

**Richard Stout**

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3 March, 2005

Mr. Robert J. Pellatt  
Commission Secretary  
British Columbia Utilities Commission  
PO Box 250  
600 – 900 Howe Street  
Vancouver, BC V6Z 2N3

Dear Mr. Pellatt:

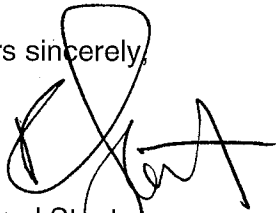
**RE: British Columbia Hydro and Power Authority (“BC Hydro”)  
Compliance Filing on Deferral Accounts (Fiscal 2005 Third Quarter Report)**

Pursuant to Commission Directive No. 17 of the October 29, 2004 Decision, BC Hydro encloses its Fiscal 2005 Third Quarter report on the Heritage Payment Obligation Deferral Account (HDA), the Non-Heritage Deferral Account (NHDA) and the Trade Income Deferral Account (TIDA).

BC Hydro proposes that the prudency review and the clearing of the deferral accounts be discussed as part of BC Hydro's Fiscal 2007 Revenue Requirement Application.

We trust the Commission will find all of the above in order.

Yours sincerely,



Richard Stout  
Chief Regulatory Officer

Enclosure (1)

**BC Hydro**  
**Deferral Account Report**  
**December 31, 2004**

March 2005

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**TAB 1**

**SUMMARY OF DEFERRAL ACCOUNTS**  
**For the nine months ended December 31, 2004**

Reference Schedule	Heritage Deferral Account (HDA)	Non- Heritage Deferral Account (NHDA)	Trade Income Deferral Account (TIDA)	Total
10 Balance as of April 1, 2004	\$ -	\$ -	\$ -	\$ -
11 Transfers for the nine months ended 12 December 31, 2004	C, C-2 153.8	58.5	(128.7)	83.6
13 Interest on deferral accounts (Note 1)	4.1	1.3	(1.9)	3.5
	<u>\$ 157.9</u>	<u>\$ 59.8</u>	<u>\$ (130.6)</u>	<u>\$ 87.1</u>
15				
16 General ledger (G/L) account numbers for Deferral Accounts (Note 2)	076000	076100	076200	
17 G/L account numbers for interest on Deferral Accounts (Note 2)	076001	076101	076201	

- 18 • The transfers from the HDA and NHDA relate solely to variances in energy costs, not related to  
19 changes in load, from the forecast used in establishing rates (See Schedule C). These energy  
20 cost variances are largely due to higher than planned market prices for energy purchases and to  
21 the greater use of energy purchases in place of planned hydro generation. Hydro generation was  
22 reduced and energy purchases increased by approximately 2,670 GW.h due to lower water  
23 inflows and to greater market opportunities for economic purchases. The decision to import  
24 energy instead of utilizing hydro generation is based on many factors, such as the forecast  
25 market price of energy in future periods relative to the current period, current reservoir levels and  
26 future demand requirements.
- 27 • The transfer to the TIDA relates to the higher than Plan Trade Income primarily a result of the  
28 settlement received from Alcan Inc. (See Schedule C-2). The proceeds of this settlement are  
29 shown as part of Trade Income.
- 30 • There were no non-cost of energy variances eligible for deferral account transfers for the nine  
31 months ended December 31, 2004.

32 Notes:

- 33 1. The interest charge/credit is shown as part of finance charges on the Statement of Operations  
34 (Schedule A - 2). Interest is calculated on the ending months balance (excluding the interest  
35 portion) in each deferral account. The interest rate used is BC Hydro's weighted cost of debt.
- 36 2. In compliance with Commission Directive No.19 of the October 29, 2004 Decision, BC Hydro is  
37 providing the G/L accounts from its Code of Accounts used to track the deferral account  
38 balances. The G/L accounts ending in 00 above refer to the deferral account balances before  
39 interest and the G/L accounts ending in 01 above refer to the interest portion on the deferral  
40 accounts. The G/L accounts are Balance Sheet items.

