

**BC Hydro
Revenue Requirements Application
2004/05 and 2005/06**

**Joint Industry Electricity Steering Committee
Information Request No. 1**

COST OF SERVICE – Operating, Maintenance & Administration (OM&A)

Q 1. Reference: Application, Page 2-40; Appendix J, Page 1

Explanation: Additional information is required on historical expenses and trends.

Request:

- a. Provide a schedule of OM&A for each year from 1994 to 2006 in the format set out below. The cost information provided should not include allocations of support services.

Annual – 1993/94 to 2005/06

Generation

Operation

Maintenance

Administration & Other - Direct

Total

Less: Non-Recurring Costs (Describe)

Normalized Generation Expenses

Transmission & BCTC

Operation

Maintenance

Administration & Other - Direct

Total

Less: Non-Recurring Costs (Describe)

Normalized Generation Expenses

Distribution

Operation

Maintenance

Administration & Other - Direct

Total

Less: Non-Recurring Costs (Describe)

Normalized Generation Expenses

Administration & Other
Executive, Legal, Property Services,
Finance & CFO, Audit, Treasury,
Regulatory, Human Resources,
Customer Care, Communications
& Public Affairs, Information Systems
& Technology
Engineering
Research & Development
DSM/PowerSmart Administration

Total
Less: Non-Recurring Expenses (Describe)
Normalized Admin & Other Expenses

Total OM&A Expenses
Operation
Maintenance
Administration & Other
Total
Less: Non-Recurring Expenses (Describe)
Normalized Expenses
Add: Overheads Capitalized
Gross OM&A Expenses

Head Count
M&P
IBEW
OPEIU
Total
Transferred to ABS
Total

Q 2. Reference: Not Applicable

Explanation: BC Hydro entered into the ABS contract and anticipates significant savings. The application does not address other opportunities for savings in operations or maintenance activities.

Request:

- a. Has BC Hydro investigated cost saving opportunities by contracting out operations and maintenance activities or through workplace flexibility initiatives?
- b. Provide copies of all studies of operating and maintenance efficiency initiatives.

- c. What restrictions, if any, have prevented BC Hydro from implementing changes and achieving efficiencies and cost savings in operating and maintenance activities?

Q 3. Reference: Application, Page 3-57; Page 8-20; Page 9-64; BCUC IR1.75.7

Explanation: With the restructuring of BC Hydro into the Line of Business model and the formation of BCTC, BCTC and the Business Units have taken on some functions and others are provided by Corporate. There has been increases in costs with the creation of BCTC.

Request:

- a. Identify all incremental operating and capital costs resulting from the BCTC reorganization by year, by function from 2002/03 to 2005/06.
- b. Identify all incremental operating and capital costs resulting from the implementation of the Line of Business model by year, by function from 2003/03 to 2005/06.
- c. Provide the business plan(s) for the reorganizations and all reviews of the results achieved.

Q 4. Reference: BC Hydro Annual and Quarterly Reports

Explanation: BC Hydro and Powerex have incurred legal and other costs related to the actions taken by the FERC and the State of California and BC Hydro has made an allowance for uncollectible accounts. The Trade Revenue and net income of BC Hydro is net of Powerex costs and income surpluses and shortfalls have flowed into and out of the RSA. Powerex also manages the Downstream Benefits (DSBs) on behalf of the Province.

Request:

- a. Provide the Trade Revenue, the DSB revenue and the amount of the allowance for uncollectible accounts related to electricity sales for each of BC Hydro/Powerex and the province by year from 1994/5 to 2005/6 and describe how the allowance for each was determined and the amount that is outstanding at this time.
- b. What are the prospects for recovery of the outstanding amounts?
- c. Provide the costs related to the defense of such sales by year by type of expense.

- d. Provide the recovery of costs from the province by year for:
 - i. Sale of DSBs,
 - ii. Legal and other costs.
- e. Provide the policy for recovery of BC Hydro and Powerex costs related to the management and sale of DSBs.

