisBC Energy Inc.

Annual Review for 2018 Delivery Rates

Reasons for Decision

December 21, 2017

Before:
D. J. Enns, Panel Chair/Commissioner
B. A. Magnan, Commissioner
R. D. Revel, Commissioner

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1.0 Introduction

1.1 Background

By Order G-138-14 dated September 15, 2014, the British Columbia Utilities Commission (Commission, BCUC) approved a Performance Based Ratemaking (PBR) Plan for FortisBC Energy Inc. (FEI) covering a six-year period commencing in 2014. A primary purpose of the PBR Plan is to create an incentive for FEI to adopt a productivity focus and seek out sustainable operating and capital savings while maintaining service quality as measured by Service Quality Indicators (SQIs). The PBR Plan provides for an equal sharing of any PBR-related savings between the customer and FEI.

A key element of the PBR Plan is the provision for an annual review. As part of the FEI Application for Approval of a Multi-Year PBR Plan for 2014 through 2019 Decision (PBR Decision), the Commission set out the following items to be addressed at each annual review:

1. Evaluation of the operation of the PBR Plan in the past year(s) and identification by any party of any deficiencies/concerns with the operation of the PBR Plan that have become apparent.
2. Review of the current year projections and the upcoming year's forecast.
3. Identification of any efficiency initiatives that FEI has undertaken, or intends to undertake, that require a payback period extending beyond the PBR Plan period and make recommendations to the Commission with respect to the treatment of such initiatives.
4. Review of any exogenous events that FEI or stakeholders have identified that should be put forward to the Commission for decision as to their exclusion from the PBR Plan.
5. Review of FEI's performance with respect to SQIs. Bring forward recommendations to the Commission where there has been a "sustained serious degradation" of service.
6. Assess and make recommendations with respect to any SQIs that should be reviewed in future annual reviews.
7. Assess and make recommendations to the Commission on the scope for future annual reviews.[1]

On August 4, 2017, FEI filed its Annual Review for 2018 Delivery Rates Application (Application). FEI forecasts a decrease in the delivery rate of 0.5 percent from 2017, but proposes to hold 2018 rates at 2017 levels and to capture the difference in the existing Revenue Surplus deferral account, stating: "This will avoid the volatility associated with a rate decrease in 2018 followed by a larger rate increase in 2019 when other large capital projects enter the rate base."[2]

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[1] FEI Application for Approval of a Multi-Year Performance Based Ratemaking Plan for 2014 through 2019 (PBR), Decision dated September 15, 2014, pp. 185-186.
[2] Exhibit B-2, p. 1.

On September 26, 2017, FEI filed an evidentiary update to the Application (Evidentiary Update). FEI explains that the following two items have resulted in changes to the Application and the resulting revenue surplus effective January 1, 2018:

1. Change to the completion date for the Tilbury Expansion project; and
2. Update to the Average Weekly Earnings (AWE)-BC index.[3]

The item with the greatest impact on the 2018 revenue surplus is the delay in the completion of the Tilbury Expansion Project, which is delayed until at least the end of 2017. The impact of this delay, and the updated AWE-BC results, increases the forecast 2018 revenue surplus from $3.824 million to $7.960 million. FEI continues to propose to hold 2018 rates at 2017 levels and to capture the difference in the existing Revenue Surplus deferral account.[4]

1.2 Approvals sought

FEI seeks the following approvals pursuant to sections 59 to 61 of the *Utilities Commission Act* (UCA):

1. Maintain 2018 delivery rates at approved 2017 levels, holding the delivery charge and basic charge at existing levels;
2. The following deferral account approvals as described in Sections 7.5 and 12.4 of the Application:
    a. Creation of a rate base deferral account for the 2020 Revenue Requirement regulatory proceeding with an amortization period to be proposed when that application is filed;
    b. Creation of a rate base deferral account for the Surrey Operating Agreement regulatory proceeding with a three-year amortization period;
    c. A three-year amortization period for the existing 2016 Cost of Capital Application deferral account, commencing in 2018; and
    d. A name change of the 2017 Revenue Surplus account to the 2017-2018 Revenue Surplus account, and an addition of the 2018 surplus of $7.960 million to the 2017–2018 Revenue Surplus account;
3. A Biomethane Variance Account (BVA) Rate Rider for 2018 in the amount of $0.026 per gigajoule (GJ) as calculated in Section 10.2.1 of the Application;
4. Revenue Stabilization Adjustment Mechanism (RSAM) riders for 2018 in the amount of $(0.041) per GJ as set out in Table 10-11 in Section 10.2.2 of the Application; and
5. The transfer of the ending 2017 balances in the Rate Stabilization Deferral Account (RSDA), Phase-in Rider Balancing Account and Amalgamation Regulatory Account to the Residual Delivery Rate Riders deferral account as described in Section 10.2.3 of the Application.[5]

These approvals are addressed in Section 2 of the Reasons for Decision.

