



---

# **Submission to the BC Utilities Commission**

**BC Hydro and Power Authority  
Revenue Requirement Application 2004/5 and 2005/6**

**April 2004**

## **By the Citizens for Public Power**

608-207 West Hastings Street  
Vancouver, B.C.  
Tel: 604-681-5939  
Fax: 604-681-2127

**Prepared by Dr. John Calvert**

## Table of Contents

Introduction	3
Summary	3
Background	4
Increasing cost of purchasing privately produced energy	5
Impact of Power Smart	12
Additional costs of restructuring	15
BC Hydro dividend to government	18
Cost of providing new services to IPPs	19
Cost of contracting out administrative services	19
Cost of establishing and operating the BCTC	22
Cost of not permitting BC Hydro to invest in new generation	28
Future costs of RTO West membership	29
Conclusion	33
Appendix A	35
Appendix B	38
Appendix C	39
Resume of Dr. John Calvert	42

## Introduction

BC Citizens for Public Power is a non-profit consumer and public advocacy group committed to protecting the rights and interests of residents of British Columbia, both as citizens and as consumers of electricity. Its membership includes a wide range of supporters from all regions of the province and all sectors of society. Citizens for Public Power believes in the benefits of a publicly owned and operated electricity system which maintains cost based rates and supplies electricity to all regions of the province using a postage stamp rate structure.

BC Citizens for Public Power is registered as a non-profit society funded by donations from individuals and groups.

## Summary

This brief examines BC Hydro's and the BC Transmission Corporation's (BCTC) arguments for a rate increase of 8.9%.

We believe that BC Hydro and the newly formed BCTC have not demonstrated a case for a rate increase of 8.9%. Both BC Hydro and the BCTC have requested a rate increase to finance three significant new expenditures which we believe cannot be justified. The first is the cost of purchasing increasingly expensive privately produced electricity. The second the cost of BC Hydro subsidies - totaling \$690 million over 10 years - which are included in the estimates for the revised Power Smart Program. This expenditure is particularly questionable given that much of the money will be allocated to large, highly profitable industrial corporations. The third is the cost of restructuring BC's electricity system for the benefit of private energy producers and power marketers.

In our view, the only justification for a rate increase is to make needed investments to improve the performance and capacity of the public system. However, when we look at the details of current and projected BC Hydro<sup>1</sup> expenditures we find that a considerable amount of the money will not go to this objective. Rather, it will be allocated to a quite different purpose: the wholesale restructuring of BC Hydro to accommodate a new market system for electricity. A significant part of the requested rate increase is to pay for

---

<sup>1</sup> For a useful discussion of the conceptual issues associated with privatization, see Pulitzer Prize winner: Paul Starr, "The Meaning of Privatization" *Yale Law and Policy Review* 6 (1988): 6-41. Reprinted in Alfred Kahn and Sheila Kamerman, eds., *Privatization and the Welfare State* (Princeton University Press, 1989).

a restructuring plan that will eventually eliminate many of the benefits BC Hydro has enjoyed as a publicly owned and controlled, vertically integrated utility.

We also believe that the current request by BC Hydro for a revenue increase is the first step in ‘adjusting’ customers in BC to prices set by a highly volatile electricity market, rather than BC’s historic cost based approach based on public investment in, and ownership of, generation facilities. The outcome of this ‘adjustment’ process will be to ratchet up prices to levels comparable to the prevailing prices in the U.S over time.

## **Background**

This submission examines the recent revised application by BC Hydro for a revenue increase of 8.9%. This request consists of a 7.23% increase on April 1<sup>st</sup>, 2004 and an additional 1.67% increase 30 days after the BCUC issues its order confirming the new rate, which the applicant anticipates will be approved by the autumn.<sup>2</sup>

BC Hydro has indicated that it needs the additional revenue for a number of reasons. Some of these are legitimate, including: funding to cover the rising costs of various productive inputs; the need to upgrade older equipment; the requirement to modernize some of its aging control centres and the fact that BC Hydro has not had a rate increase since 1994, despite cumulative inflation of about 14% during the past decade.