Q 5. Reference: Application, Page 1-25; Page 3-32; Page 3-33; Page 3-49; Page 3-50; Page 5-6; Page 5-10; Page 5-25; Page 5-45; Page 6-40; Page 6-42; Page 6-43; Page 8-2; Page 8-6; Page 8-10; Page 8-13; Appendix B; Appendix I, PowerSmart 10 Year Plan, Page 4, 11, 21; BCUC IR 1.5.10; BCUC IR 1.5.14; BCUC IR 1.5.36; BCUC IR 1.19.1; BCUC 1.20.1; BCUC 1.20.2; BCUC 1.20.3; BCUC IR 1.70.4; BCUC 1.75.5; Schedule 75-5-3; Schedule 75-5-4; Schedule 75-6-2; Schedule 75-6-3; BCUC IR 75-10, Internal Audit Report Page A6; IAR Maintenance Page 16; BCUC IR 1.83.1;

Explanation: BC Hydro incurs costs for stakeholder relations in a number of areas. Information on these expenditures is required.

Request:

- a. Provide the operating costs, capitalized costs and capital expenditures incurred by year from 1993/94 to 2005/06 for:
 - i. Donations,
 - ii. Corporate Communications & Public Relations,
 - iii. Advertising & Promotion:
 - PowerSmart,
 - Powerex,
 - BC Hydro,
 - iv. Aboriginal Relations & Negotiations.

Q 6. Reference: Application, Page 3-29, 3-30, 3-31

Explanation: BC Hydro compensation programs include incentive compensation and the application includes incentive compensation costs.

Request:

- a. What is the level of incentive pay and total compensation including benefits for BC Hydro relative to the marketplace?
- b. Provide the budget and actual incentive compensation by year from 2002/01 to 2003/04 by Business Unit, including subsidiary operations (Powerex, Westech, Powertech).
- c. Where incentive pay was 10% less than or greater than budgeted incentive pay, by Line of Business, identify the reasons why.

Q 7. Reference: Application, Page 2-57

Explanation: BC Hydro has included amounts for contingencies in the forecast OM&A.

Request:

- a. Provide a listing for 2004/05 and 2005/06 of all of the allowances for contingencies included in the application.

Q 8. Reference: Application, Page 2-13

Explanation: Depreciation includes:

- Amortization of studies and abandoned or indefinitely deferred projects
- Amortization of deferred Aboriginal negotiation and settlement costs

Request:

- a. Identify any depreciation amounts for studies, projects and deferred Aboriginal costs for 2003/04 to 2005/06.
- b. Provide the costs incurred by year from 1994/95 to 2005/06 for studies, projects and deferred Aboriginal costs.

Q 9. Reference: Application, Page 2-16

Explanation: BC Hydro has included \$9 million in 2004/05 for increased depreciation due to a revision in the estimated useful life of certain distribution assets. Of the total, \$3 million represents a one-time adjustment.

Request:

- a. Explain why BC Hydro did not record the one-time adjustment in the 2003/04 fiscal period.

Q 10. Reference: Application, Page 3-43, Table 3-26

Explanation: BC Hydro has provided a comparison of BC Hydro and utility industry IT spending.

Request:

- a. Confirm that the benchmark is an industry average.
- b. Are the IT spending statistics only operating costs or operating and capital costs?

- c. What cost savings are expected from forecast IT expenditures from 2003/04 to 2005/06?

CAPITAL EXPENDITURES

Q 11. Reference: Application, Page 11-2, Table 11-2

Explanation: Additional information is required about the level of and trend in capital expenditures and maintenance programs. BC Hydro has cancelled or deferred capital and maintenance expenditures in the past. The current application is proposing a significant increase in expenditures and in addition, BC Hydro has requested deferral accounts

Request:

- a. Provide a schedule of actual capital expenditures and maintenance programs from 1993/94 to 2005/06 in the format below:

Annual – 1993/94 to 2005/06

Capital Expenditures

Generation
Transmission
Distribution
Administration & Other (General Plant)

Total

Maintenance Programs

Generation
Transmission
Distribution

Total

Overheads Capitalized (ODC)
Allowance for Funds Used During Construction (AFUDC)

- b. Provide the budgeted capital expenditures by year in the format set out above and in the format of Table 11-2.
- c. Where expenditures have varied by 10% or more from budget or where there were unanticipated one-time expenditures, provide an explanation.