[3] Exhibit B-2-1, p. 1.
[4] Exhibit B-2-1, pp. 1–3.
[5] Exhibit B-2, p. 2, FEI Reply Argument, pp. 1–2.

1.3 Application review process

In accordance with the Regulatory Timetable established by Order G-115-17, the following review process was undertaken:

- One round of Commission and intervener information requests (IRs);
- A workshop open to all participants held on October 17, 2017;
- An opportunity for FEI to file responses to undertakings arising from the information requested at the workshop;
- Written final arguments from interveners filed by November 9, 2017; and
- FEI's written reply argument filed by November 17, 2017.

The following interveners registered in the proceeding:

- BC Sustainable Energy Association and the Sierra Club of British Columbia (BCSEA-SCBC);
- British Columbia Old Age Pensioners' Organization *et al.* (BCOAPO);
- Canadian Office and Professional Employees' Union, Local 378 (MoveUP); and
- Commercial Energy Consumers Association of British Columbia (CEC).

1.4 Interim rate approval

On November 30, 2017, FEI submitted a request to the Commission for approval of interim delivery rates and rate riders effective January 1, 2018 (Interim Rate Application). In the Interim Rate Application, FEI requested approval to maintain delivery rates for 2018 at the existing approved 2017 levels and to establish various rate riders for 2018. FEI stated that due to the procedural timetable being later in the year than in prior annual reviews, FEI is filing this request in the event that the Commission may not be able to issue its decision by December 8, 2017, allowing enough time for implementation of permanent rates for January 1, 2018.[6]

By Order G-177-17 dated December 4, 2017, the Commission approved the Interim Rate Application.

1.5 Issues arising

In addition to the approvals sought by FEI in the Application and subsequently updated in the Evidentiary Update, the following issues arose during the course of the proceeding requiring further determinations and/or discussion:

1. Treatment of formula capital expenditures in excess of the capital dead-band;
2. SAP Integration; and
3. Annual review process and PBR evaluation.

These issues are addressed in Section 3 of the Reasons for Decision.

[6] Exhibit B-12.

2.0 Determinations on approvals sought

FEI's approvals sought in the Application and updated in the Evidentiary Update are outlined above in Section 1.2. No issues were raised by parties to the proceeding with respect to FEI's requests and none of the interveners opposed the Commission's approval of FEI's requests in their respective final arguments. Based on the evidence reviewed in this proceeding, **the Panel finds FEI's requests to be reasonable and accordingly approves them. The delivery rate and rate riders previously approved on an interim basis by Order G-177-17 are hereby approved on a permanent basis, effective January 1, 2018.**

The Panel considers it appropriate to maintain 2018 delivery rates at the existing 2017 levels and to record the forecast 2018 revenue surplus in the Revenue Surplus deferral account because this treatment results in less rate volatility and the surplus can be used to mitigate anticipated future larger rate increases caused by large capital projects such as the Tilbury Expansion Project entering rate base in upcoming years.

FEI's requests to establish two new regulatory proceeding deferral accounts are consistent with its previous treatment of regulatory proceeding costs and the Panel therefore finds the requests reasonable.

With regard to the 2016 Cost of Capital Application deferral account, the Panel notes that FEI's request for a three-year amortization period of this account was not approved by the Commission in the previous year's annual review decision and that FEI was directed to provide additional information on the amount of experts/consultants costs and external legal costs.[7] While the Panel remains concerned as to the overall quantum incurred by FEI for its expert/consultant and external legal counsel, we find no evidence to indicate that the costs were not prudently incurred and acknowledge that a contributing factor in the increased costs was the unfavourable exchange rate between US and Canadian dollars.

FEI's requests to set various rate riders, including the BVA Rate Rider and the RSAM rate rider, are consistent with previous Commission approvals and the Panel accordingly finds the requests reasonable.

3.0 Determinations and/or discussion on issues arising

A number of issues were raised in IRs and at the workshop, as well as in final arguments. These issues are addressed in the following subsections.

3.1 Capital spending in excess of the dead-band

In the PBR Decision, the Commission established both a one-year 10 percent capital dead-band, and a two-year 15 percent cumulative capital dead-band with regard to FEI's formula-driven capital spending.[8] Subsequently, in the FEI-FBC Capital Exclusion Criteria under PBR Reasons for Decision attached to Order G-120-15, the Commission directed FEI, in the event that the dead-bands are exceeded, to include in its annual review application a recommendation as to any adjustment to base capital.[9]

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[7] FEI Annual Review for 2017 Delivery Rates, Order G-182-16 and Reasons for Decision, dated December 7, 2017, Appendix A, p. 12..
[8] FEI PBR Decision, p. 81.
[9] FEI-FBC Multi-Year Performance Based Ratemaking Plans for 2014 through 2019, Approved by Decisions and OrderG-138-14 and G-139-14 Capital Exclusion Criteria under PBR – Compliance Filing, Order G-120-15 and Reasons for Decision, dated July 22, 2015, Appendix A, p. 17.