**TAB 2**

1

## Deferral Account Rules

2 The following “rules” are used by BC Hydro for providing clarity in determining the deferral  
3 account transfers. These rules are derived from BC Hydro’s interpretation of the evidence and  
4 testimony provided during the 2004 Revenue Requirement proceeding and in response to  
5 Commission directive No. 19 of the October 29, 2004 Decision.

### 6 Heritage Payment Obligation Deferral Account (HDA)

7 Variances between the forecast and the actual cost for the following components of the Heritage  
8 Payment Obligation will flow through the HDA:

- 9 1. Cost of energy, except those arising from changes in customer load. This item is expanded in  
10 greater detail below to provide clarification on the methodology used to determine variances:
- 11 • Market electricity purchases are treated as the dispatchable resource;
  - 12 • If no market purchases are planned or made, the next dispatchable resource is assumed  
13 to be generation from the Burrard facility;
  - 14 • If generation volumes are lower than Plan, the Load Variance is calculated using the Plan  
15 YTD average market purchase price of electricity;
  - 16 • If generation volumes are higher than Plan, the Load Variance is calculated using the  
17 Actual YTD average market purchase price of electricity (netted for any gains/losses on  
18 energy derivatives and financial instruments used to manage energy costs); and
  - 19 • Cost of energy variances resulting from changes to compensation and mitigation costs,  
20 water rental remissions, or Skagit energy transportation contracts are eligible for deferral.  
21 These are price variances as they do not vary with volume.
- 22 2. Variable costs related to thermal generation.
- 23 3. Significant unplanned major maintenance costs greater than \$1 million related to single event  
24 equipment or infrastructure failure or caused by weather related events.
- 25 4. Significant unplanned major capital expenditures having an incremental annual impact on the  
26 Income Statement greater than \$1 million related to single event equipment or infrastructure  
27 failure or caused by weather related events.
- 28 5. Amortization of unplanned deferred capital costs pursuant to Commission Order No. G-53-02.
- 29 6. All net revenues from surplus hydro electricity sales.
- 30 7. Skagit Valley Treaty revenues and ancillary services revenues.
- 31 • An interest charge/credit is to be calculated on the ending monthly balance (excluding the  
32 interest portion) in each deferral account. The interest rate used is BC Hydro’s weighted cost  
33 of debt during the period.

1 **Non-Heritage Deferral Account (NHDA)**

2 Variances between the forecast and the actual cost for the following components of the Non-  
3 Heritage Payment Obligation will flow through the NHDA:

4 1. Cost of energy - all non-HPO energy costs except those arising from changes in customer  
5 load. This item is expanded in greater detail below to provide clarification on the methodology  
6 used to determine variances:

7 • If IPP and Non-Integrated supply volumes are lower than Plan, the Load Variance is  
8 calculated using the Plan average unit purchase price for IPP's and Non-Integrated  
9 Supply. For Non-Integrated Supply, the fuel costs are treated as the next dispatchable  
10 resource;

11 • If supply volumes are higher than Plan, the Load Variance is calculated using the  
12 weighted average unit prices of Actual IPP's and Non-Integrated energy (i.e. the  
13 variances related to IPP's and Non-Integrated energy are calculated separately). The  
14 weighted average unit price would include any gains/losses on energy derivatives and  
15 financial instruments used to manage energy costs;

16 • Any variances relating to fixed price gas transportation contracts would flow through the  
17 deferral accounts as they do not vary with volume;

18 • Future Trade: when Powerex purchases energy for future trade the cost of the purchase  
19 from the external party and the sale to BC Hydro of this energy is recorded in Powerex  
20 and is included as part of Trade Income. The BC Hydro side of this entry is shown as part  
21 of domestic energy costs (on consolidation, the Powerex revenue from BC Hydro and the  
22 BCH energy costs from Powerex are eliminated). The difference between Actual and  
23 Plan on the BC Hydro side relating to energy for future trade will flow through the Non-  
24 Heritage Deferral Account. The Powerex side of the transaction is part of Trade Income  
25 and flows through the Trade Income Deferral Account. Similar treatment is made when  
26 the energy is returned to Powerex; and

27 • Future Trade: when Powerex purchases energy for future trade, the Heritage Payment  
28 Obligation (HPO) is charged with a notional water rental charge for the use of this energy.  
29 The other side of this entry is shown as part of Non-Heritage energy. These entries are  
30 eliminated on consolidation. The difference between the Actual and Plan notional water  
31 rentals that is part of the HPO would flow through the Heritage Deferral Account. The  
32 opposite variance relating to the Non-Heritage side of the notional water rental  
33 transaction will flow through the Non-Heritage Deferral Account.