However, others are much less defensible, including: the projected expenditures for restructuring B.C.’s electrical system; the additional cost of expensive energy purchases from the private sector, the requirement to provide a full dividend to government despite the additional costs its recent legislation and policies have imposed on BC Hydro; new expenditures associated with setting up a separate transmission company (BC Transmission Corporation); the costs of establishing deferral accounts and other insurance arrangements dedicated to the further development of an electricity market structure, and the funding for an ambitious new Power Smart program that will cost ratepayers an estimated \$690 million over the next decade.

We recognize that BC Hydro has not had a rate increase for 10 years and that inflation has eroded the real value of its revenues significantly during that period. Equipment and facilities are getting older and BC Hydro needs to make some capital investments to renew/upgrade various components of its existing system. There is a good case for

---

<sup>2</sup> It is understood that BC Hydro is filing this revenue application on its own behalf and on behalf of the newly formed BC Transmission Corporation.

investing in new publicly owned assets to modernize the system and we support such investments.

At the same time BC Hydro has benefited from much lower interest rates on its debt in recent years. It has also been able to take advantage of advances in technology and information systems that have made it cheaper for it to carry out some of its functions. And, it has made some additional revenue from energy trade, primarily through its subsidiary Powerex - revenue which, admittedly, is not guaranteed in the future, given fluctuating market conditions. While these positive factors may not fully offset the impact of inflation on BC Hydro's revenues, they do need to be considered in determining what is actually needed to maintain and improve BC Hydro's services to the people of the province.

### **The Increasing Costs of Purchasing Privately Produced (IPP) Energy**

In its listing of the "Principal Cost Drivers Related to the Test Year Revenue Requirements" (vol. 1. p. 1-15), BC Hydro identifies the increasing cost of energy as the *first* of the 'drivers' behind its request for as significant revenue increase. According to BC Hydro:

*"Relative to F1994, the principal drivers causing the revenue that must be recovered from domestic ratepayers are:*

- *Increased cost of energy."*

The table below (table 6), from BC Hydro's revenue submission, documents the growth in the amount of electricity purchased from IPPs between 1994 and 2003. We note that there have been significant fluctuations in the amount of power generated by BC Hydro, due to annual precipitation and demand growth (among other factors).<sup>3</sup> However, the key development is the increase in the amount purchased from IPPs which has risen by 77.4% during the period.

---

<sup>3</sup> BC Hydro's year by year generation numbers are contained in its response to the first round of BCUC requests. The numbers should quite significant variations largely as a result of significant year by year changes in rainfall.

**Table 6. Comparison of Energy Sources**

(GWh)	F1994	F2003	Change
Hydro generation	40,101	47,665	7,564
Independent Power Producers (IPP) and other long-term purchase contracts	2,791	4,950	2,159
Other Energy Purchases	0	896	896
Thermal Resources	3,248	251	(2,997)
Non-integrated Energy	62	96	34
Net Purchase from Powerex		1,113	1,113
Net Storage Returns (Exchange Net)	131	(1,605)	(1,736)
	46,333	53,366	7,033
Line Loss and System Use	(4,315)	(4,689)	(374)
<b>Domestic Sales Volume</b>	<b>42,018</b>	<b>48,677</b>	<b>6,659</b>

The increase in purchases from IPPs has been compounded by the increase in the price of IPP-generated power during the decade. According to the data provided in its submission, BC Hydro is already spending more for the purchase of IPP power than it spends on the generation of its own power.<sup>4</sup> The following tables, again taken from the revenue application provide data on the growth of power purchases from IPPs and the corresponding growth of costs to BC Hydro.

<sup>4</sup> It is not entirely clear from BC Hydro's table whether the costs of its own hydro generated power include the cost of capital and various other overheads. In other words, it is not clear if the table compares apples with apples or if the numbers exclude certain BC Hydro costs that are included in the prices paid to IPPs. However, even if some overhead costs, not included in BC Hydro entry in the table should be added to the public utility's costs, it is clear that generation by BC Hydro is only a fraction of the cost of purchasing similar amounts of power from IPPs.