In FEI's previous annual review application, the FEI Annual Review for 2017 Delivery Rates (2017 Annual Review), FEI projected that it would exceed the two-year cumulative capital dead-band by 4.1 percent, or $6.118 million, and requested Commission approval to remove this amount from the earnings sharing calculation and instead add the amount to opening plant in service for 2017. The Commission approved FEI's requested treatment in the Reasons for Decision attached as Appendix A to Order G-182-16.[10]

In this Application, FEI states that it expects to exceed the cumulative capital dead-band by 17.74 percent. Similar to the approach proposed in the 2017 Annual Review, FEI proposes to add 17.74 percent of its 2017 capital, or $26.473 million, to its opening plant in service for 2018 so that the two-year cumulative capital variance is within the two-year dead-band of 15 percent.[11]

FEI also notes that although in the 2017 Annual Review it had projected a 2016 dead-band adjustment of $6.118 million, the actual 2016 dead-band adjustment was $9.176 million. As a result, the amount added to FEI's 2017 opening plant in service was actually $9.176 million instead of the previously projected $6.118 million.[12]

PBR formula capital spending

Over the first three years of the PBR term (i.e. 2014 through 2016), actual total capital spending (excluding non-formula capital expenditures) has been $35.602 million, or 8.54 percent, higher than formula. Of this total, $34.287 million is attributable to growth capital.[13]

For 2017, FEI projects that actual total capital spending will exceed the capital formula by $41.218 million, or 27.62 percent. Of this total, $14.547 million is expected to be attributable to growth capital and $26.671 million is expected to be attributable to sustainment/other capital.[14]

FEI submitted that it "considers the 2017 capital formula variance to be significant in the context of the PBR Plan because the variance is materially over the dead band." [15] FEI further confirmed that it expects that it will exceed the capital dead-band in each of the remaining years of the PBR term.[16]

With regard to growth capital, FEI stated that there is little likelihood that the volume and cost assumptions utilized in developing the PBR Base Capital costs for growth capital will be reflective of actual results during the remainder of the PBR term.[17] However, FEI expects that, excluding any variances resulting from growth capital, 2017 will be the year with the largest sustainment/other capital variance during the PBR term.[18]

FEI's growth capital is composed of capital spending on mains, meters, and service line additions (SLAs). The two components of growth capital which have contributed to the majority of the variance between actual and formula growth capital are mains and SLAs. The two primary factors driving the increased costs are: (i) an

[10] FEI Annual Review for 2017 Delivery Rates, Order G-182-16 and Reasons for Decision, dated December 7, 2017, AppendixA, p. 16.
[11] Exhibit B-2, p. 14.
[12] Ibid.
[13] Exhibit B-2, Table 1-4, p. 11.
[14] Exhibit B-2, Table 1-4, p. 11.
[15] Exhibit B-3, BCUC IR 10.2.
[16] Exhibit B-3, BCUC IR 10.3.
[17] Exhibit B-3, BCUC IR 6.3.
[18] Exhibit B-3, BCUC IR 10.2.

increase in the volume of service and main installations; and (ii) a higher per installation cost than was utilized in calculating the approved formula growth capital amounts.[19]

With regard to the projected $26.671 million sustainment/other capital variance for 2017, FEI states that in addition to the formula-related pressures it is experiencing, it is faced with other capital cost pressures in 2017 due to work that had been re-prioritized from previous years of the PBR term into 2017 and due to managing "unforeseen urgent and higher priority activities in 2017."[20] FEI states that in order to manage cost pressures experienced during years 2014 to 2016, some projects that were assessed as being "less critical" to the system, or that were temporarily less time-sensitive, were reprioritized to future years.[21] Some of the more significant work that had been re-prioritized from previous years of the PBR term includes the following:

- Km of 168 mm renewal on Lougheed Highway in Burnaby ($1 million in 2017);
- 18 smaller main renewals throughout the province ($3.6 million in 2017);
- Mt. Hayes - install second run for fuel gas system and process gas system, Amine system upgrade (collectively $1.16 million in 2017);
- Joyce Avenue station, district station upgrade ($560 thousand in 2017); and
- Workforce Management Software Replacement ($890 thousand in 2017).[22]

FEI also provides a list of capital projects that it had originally identified for execution during the PBR Plan term but has now decided to delay until after the PBR term. FEI explains that it "reprioritizes capital spending as part of its routine management of the capital portfolio and has done so in prior years to accommodate unforeseen events and work, and to mitigate in part some of the pressures seen in the past years of the PBR term." If a project is assessed to be "less critical" to FEI's system, or is considered less time-sensitive, it may be reprioritized to future years to accommodate more urgent projects.[23]

The following table shows some of the projects which FEI had originally planned to initiate during the PBR Plan term but has now delayed until after the PBR Plan, along with the estimated capital cost of each project:[24]

[19] Exhibit B-2, Appendix C4, p. 2.
[20] Exhibit B-2, p. 11.
[21] Exhibit B-2, Appendix C4, p. 8.
[22] Exhibit B-3, BCUC IR 8.1.
[23] Exhibit B-2, Appendix C4, Table C4-5, pp. 17-18.
[24] Exhibit B-3, BCUC IR 9.1.