34 2. Significant unplanned major maintenance costs greater than \$1 million related to single event  
35 equipment or infrastructure failure.

36 3. Significant unplanned major capital expenditures having an incremental annual impact on the  
37 Income Statement greater than \$1 million related to single event equipment or infrastructure  
38 failure or caused by weather related events.

39 4. Founding Partner Benefits and any CIS Credits under the ABS Contract.

40 • An interest charge/credit is to be calculated on the ending monthly balance (excluding the  
41 interest portion) in each deferral account. The interest rate used is BC Hydro's weighted cost  
42 of debt during the period.

1 **Trade Income Deferral Account (TIDA)**

- 2 • Any variance between the forecast Trade Income and the actual trade income will flow  
3 through the TIDA except where Annual Trade Income is below \$Nil and above \$200 million.
- 4 • An interest charge/credit is to be calculated on the ending monthly balance (excluding the  
5 interest portion) in each deferral account. The interest rate used is BC Hydro's weighted cost  
6 of debt during the period.

**TAB 3**

**Consolidated Statement of Operations**  
**For the nine months ended December 31, 2004**  
**(\$ millions)**

	A	B	C	Reference Schedule
	Actual	Plan	Variance	
<b>REVENUES</b>				
Domestic				
Residential	\$ 701	\$ 724	\$ (23)	
Light industrial and commercial	713	718	(5)	
Large industrial	427	407	20	
Other energy sales	59	60	(1)	
Miscellaneous	40	46	(6)	
	<u>1,940</u>	<u>1,955</u>	<u>(15)</u>	
Intersegment revenues	43	90	(47)	D
	<u>1,983</u>	<u>2,045</u>	<u>(62)</u>	
<b>EXPENSES</b>				
Domestic energy costs	877	645	(232)	B
Operations expense	128	134	6	
Maintenance expense	180	184	4	
Administration expense	93	114	21	
Depreciation and amortization	324	353	29	
Taxes	107	109	2	
Finance charges	320	325	5	
	<u>2,029</u>	<u>1,864</u>	<u>(165)</u>	
<b>DOMESTIC INCOME (LOSS) BEFORE TRANSFER (TO)/FROM DEFERRAL ACCTS</b>	<b>(46)</b>	<b>181</b>	<b>(227)</b>	
<b>TRADE INCOME BEFORE TRANSFER (TO)/FROM DEFERRAL ACCTS</b>	<b>262</b>	<b>71</b>	<b>191</b>	
<b>TOTAL INCOME BEFORE TRANSFER (TO)/FROM DEFERRAL ACCOUNTS</b>	<b>216</b>	<b>252</b>	<b>(36)</b>	
Heritage Deferral Account transfers	154		154	C
Non- Heritage Deferral Account transfers	58		58	C
Trade Income Deferral Account transfers	(129)		(129)	C-2
Regulatory provision for future removal and site restoration costs	10		10	
<b>TOTAL NET INCOME</b>	<b>\$ 309</b>	<b>\$ 252</b>	<b>\$ 57</b>	

The Statement of Operations is presented in a consistent format to the Statement of Operations presented in the 2004 Revenue Requirement Application.