- d. Identify capital and maintenance programs for system upgrades and reliability that were proposed to occur between 1993/94 and 2002/03 that were either removed from the budget or cancelled. Provide the reasons.

Q 12. Reference: Application, Appendix I, PowerSmart 10 Year Plan, Page 28, 45, 61, 77, 93, 109, 125, 141, 157, 173; BCUC IR 1.25.2

Explanation: BC Hydro PowerSmart programs include programs where the Total Resource Costs exceed the benefit.

Also, the BC Hydro IEP assumes reductions in demand (capacity and energy) from DSM. Information is required on how the DSM results are linked into the IEP and planning horizon.

Request:

- a. Provide, by program, the accumulated and annual capital costs and related revenue requirements of DSM programs where the TRC benefit/cost is less than 1.0.
- b. Describe how BC Hydro monitors DSM results and how BC Hydro deals with unanticipated demand growth or lower DSM results in the context of planning horizon for new capacity and supply.

Q 13. Reference: Application, Page 2-41

Explanation: BC Hydro Includes Contributions & Grants from customers in the calculation of return on equity. CIAC are provided to offset the cost of capital additions to serve customers and to mitigate the effect on rates to all customers.

Based on the ROE in the application, the effect of the current treatment of CIAC is to increase rates to all customers. This occurs because CIAC are not applied against plant or treated as zero cost capital and the cost of the pre-tax ROE is significantly greater than the amortization.

Request:

- a. Provide a schedule for 2003/04 to 2005/06 comparing the ROE on Customer Contributions to the amortization of the customer contributions and showing the net increase or decrease in revenue requirements.
- b. Explain why BC Hydro should not be required to discontinue the collection of CIAC and to refund all customer contributions.

DEFERRAL ACCOUNTS

Q 14. Reference: Application, Page 2-22 to Page 2-24

Explanation: BC Hydro has proposed a number of deferral accounts including:

- BCTC Transition
- Major Maintenance (\$1 million per event)
- Major OM&A (\$1 million per event)
- Major Capital (\$1 million per event – dep'n, financing)
- Finance Charges
- Skagit Valley Treaty Revenues

Deferral Accounts related to Heritage supply, energy costs and trade revenues are addressed separately.

Request:

- a. If the financial performance of BC Hydro is improved by other events such as increased sales, lower expenses or lower capital expenditures, how would these be reflected in the deferral and recovery of costs?
- b. Given the apparent one-sided nature of the deferral accounts, what incentives do BC Hydro and BCTC have to control, mitigate and offset unanticipated costs?
- c. How were the materiality levels for deferral of costs determined?
- d. How do the risks for the events for which deferral accounts have been proposed compare to the risks and volatility of other financial items such as sales?
- e. Confirm that the deferral account for finance charges will include short term and long term interest cost changes related to interest rates.

COST OF ENERGY

Q 15. Reference: Application, Page 3-3; Chapter 2A

Explanation: BC Hydro has provided an update on water levels, domestic energy costs and trade revenues.

The news release dated February 17, 2003 for the 3rd quarter results stated that: *“Improved water inflow, decrease in prices of electricity and natural gas purchases and higher domestic consumption improve outlook for year end”*.

The February 20, 2004 covering letter to the Application updates (Chapter 2A) states that: *“Inflows. Including snow pack, since the Application was prepared have been below normal.”* Chapter 2A states that: *“The major reasons for the changed forecasts include lower forecast water inflows in F2005.”*

Request:

- a. Reconcile the comments in the 3rd quarter financial results and the update of the Application?
- b. Will BC Hydro be providing an update after March and prior to the hearing date?
- c. In order to better understand the Cost of Energy and the likely Trade Revenue, provide an update of natural gas prices, electricity prices and the spark spread with monthly information from October 1, 2003 to 2005/06 with a comparison to the assumptions used in the application.