Description	Estimated Timing	Estimated Cost ($millions)	Current Status
Class Location Upgrade: 765m (9 segments) of 1975 vintage 323mm OD East Kootenay Link Mainline, Salmo and Creston	2016	$1.9	Planned for 2022
Class Location Upgrade: 1319m (1 segment) of 2000 vintage 610mm OD Southern Crossing Pipeline, West of Moyie River at Yahk	2017	$2.0	Planned for 2022
Class Location Upgrade: 2782m (1 segment) of 2000 vintage 610mm OD Southern Crossing Pipeline, Grand Forks	2018	$3.5	Planned for 2022
Tilbury LNG Plant Buildings	2018	$1.4	Planned for 2020. Delayed to assess business requirements.
Distribution Main, Service Renewals and Alterations: Penticton Second Supply – Penticton	2015	$2.4	Planned for 2020. Reprioritized due to capital constraints and to allow routing and siting review with the City of Penticton.
The addition of pipe storage to the Burnaby Operations building	2014	$1.9	Delayed due to further review of requirements for space strategy and capital constraints.

Treatment of capital spending in excess of the capital dead-band

A number of options were explored in IRs for treating the projected 2017 capital expenditures in excess of the capital dead-band:

1. FEI's proposed approach of adding the 2017 capital expenditure amount in excess of the cumulative capital dead-band (i.e. $26.473 million) to its opening plant in service for 2018 so that the two-year cumulative capital variance is within the two-year dead-band. FEI would also reduce the cumulative capital expenditures utilized in the earnings sharing mechanism by the same amount, meaning that there would be no earnings sharing on the amount by which FEI exceeded the dead-band.[25]
2. Re-basing the capital formula which would result in adjusting the PBR Base Capital formula spending amount for the remainder of the PBR Plan term. This option would require a separate regulatory process.
3. Including the capital expenditures in excess of the capital dead-band as part of the earnings sharing amount so that the costs of the additional capital expenditures would be shared 50/50 between FEI and ratepayers.

[25] Exhibit B-2, p. 14.

With regard to the option of re-basing formula capital as opposed to FEI's proposed approach, FEI submitted the following:

> …FEI is nearing the end of its fourth year of the PBR Plan, with only 2018 and 2019 left in the PBR term. Given the re-basing proceeding that would be required to properly set a new base capital level for the PBR term, it is likely that any change to the PBR plan would not be implemented until 2019. Given the short time span remaining in the term, any-rebasing will not have a material impact on cost recovery or rates in general.[26]

With regard to other options for treating the capital spending in excess of the dead-band, such as sharing the costs 50/50 with ratepayers (i.e. the same treatment applied to costs within the dead-band), FEI stated the following:

> FEI understands this to mean that the capital above the dead-band is not added to rate base the following year, but that customers pay for one-half of the return through the earnings sharing mechanism for the remaining years of the PBR term. FEI understands this to be the same as removing the dead-band mechanism on capital spending altogether, which would not be appropriate…The formula is a fundamental component of the PBR Plan, and removing the dead band on the capital formula would change the balance struck by the Commission in its PBR Decision…FEI does not believe it would be fair to remove the protection of a symmetrical dead band now that the risk of higher capital requirements has materialized for the utility.[27]

FEI submits that by not adjusting the capital formula amount through re-basing, the incentive properties of the PBR Plan remain intact and consistent throughout the remainder of the PBR term.[28] When asked to clarify how the incentive properties are expected to remain intact given that under FEI's proposed approach capital spending in excess of the dead-band will automatically be added into the following year's opening plant in service and not be subject to the 50/50 earnings sharing mechanism, FEI responded as follows:

> The incentive properties remain intact because the PBR Plan remains as originally approved, with incentives for savings within the dead band but not outside the dead band…Consistent with the PBR Plan, there is no PBR-specific incentive once the dead band is exceeded. However…FEI relies on prudent capital management practices, and adheres to consistent policies and procedures to execute on the required capital expenditures both to support growth in customers and to maintain the safety and integrity of the gas system, regardless of whether capital expenditures fall within the dead band outside of the dead band.[29]

FEI further submitted that given the PBR Plan is nearing the end of its fourth year, with only 2018 and 2019 left in the term, and that a re-basing proceeding would be required to properly set a new base capital level for the PBR term, it is likely that any change to the PBR Plan would not be implemented until 2019. Thus, any impact from re-basing would not have a material impact on cost recovery or rates in general.[30]

[26] Exhibit B-3, BCUC IR 10.8.
[27] Exhibit B-3, BCUC IR 10.8.
[28] Exhibit B-2, p. 14.
[29] Exhibit B-3, BCUC IR 10.4.
[30] Exhibit B-3, BCUC IR 10.8.