**TAB 4**

**DOMESTIC COST OF ENERGY**  
**For the nine months ended December 31, 2004**

(\$ millions)	Actual	Plan	Variance	Reference Schedule
<b>Heritage Energy:</b>				
Water rentals	\$ 163.4	\$ 181.0	\$ 17.6	
Market electricity purchases	337.2	113.0	(224.2)	C-1
Natural gas for thermal generation	40.4	28.0	(12.4)	
Domestic Transmission	11.7	11.7	-	
Other	2.7	2.6	(0.1)	
	<u>\$ 555.4</u>	<u>\$ 336.3</u>	<u>\$ (219.1)</u>	C
<b>Non-Heritage Energy:</b>				
IPP's and long-term purchase commitments	\$ 294.7	\$ 288.2	\$ (6.5)	
Non-Integrated Areas:				
NIA Fuel	6.5	3.1	(3.4)	
NIA IPP's	4.6	7.6	3.0	
Gas and Other Transportation	10.3	9.8	(0.5)	
Net purchases from Powerex (Trade Account)	6.0	-	(6.0)	
	<u>\$ 322.1</u>	<u>\$ 308.7</u>	<u>\$ (13.4)</u>	C
<b>Total Domestic Cost of Energy</b>	<u><b>\$ 877.5</b></u>	<u><b>\$ 645.0</b></u>	<u><b>\$ (232.5)</b></u>	A - 2
<b>(GW.h)</b>				
<b>Heritage Energy:</b>				
Water rentals	29,473	32,139	2,666	
Market electricity purchases	5,978	3,010	(2,968)	C-1
Natural gas for thermal generation	485	273	(212)	
Exchange net	(131)	189	320	
	<u><b>35,805</b></u>	<u><b>35,611</b></u>	<u><b>(194)</b></u>	C
<b>Non-Heritage Energy:</b>				
IPP's and long-term purchase commitments	4,844	5,050	206	
Non-Integrated Areas:				
NIA Fuel	53	30	(23)	
NIA IPP's	24	45	21	
	<u><b>4,921</b></u>	<u><b>5,125</b></u>	<u><b>204</b></u>	C-1
Total sources of supply	<b>40,726</b>	<b>40,736</b>	<b>10</b>	
Less : Line loss and system use	(3,454)	(3,911)	(457)	C-1
Net sales to Powerex	(261)	(1,128)	(867)	C
<b>Domestic Sales Volumes</b>	<u><b>37,011</b></u>	<u><b>35,697</b></u>	<u><b>(1,314)</b></u>	C-1
<b>(\$/MW.h)</b>				
Water rentals	5.5	5.6	0.1	
Market electricity purchases	56.4	37.5	(18.9)	
Natural gas for thermal generation	83.3	102.6	19.3	
IPP's and long-term purchase commitments	60.8	57.1	(3.8)	C-1
Non-Integrated Areas:				
NIA Fuel	122.6	103.3	(19.3)	
NIA IPP's	191.7	168.9	(22.8)	
<b>Total weighted average cost</b>	21.5	15.8	(5.7)	

The Cost of Energy Schedule is presented in a similar format to the Cost of Energy Schedule (Schedule A-9) presented as part of the 2004 Revenue Requirement Application. The only exception is that this schedule further breaks down energy costs between Heritage and Non-Heritage cost of energy.

**TAB 5**

**TRANSFERS TO HERITAGE (HDA) AND NON-HERITAGE (NHDA) DEFERRAL ACCOUNTS**  
**For the nine months ended December 31, 2004**

**Reconciliation of Energy costs for Deferral Account Treatment**

(\$ millions)	Actual	Plan	Variance	Reference Schedule
<b>Heritage Energy:</b>				
Heritage Energy costs	\$ 555.4	\$ 336.3	\$ (219.1)	B
Notional Water rental (Displaced Hydro) (Note 1)	(1.4)	(5.5)	(4.1)	
Mark to market (gain)/loss on energy derivatives and financial settlements (Note 2)	(11.6)		11.6	C-1
<b>Cost of energy portion of Heritage Payment Obligation</b>	<b>\$ 542.4</b>	<b>\$ 330.8</b>	<b>\$ (211.6)</b>	(a)
<b>Non-Heritage Energy:</b>				
Non-Heritage Energy costs	\$ 322.1	\$ 308.7	\$ (13.4)	B
Net sales to Powerex - Future Use (Note 3)	-	(43.8)	(43.8)	D
Notional water rentals (Displaced Hydro) (Note 1)	1.4	5.5	4.1	
F/X loss(gain) on Pwx trade account (Note 4)	(10.5)		10.5	
Mark to market (gain)/loss on energy derivatives and financial settlements (Note 2)	4.5		(4.5)	
<b>Cost of energy portion of Non-Heritage Payment Obligation</b>	<b>\$ 317.5</b>	<b>\$ 270.4</b>	<b>\$ (47.1)</b>	(b)
<b>(GW.h)</b>				
<b>Heritage Energy:</b>				
Heritage Energy Supply	35,805	35,611	(194)	B
Notional water rentals (Displaced Hydro)	(261)	(1,128)	(867)	B
<b>Heritage Payment Obligation Energy</b>	<b>35,544</b>	<b>34,483</b>	<b>(1,061)</b>	C-1