Q 16. Reference: Application, Page 2-22 to Page 2-24

Explanation: Heritage supply, trade revenues and domestic energy costs are all affected by water levels. The Heritage supply was estimated by BC Hydro in the Heritage Contract proceeding to be 49,125 GWh per year under average water conditions. In the revenue requirements application the Heritage supply is less than the supply under average water conditions. It is not clear that domestic energy costs and trade revenue are based on average water conditions.

Request:

- a. Confirm that the revenue requirements for 2004/05 and 2005/06 are based on average water conditions and 49 125 GWh. If not, provide the effect on revenue requirements assuming average water conditions and a reconciliation of the Heritage supply to 49 125 GWh.
- b. Will the Heritage Deferral Account include all variances in domestic energy costs and trade revenue resulting from variances from average water conditions? If not, identify any changes in revenues or costs that will not flow through a deferral account.
- c. In the opinion of BC Hydro, what is a normal cycle in years for water conditions?
- d. Should the recovery period of the HDA, including domestic energy costs and trade revenues, reflect the cycle for average water conditions?

Q 17. Reference: Application, Page 2-22

Explanation: BC Hydro has applied for a deferral account for cost of energy and variable operating costs of thermal generation.

Request:

- a. Provide expected range of variability in these costs and the effect on revenue requirements net of any expected effect on trade revenue.

EQUITY & COST OF CAPITAL

Q 18. Reference: Application, Page 10-5 to 10-8

Explanation: BC Hydro has based the ROE in the application on the Terasen pre-tax ROE.

Request:

- a. What was the fiscal period for the Terasen effective income tax rate used in the Application?
- b. Provide the statutory provincial and federal income tax rate (including LCCT) for the reference year and subsequent years.
- c. If BC Hydro has not adjusted the pre-tax ROE in the application for any announced reductions in corporate income tax rates, explain why reductions have not been reflected.

Q 19. Reference: Application, Page 3-3; Chapter 2A

Explanation: BC Hydro has provided an update on foreign exchange and interest rate forecasts. The update has resulted in a reduction in revenue requirements.

Request:

- a. Will the province be updating the forecast interest rates and foreign exchange rates prior to the hearing date?
- b. Will BC Hydro be providing further updates to the forecast?

Q 20. Reference: Application, Page 2-15; Page 2-16; Page 2-18; Page 2-41; Page 2-43; Page 2-66; Page 6-76; Appendix J, Page 9, 10; BCUC IR 1.8.1; BCUC IR 1.78.1 (Dep'n Study)

Explanation: BC Hydro has proposed to transfer the balance in the Site Restoration & Removal Costs (SRRC/FSRS) to Retained Earnings and to recover future costs from customers in rates. Under the BCUC Uniform System of Accounts, these costs are included in Accumulated Depreciation. In the US, FASB 143 raises issues that are similar to those raised by CICA Handbook Section 3110.

Request:

- a. Confirm that the reserve for Site Restoration & Removal Costs has been accumulated through a charge against income and have been recovered through customer rates.
- b. Confirm that BC Hydro intends to recover all future costs for SRRC from customers.
- c. In the opinion of BC Hydro, explain why the balance in Site Restoration & Removal Costs should not be:
 - i. Left recorded as it is,
 - ii. Treated as accumulated depreciation, or
 - iii. Refunded to customers.
- d. Provide details of how other Canadian regulated utilities are treating, or propose to treat, the SRRC. Please indicate in each case:
 - i. Did the utility seek regulatory approval?
 - ii. Did the regulator approve the transfer of the SRRC provision to retained earnings?
 - iii. Did the regulator approve the recovery of all future SRRC costs from customers?
 - iv. Provide relevant portions of the decision by the regulator, with reasons.
- e. Provide details of how the U.S. regulated utilities that BC Hydro is aware of, have dealt with similar situations under FASB 143. Please indicate in each case:
 - i. Did the utility seek regulatory approval?
 - ii. Did the regulator approve the transfer of the SRRC provision to retained earnings?
 - iii. Did the regulator approve the recovery of all future SRRC costs from customers?
 - iv. Provide relevant portions of the decision of the regulator, with reasons.