Position of the parties

BCOAPO states that the treatment of capital expenditures should be re-examined should an additional PBR plan be proposed, and that in any rebasing review, major capital projects should be subject to a prudency review. BCOAPO further states that because the current PBR Plan term is almost over, it would not be efficient to reopen the PBR Plan at this time to examine capital expenditures.[31]

CEC submits that the "consistent over-spending relative to formula for capital is evidence that the formula has over-simplified a complex cost structure and does not serve its purpose well."[32] CEC further expresses concern that a "significant number of capital projects have been deferred and are creating cost pressures at this time showing that the formula approach to capital is a poor design."[33]

CEC submits that "formula for capital determination without accountability for appropriate capital project planning combined with incentives to re-prioritize capital outside the PBR period for benefits is not a suitable approach to efficiency in capital management."[34] However, CEC agrees with FEI that it is reasonable to leave the current capital formula in place for the remainder of the PBR Plan term.[35]

MoveUp raises issues with capital spending in the context of the overall design of the PBR plan. These issues are discussed in subsection 3.3.

BCSEA-SCBC indicates concurrence with FEI's proposed treatment of capital expenditures.[36]

FEI responds that it has been transparent in its reporting of capital expenditures and that while it has not been able to keep capital spending within the PBR formula, CEC's concerns about projects deferred outside the PBR Plan are not warranted.[37] FEI rejects that it has deferred capital expenditures unnecessarily and states that its decisions regarding capital expenditures are subject to re-prioritization and ongoing management, and that it has gained no benefits as a result of deferring such expenditures.[38]

Commission determination

The Panel is concerned about the continuing trend of capital expenditures exceeding the capital dead-band, particularly given the significant amount by which FEI projects its capital expenditures to exceed the dead-band in 2017. The Panel also has concerns that, contrary to FEI's statements in IR responses, the incentive properties of the PBR Plan are diminished as a result of FEI's proposed approach of adding the capital expenditures in excess of the dead-band to the next year's opening plant in service. The Panel notes that under FEI's proposed approach, which was approved by the Commission in the 2017 Annual Review, the actual capital expenditures added to 2017 opening plant in service were $3.058 million or 50 percent higher than the amount projected during the 2017 Annual Review.

It is clear based on the evidence that FEI expects to exceed the capital dead-band in each of the remaining years of the PBR Plan term and that growth capital in particular will continue to exceed formula amounts. The Panel

[31] BCOAPO Final Argument, pp. 4-5.
[32] CEC Final Argument, p. 13.
[33] CEC Final Argument, p. 11.
[34] CEC Final Argument, p. 11.
[35] CEC Final Argument, p. 20.
[36] BCSEA-SCBC Final Argument, p. 3.
[37] FEI Reply Argument, p. 15.
[38] FEI Reply Argument, p. 16.

also notes FEI's response to BCUC IR 6.3 in which FEI confirmed that there is little likelihood that the volume and cost assumptions utilized in developing the PBR Base Capital costs for growth capital will be reflective of actual results during the remainder of the PBR term.[39] Given these circumstances, re-basing formula capital would generally be an appropriate action to take so as to bring the formula spending into better alignment with FEI's actual capital spending needs. Further, it is clear that the Commission in the PBR Decision contemplated re-basing as a potential course of action, as the Commission stated, when considering the cumulative impact of capital spending outside the dead-band: "The Panel finds this an appropriate mitigation, providing the dead-band trigger results in a rebasing of the capital formula, and that in this eventuality, the rebased amount be applied to the subsequent year's formula."[40]

However, the Panel acknowledges that the PBR Plan term is nearing the end and that any changes at this time to base capital resulting from re-basing would not take effect until the final year of the PBR Plan term. Thus, the Panel does not consider it appropriate to impose the additional regulatory process and costs which would be required for a re-basing hearing given the limited time remaining in the current PBR Plan term. While the Panel does consider there to be some merit to including the capital spending in excess of the dead-band as part of the 50/50 earnings sharing mechanism, as this would potentially serve to better maintain the incentive properties of the PBR Plan, the Panel acknowledges FEI's statement that this would result in a change to the overall PBR Plan design and that such a change is not within the scope of this annual review. Additionally, none of the interveners oppose FEI's proposed approach. **Therefore, the Panel approves FEI's proposal to remove the amount of formula capital which has exceeded the cumulative dead-band from the earnings sharing calculation, and to add the amount of capital in excess of the dead-band to FEI's opening 2018 plant additions balance.**

Given the ongoing issues with capital spending, the Panel directs FEI to continue to report on capital spending in the manner outlined in the FEI Annual Review for 2017 Delivery Rates Reasons for Decision, attached as Appendix A to Order G-182-16, for the remainder of the PBR Plan term.[41] These capital reporting requirements must include updating the information in Table 1-4 provided in the Application as well as updating the information in Appendix C4 to the Application.