**(\$millions)**

**Transfer to HDA:**

Total Heritage energy variance	(a)	\$ 211.6	
Less: Load Variance (Note 5)		57.8	
<b>Transfer to HDA</b>		<b>\$ 153.8</b>	A

**Transfer to NHDA:**

Total Non-Heritage energy variance	(b)	\$ 47.1	
Less: Load Variance - IPP's (Note 6)		(11.6)	
Load Variance - Non-Integrated areas		0.2	
<b>Transfer to NHDA</b>		<b>\$ 58.5</b>	A

**Notes:**

1. Notional water rentals (Displaced Hydro) relates to water rentals associated with trade income. The notional water rental mechanism is described in the response to BCUC IR No. 1.2.36 dated January 23, 2004. The transactions relating to the notional water rental are eliminated on consolidation and there is no net impact on the combined HDA and NHDA as the transactions are mirrored within each account.

2. In order to mitigate some of the commodity risk on domestic energy costs, BC Hydro enters into various forward contracts with Powerex for the purchase of electricity and natural gas. Powerex can then choose to match these forward contracts with a third party or can take on the risk/benefits on their own. The transactions between BC Hydro and Powerex are eliminated on consolidation. With respect to the deferral accounts, any gain or loss on the derivative instruments on the Powerex side would flow through the Trade Income Deferral Account (TIDA) and the corresponding gain/loss on the BC Hydro side would flow through the HDA and NHDA. While the gain/loss on these derivative instruments are not shown as part of energy costs on the financial statements due to GAAP reporting requirements, these gains/losses are reclassified for the calculation of deferral account transfers as they are part of managing the energy purchase costs.

The gain on energy derivatives related to Heritage energy totalled \$16.3 million for the nine months ended December 31, 2004 with the corresponding loss shown as part of Trade Income. The loss on energy derivatives related to Non-Heritage energy totalled \$2.3 million with the corresponding gain shown as part of Trade Income. The gain/loss on BC Hydro's side related to these energy derivatives is shown as part of intersegment revenues.

**Transfer to HDA and NHDA continued**

**Schedule C-1**

1 BC Hydro also enters into derivatives with third parties to manage foreign exchange exposure on energy  
 2 transactions. Gains and losses on these transactions are netted against Heritage and Non-Heritage Energy  
 3 purchase costs as they are used to manage these energy costs and mitigate risk. On the consolidated  
 4 income statement these gains/losses are recorded as part of other miscellaneous income to comply with  
 5 GAAP reporting requirements. The loss on financial settlements for the nine months ended December 31,  
 6 2004 was \$4.7 million related to Heritage Energy and \$2.2 million related to Non-Heritage Energy.

7  
 8 (\$millions)  
 9 **Summary:**

	<u>Heritage</u>	<u>Non-</u>	<u>Total</u>	<b>Reference Schedule</b>
11 Gain (loss) on energy derivatives	\$ 16.3	\$ (2.3)	\$ 14.0	D
12 Gain (loss) on Foreign exchange derivatives	(4.7)	(2.2)	(6.9)	
13	<u>\$ 11.6</u>	<u>\$ (4.5)</u>	<u>\$ 7.1</u>	

14  
 15  
 16 3. These sales relate to the return of energy bought by Powerex in prior periods to enable future sale. These revenues are  
 17 eliminated against trade cost of energy on consolidation. The transactions between BC Hydro and Powerex has no net  
 18 impact on the combined NHDA and the Trade Income Deferral Account.