Q 21. Reference: Volume 1, Section 3.7.3, Page 2-17, 2-18; Volume 2, Section J; Response to BCUC Information Requests No. 1.53.1 and 1.78.1

Explanation: BC Hydro describes proposed changes with respect to accounting necessitated by Section 3110 Asset Retirement Obligations, in the CICA Handbook. These changes have rate implications from a financial accounting perspective as well as from a depreciation accounting perspective.

Request:

(a) Please provide a detailed explanation of BC Hydro's accounting practices with respect to depreciation, the recording of net negative salvage (future removal and site restoration), accounting for retirements including determination of retirement dates treatment of salvage and costs associated with retirements and replacements.

(b) For each asset plant account or CAU provide the projected original cost, the accumulated depreciation the provision for future dismantling costs and the provision for salvage proceeds as of March 31, 2004 and the rates used for depreciation and FRSR. In addition indicate whether the recommendations of Gannett Fleming were adopted with respect to amortizing the reserve deficiency as shown in Figure 1 of the March 27, 2003 review letter.

(c) Table 2-14 indicates an impact of \$244 million for the reversal of Future Removal and Site Restoration (FRSR) costs booked in prior years.

(i) By utility plant account or capital asset units (CAU) provide the provision for future dismantling costs recorded by year that totals the \$244 million.

(ii) By utility plant account or CAU provide the provision for future salvage proceeds recorded by year that totals the \$64 million.

(iii) The 2003 Annual report shows an amount of \$174 million far March 31, 2003. Provide a detailed reconciliation between this amount and the \$244 million shown on Table 2-14.

(iv) To the extent not explained in (iii) above explain the forecast of \$180 million shown on Schedule A-2 (page 2-41)

(v) For each utility plant account or CAU for which future dismantling costs were recorded, provide the study, work papers, products or other documentation relied upon to determine the amount of future dismantling costs recorded in each year and any adjustments by plant account to the amounts as the result of retirements or changed estimates (???)

(vi) For each utility plant account (CAU) for which future salvage proceeds were recorded, provide the study, work papers, products or other documentation relied upon to determine the amount of future salvage proceeds recorded in each year and any adjustments by plant account to the amounts as the result of retirements or changed estimates.

(d) Page 2-18 states “[a]s at April 1, 2004, the accumulated depreciation on these ARO assets, which will be reflected in retained earnings, will be \$7 million. The present value of the ARO liability as at April 1, 2004 will be \$18 million. The

accumulated accretion to April 1, 2004 on this liability, which will be reflected in retained earnings, will be \$4 million.”

- (i) Provide a detailed description of the ARO assets including the plant accounts or CAU's.
- (ii) Provide all working papers, work products or other documentation used to determine the \$7 million for the retroactive accumulated depreciation adjustment.
- (iii) Provide all working papers, work products or other documentation used to determine the \$18 million for the ARO liability.
- (iv) Provide all working papers, work products or other documentation used to determine the \$4 million for the accumulated accretion.
- (v) Provide all documentation, including legal opinions, contracts, laws, regulations or other work papers or products used to determine that a legal obligation exists or that a promise that conveys an expectation of promissory estoppel exists.
- (vi) Provide the accounting entries proposed, including the BC Hydro and BCUC account numbers and descriptions, for each of 2004, 2005 and 2006 to record the proposed entries for each of:
 - A. The reversal of the \$244 million FRSR provision,
 - B. The recording for the \$64 million adjustment of future salvage proceeds,
 - C. The recording for the retroactive accumulated depreciation on ARO asset of \$7 million,
 - D. Recording of the retroactive accretion on ARO liability of \$ 4 million,
 - E. Recording the ARO liability of \$18 million, and
 - F. Recording the ARO asset of \$14 million.

Q 22. Reference: Appendix J, Page 1

Explanation: BC Hydro has provided a comparative Income Statement for F1994 and 2003. The Net Income in 1994 was forecast to be \$190 million and for 2003 is forecast to be \$418 million.

Request:

- a. Provide a reconciliation and explanation for the increase in Net Income from 1994 to 2003.
- b. Provide the following information for each year from 1993/94 to 2005/06:

Net Income
Rate of Return on Equity
 Allowed
 Actual
Transfers to/from RSA
Dividends to the Province
Provincial Revenues from DSBs