3.2 SAP integration

FEI describes a new initiative in the current Application which it refers to as the "SAP Integration" initiative. The purpose of the initiative is to integrate the FEI and FortisBC Inc. (FBC) SAP systems, moving towards a common SAP platform for both companies, and it will primarily include the integration of the Human Resources, Supply Chain and Finance systems in SAP. FEI describes the benefits as including "a simplified support model, alignment of processes, simpler business processes (i.e. employee expense processing and single sign-on), reduced licensing costs and integrated payroll."[42] FEI clarified in response to BCUC IR 5.2 that "[a]lthough FBC also utilizes SAP for many of the same functions as FEI does, the planned common platform is the one currently being used by FEI."[43] FEI explained that configuration changes and improvements will be made to the existing up-to-date FEI SAP platform to "align processes, adopt best practices, allow for upcoming and potential future projects that provide efficiencies, and the implementation of paperless expense management and single sign-on module."[44]

[39] Exhibit B-3, BCUC IR 6.3.
[40] Exhibit B-3, BCUC IR 10.7, Attachment 10.7.
[41] FEI Annual Review for 2017 Delivery Rates, Order G-182-16 and Reasons for Decision, dated December 7, 2017, Appendix A, p. 17.
[42] Exhibit B-2, p. 9.
[43] Exhibit B-3, BCUC IR 5.2.
[44] Exhibit B-3, BCUC IR 5.2.

FEI expects to complete the project in the third quarter of 2018 for a total estimated cost of $4.5 million. FEI proposes to allocate the costs between FEI and FBC based on the number of employees between the two companies, which results in a cost allocation of 75 percent to FEI and 25 percent to FBC. FEI expects total operations and maintenance (O&M) expense savings for the project to be approximately $0.9 million annually, with $0.6 million savings expected in FEI and $0.3 million savings expected in FBC. The O&M savings are expected to start being realized in 2019.[45] For FEI, the annual forecasted O&M savings related to licensing and contractor costs are expected to be $150 thousand and $300 thousand, respectively.[46]

At the workshop, FEI filed FBC's response to BCUC IR 6.5 in the FBC Annual Review for 2018 Rates proceeding which explains why the allocation method of number of employees was chosen for allocating the SAP Integration costs. In this response, FBC explained that the number of employees is "representative of the drivers of the costs being incurred for the project and is consistent with the cost-causality approach…For example, the employees in each of FEI and FBC are the primary users of the paperless expense management and single sign on module of the SAP integration project, which supports the number of employees as an appropriate cost driver for the project costs." FBC further stated that this cost allocation approach is often used for shared IT platforms that are used internally by both organizations.[47]

FEI and FBC considered three other potential methods for allocating the SAP Integration costs: (i) the Massachusetts Formula; (ii) the number of customers for each company; and (iii) the benefits to be derived from the project. Based on their review of each method, FEI and FBC concluded that the number of employees is the most appropriate allocator because it "best reflects the driver of the costs."[48]

Position of the parties

BCOAPO states that "[w]ithin the limited scope of the PBR Annual Review process, there was little opportunity to test proposed solutions and none to provide intervener evidence that supports alternative views" as to whether "SAP was the appropriate platform moving forward".[49]

CEC submits that the cost allocations to FBC and FEI are acceptable. However, CEC argues that ratepayers will realize only $0.3 million of benefits from the SAP Integration initiative by the end of the PBR yet will have paid $3 million for the project, while FEI's shareholders will have benefited by $0.3 million with "very little to no risk."[50]

CEC further submits that the SAP Integration project could potentially have been deferred, noting that FEI identified the project as "flexible".[51]

MoveUP states that the SAP project will further integrate FEI and FBC's operations and expresses the following concern:

> …the modified IT platform emerging from the SAP integration project, and the way the work is being re-organized upon it, is obliterating the capacity of the utilities to more precisely track the

[45] Exhibit B-2, p. 9.
[46] Exhibit B-3, BCUC IR 5.1.
[47] Exhibit B-9.
[48] Exhibit B-9.
[49] BCOAPO Final Argument, pp. 4–5.
[50] CEC Final Argument, p. 7.
[51] CEC Final Argument, p. 7.