19  
 20 4. This relates to the foreign exchange gain on the Trade Account payable to Powerex. Powerex would have a corresponding  
 21 loss on their receivable and this loss would be part of Trade Income. Foreign exchange gains/losses arise as the Trade  
 22 Account is recorded in \$US. The gain/loss on the BC Hydro side is eliminated against the loss/gain on the Powerex side on  
 23 consolidation within the finance charge component. As the mirror entry for Trade Income relating to F/X on the Trade Account  
 24 is recorded on the Non-Heritage energy side, there is no net impact on the combined NHDA and TIDA due to these  
 25 transactions.

26  
 27  
 28 5. Load Variance for HDA is calculated as the Load Volume variance multiplied by the actual average price of market  
 29 purchases net of the gain/losses on mark to market energy transactions. (1,061 GW.h \* \$54.5/MW.h) = \$57.8 million.

30  
 31 (\$millions)

			<b>Reference Schedule</b>
34 Market energy purchases	\$ 337.2		B
35 Mark to market gains	(11.6)		C
36	<u>\$ 325.6</u>	(1)	
37			
38 Market energy purchase volumes (GW.h)	5,978	(2)	B
39			
40 Average price ((1)/(2)) (\$/MW.h)	54.5		
41			
42 Load Volume variance (GW.h)	1,061		C
43			

44 6. Load Variance for NHDA calculated as Load Volume variance multiplied by the Plan average price of IPP and  
 45 long-term purchase commitments (206 GW.h \* \$57.1/MW.h) = \$11.6 million.

46  
 47 **Reconciliation of Energy Volumes (GW.h)**

48			
49 Increase in domestic sales volumes from Plan	1,314		B
50 Decrease in line loss and system use	(457)		B
51 Net change in volumes	<u>857</u>		
52			
53 Change in HPO energy volumes	1,061		C
54 Change in Non-Heritage energy:			
55 IPP's and long-term purchase commitments	(206)		B
56 Non-Integrated areas	<u>2</u>		
57	<u>857</u>		

**Transfer to Trade Income Deferral Account**  
**For the nine months ended December 31, 2004**  
(\$ in millions)

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		<b>Reference Schedule</b>
Actual Trade Income	\$ 262.0	A - 2
Excess over Cap for deferral account transfer	<u>(62.0)</u>	
	\$ 200.0	
Less: Plan Trade Income	<u>71.3</u>	A - 2
Transfer to Trade Income Deferral Account	<u><u>\$ 128.7</u></u>	A

BC Hydro has exceeded the \$200 million cap on Trade Income largely a result of the settlement recieved from Alcan Inc in December 2004.

**TAB 6**

**INTERSEGMENT REVENUES**  
**For the nine months Ended December 31, 2004**

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	<u>Actual</u>	<u>Plan</u>	<u>Variance</u>	<u>Reference Schedule</u>
Net sales to Powerex - Future Trade <i>(Note 1)</i>	\$ -	\$ 44	\$ (44)	C
Point-to-Point wheeling charge to Powerex <i>(Note 2)</i>	18	35	(17)	
Point-to-Point wheeling charge to BCH <i>(Note 3)</i>	9	9	-	
Allocation of BCH Corporate costs to Powerex <i>(Note 4)</i>	2	2	-	
Mark to Market gains on energy derivatives with Powerex <i>(Note 5)</i>	14	-	14	C
<b>Total</b>	<b><u>\$ 43</u></b>	<b><u>\$ 90</u></b>	<b><u>\$ (47)</u></b>	A - 2

**Notes:**

1. These sales in the Plan relate to a return of energy bought by Powerex in prior periods to enable future sale. These revenues are eliminated against trade cost of energy on consolidation.
2. These transmission revenues relate to an allocation of BC Hydro's cost of purchases of point-to-point transmission within BC for export and some import transactions. These revenues are eliminated against trade cost of energy on consolidation.
3. These transmission revenues relate to an allocation of BC Hydro's cost of purchases of point-to-point transmission relating to BC Hydro's Skagit Valley Treaty commitment. These revenues are eliminated against domestic cost of energy on consolidation.
4. These revenues relate to an allocation of corporate costs to Powerex and are eliminated against trade income on consolidation.
5. This relates to a mark to market gain on energy derivatives with Powerex. This revenue is eliminated against trade income on consolidation. The gain is broken down as a \$16.3 million gain on Heritage Energy and a \$2.3 million loss on Non-Heritage Energy.