> sharing of customer call centre services of this nature, to address the situation where the total annual cost exceeds $100,000 in one year.[52]

MoveUP further argues:

> …absent the decision to migrate FBC onto its system, FEI and its ratepayers were managing well within the SAP program; for the most part, purported O&M "savings" for FEI and its ratepayers have consisted of a more efficient way of integrating FBC in FEI's system and delivering shared services to FBC. FEI argues that the impact of the SAP integration includes overall savings to the two FortisBC utilities taken as a whole, it has not demonstrated that the proportional imputed benefit to FEI and its ratepayers arising from the process of upgrading FBC to its platform and facilitating those shared services, realistically supports assigning roughly one half the cost of the project to the utility that is the one receiving the system upgrade.[53]

MoveUP suggests that a "more appropriate approach would be to reverse the allocations as between the two, to provide a 37:63 split as between FEI and FBC."[54]

BCSEA-SCBC did not comment on the SAP Integration in its final argument.

FEI argues that MoveUP's position is "incorrect, appearing to be based more on its opposition to shared services than an assessment of the evidence, and reflects mistaken assumptions about the nature and consequences of the SAP Integration." FEI also points out that MoveUP incorrectly stated that FEI's proposed cost allocation is 63 percent to FEI and 37 percent FBC; whereas the actual proposed cost allocation is 75 percent to FEI and 25 percent to FBC.[55]

FEI counters MoveUP's assertions regarding ability to track costs between FEI and FBC, noting that each of the companies is identified separately under the SAP system using separate company codes and that entries to the system can be sourced by employee network ID's where required.[56] With regard to MoveUP's specific concern relating to call centre time allocation, FEI states that entries are tracked outside the SAP system.[57]

FEI submits that the benefits of the SAP Integration extend "well beyond MoveUP's limited characterization of the project being solely about moving FBC to FEI's SAP system and facilitating shared services." FEI lists 12 benefits of the SAP Integration, including reduced duplication of licensing and hardware costs, reduced dependency on contracted support services, and reduced redundancy when implementing process changes across the companies.[58]

With regard to its proposed cost allocation, FEI submits that the number of employees as a cost allocator is representative of the drivers of the costs being incurred for the project and is therefore consistent with cost causality. Further, FEI submits that its cost allocation approach is often used for shared IT platforms that are used internally by both organizations.[59]

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[52] MoveUP Final Argument, p. 8.
[53] MoveUP Final Argument, pp. 12–13.
[54] MoveUP Final Argument, p. 13.
[55] FEI Reply Argument, p. 4.
[56] FEI Reply Argument, p. 7.
[57] FEI Reply Argument, p. 7.
[58] FEI Reply Argument, p. 8.
[59] FEI Reply Argument, p. 10.

In response to BCOAPO's comments, FEI states that there were opportunities in this proceeding to test the SAP Integration, noting that there were a number of IRs and questions asked at the workshop on this topic.[60]

Panel discussion

The Panel finds FEI's proposed cost allocation for the SAP Integration project to be reasonable. The Panel is persuaded that FEI has reasonably described the costs and benefits of the system and that its decision to allocate costs based on number of employees is reasonable in this case, as this allocation method is reflective of the drivers of the costs being incurred and is therefore consistent with cost causality. While the Panel acknowledges the concerns raised by some interveners regarding the capital spending on the SAP Integration, the expenditures related to this project are being managed by FEI within the formula spending envelope. FEI is not seeking additional approval of the expenditures, nor would it be appropriate for the Panel to make a determination approving or denying these expenditures within the context of the PBR Plan and this annual review.

3.3 PBR evaluation

Many of the interveners raised issues in the workshop and in final arguments regarding the overall PBR Plan, including providing assessments on the current PBR Plan and expressing views on what actions should be taken at the conclusion of the current PBR Plan.

BCOAPO

BCOAPO states that while it does not oppose FEI's requests in the Application, it has significant concerns about the current PBR.[61] BCOAPO provides three areas which should be addressed in any subsequent PBR plan: (i) forecast sales and demands; (ii) forecast capital, and capital outside the dead band; and (iii) prudence of capital expenditures.[62]

MoveUP

MoveUP submits that there "may be consensus that the capital PBR regime has not worked well" and argues that "the deficiencies of the PBR are also exhibited on the O&M side." MoveUP asserts that the expectation of PBR is that it will provide "incremental performance from utility management, over-and-above the very high standard of diligence, prudency and efficiency to which ratepayers are entitled whether under Cost of Service or PBR, and that is embedded in the regulatory compact itself." MoveUP submits that a "demonstrable extra-ordinary benefit" is not apparent on the record.[63]

MoveUp asserts that there is a need for "a 'reality check' on the efficacy of PBR, in relation to the service obligations of the company to its ratepayers that flow more fundamentally from the *Utilities Commission Act* and the regulatory regime which it implements." MoveUP submits that as the current PBR Plan term comes to an end, the "appropriate analytical approach for the Commission and stakeholders to adopt is one of healthy skepticism with regard to the appropriateness of providing yet another cycle" of PBR.[64]

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[60] FEI Reply Argument, p. 12.
[61] BCOAPO Final Argument, p. 1.
[62] BCOAPO Final Argument, pp. 3–4.
[63] MoveUP Final Argument, p. 5.
[64] MoveUP Final Argument, p. 6.

CEC

With regard to O&M savings under the PBR Plan, CEC submits that it is important to assess the source of the savings, and the associated costs, in order to evaluate the success of the PBR.[65] CEC also raises concerns that PBR potentially creates the opportunity for FEI to arrange its Full Time Equivalents (FTEs) in order to earn O&M savings.[66]

CEC raises concerns that the Regionalization Initiative, Project Blue Pencil and the Review of Technology and Infrastructure projects have in each case failed to recover the cost of their investment within the current PBR plan's timeframe.[67] Regarding the Regionalization Initiative, CEC submits that the "economics of the project are significantly poorer from a ratepayer perspective than they would have been under Cost of Service" and that it is "reasonable to consider that the initiative could have been contemplated and available under Cost of Service."[68] Overall, CEC argues that the "Major Initiatives do not represent significant benefits that could not have occurred under prudent management and cost of service regulation."[69]

FEI reply argument

While FEI addresses the interveners' arguments regarding the PBR evaluation, it states that "this proceeding has not laid the evidentiary foundation for the Commission to make findings on the purpose or theory of PBR, or whether a second cycle of PBR should follow the present PBR Plan" and "those are decisions that should be made in the appropriate proceeding designed for that purpose."[70]

With regard to both MoveUP and CEC's submissions on the purpose of the PBR, FEI argues that their submissions repeat the "tenor of the submissions already heard by the Commission before approving the current PBR Plan" and points to the Commission's statement in the PBR Decision that "the purpose of implementing a PBR mechanism is to provide an environment where efficiencies are created through actions initiated by the utility." FEI argues that the evidence shows that the PBR mechanism has successfully created this environment.[71]

FEI counters MoveUP's claim that savings to date under the current PBR Plan have been trivial, setting out that over the life of the current PBR Plan, O&M savings have totaled $34.4 million and that in each year FEI has met the target 1.1 percent productivity factor, which accounts for an additional $10 million in O&M savings. The savings in FEI's view have contributed to rate increases less than inflation and FEI points out that it is not earning a return on half of the capital expenditures within the dead-band and that the ability to earn a return on capital expenditures beyond the dead-band is deferred until the next year.[72]

FEI uses the foregoing argument to counter CEC's assertion that ratepayers would have been equally or better served had rates been set using the cost of service model as opposed to the use of performance based rate making. [73]

[65] CEC Final Argument, p. 2.
[66] CEC Final Argument, p. 9.
[67] CEC Final Argument, pp. 4–5.
[68] CEC Final Argument, p. 4.
[69] CEC Final Argument, p. 8.
[70] FEI Reply Argument, p. 11.
[71] FEI Reply Argument, p. 17.
[72] FEI Reply Argument, pp. 17-18.
[73] FEI Reply Argument, pp. 17-18.

FEI submits that CEC's submission on major initiatives are "misleading and incorrect", noting that CEC does not explain how it calculates the ratepayer costs and benefits of the initiatives, and that although FEI has been able to replicate some of CEC's calculations, it does not agree with the underlying logic. FEI challenges CEC's basis of calculating net costs and benefits of the cited projects, noting that the savings generated will endure beyond the current PBR period. In reference to Project Blue Pencil, FEI challenges CEC's estimated cost of $2.8 million and return of $2.8 million[74] during the current PBR period by noting that the cost of the project was less than $0.3 million and that it is returning ongoing cost savings of $1 million annually.[75]

FEI further argues that CEC's comments on "what might have been done under cost of service regulation are speculative" and it is "not possible, or necessary, to prove that a project would or would not have occurred under a different form of regulation."[76]

With regard to MoveUP's submission that the PBR Plan should be followed by a period of Cost of Service-based regulation, FEI submits that the Commission's PBR Decision approving the PBR Plan assumed a second phase of PBR and provides the following excerpt from the PBR Decision: "While there is no such [benchmarking] study available at this time, the Panel considers that it would be useful to have one completed prior to the application for the next phase of the PBR."[77]

Panel discussion

The Panel acknowledges the parties' comments on the current PBR Plan and their expectations and/or concerns regarding future PBR plans. However, the Panel agrees with FEI that this topic falls outside the scope of this proceeding. The Panel has stated previously in these Reasons for Decision that it is clear based on the evidence that at least the capital formula component of the PBR Plan is not working as originally expected in the PBR Decision; however, the Panel makes no comments or determinations at this time on how capital or other components of the PBR Plan should be treated in the future. Similarly, the Panel makes no determinations on what future form of regulation should take place at the conclusion of the PBR Plan term.

[74] FEI Reply Argument, p. 5.
[75] FEI Reply Argument, p. 13.
[76] FEI Reply Argument, p. 14.
[77] FEI Reply Argument, p. 16.