**Table 7. Comparison of Energy Costs**

<b>(\$ millions)</b>	<b>F1994 (Note 1)</b>	<b>F2003</b>	<b>Change</b>
Hydro	\$217	\$259	\$42
IPPs and other long-term purchase contracts	92	290	198
Other Energy Purchases	0	54	54
Natural Gas for Thermal Generation (Note 2)	48	28	(20)
Non-integrated	11	14	3
Transmission charges and other expenses	1	13	12
Net Purchases from Powerex	0	50	50
<b>Domestic Energy Costs</b>	<b>\$369</b>	<b>\$708</b>	<b>\$339</b>

Notes:

1. Reclassified to conform to presentation in F2003, as described in schedule 1.
2. Natural gas costs in F2003 also include fixed transportation costs of approximately \$10 million related to the Bypass Transportation Agreement between Terasen and BC Hydro.

Table 8 shows the average energy price by source.

**Table 8. Average Energy Price**

<b>(\$/MWh)</b>	<b>F1994</b>	<b>F2003</b>	<b>Change</b>
Hydro	\$5.41	\$5.43	\$0.02
IPPs and other long-term contracts	32.97	58.59	25.62
Other Energy Purchases	0	60.27	60.27
Natural Gas for Thermal Generation	14.78	111.55	96.77
Non-integrated	177.42	145.83	(31.59)
Net Purchases from Powerex	0	44.92	44.92
<b>Weighted average cost (Note 1)</b>	<b>\$8.78</b>	<b>\$14.54</b>	<b>\$5.76</b>

Notes:

1. Relates to total domestic energy costs divided by domestic sales volumes.

According to the preceding tables, the unit cost per MWh of privately generated IPP energy has increased from \$32.97 in 1994 to \$58.59 in 2003 - an increase of 77.4% during the 10 year period. This contrasts with BC Hydro’s costs which have increased by only 2 cents (or only a fraction of a percent) during the same time period.

**IPP purchased power is now more than ten times more expensive than that of BC Hydro generated electricity.<sup>5</sup>**

However, in light of the Province’s direction that BC Hydro will not be allowed to invest in new public electricity generation facilities, the BC’s citizens will not be able to benefit

<sup>5</sup> It could be argued that one reason for the higher IPP costs is that the IPP generation facilities were built more recently than BC Hydro’s facilities. Hence IPP costs reflect the impact of construction price increases. However, it should also be noted that BC Hydro was saddled with long term debt for some of its major projects at interest rates of up to 20% on bonds negotiated in the late 1970s and early 1980s.

in the future from BC Hydro's expertise and experience in building energy generation. Although it may be able to squeeze out some additional electricity from upgrades to existing facilities, there are clear limits to what can be achieved through such expansions. Moreover, the government's policy is clearly to cap public electricity production so that private power producers can expand their share of the B.C. market.

If BC Hydro had purchased all its electricity from private power producers in the past, rather than building its own generation, customers would now be paying far more for their electricity. For no private IPP would be charging prices at BC Hydro's low rates if they could sell the same electricity in the U.S. market at current U.S. prices. The reason we now have cheap power is precisely because we acquired generating assets – assets which were purchased at prevailing prices several decades ago and which now provide the basis for our very inexpensive electricity.

Citizens in Ontario, Alberta, California and many other jurisdictions have seen what it means to be exposed to private, market driven prices in which the amount they pay is determined not by long term average costs of production, but rather by short term marginal costs under highly volatile market conditions.

Given the documented rise in the cost of IPP-purchased electricity over the past decade, and given BC Hydro's reluctance to base its future purchases primarily on short term supply from the market due to the instability of supply and prices, BC Hydro will end up allocating more and more money to expensive, long term electricity purchases from private IPPs.

Another factor pushing up the cost of electricity is the nature of the contracts BC Hydro is negotiating with IPPs. In response to one of our information requests (B1.0), BC Hydro provided us with a table, reproduced below, indicating the total costs and unit costs of IPP power for each year from F2005 to F2013.

### Estimated Costs of Signed IPP Contracts from F2005 to F2013

	2005	2006	2007	2008	2009	2010	2011	2012	2013
Total IPP Cost (\$ millions)	79.64	397.02	422.33	451.63	454.83	444.54	453.21	459.64	463.71
Total IPP Energy (GWh)	6,598	7,004	7,587	8,125	8,062	8,062	8,062	8,061	8,013
IPP Unit Cost (\$MWh)	57.4	56.7	55.7	55.6	56.4	55.1	56.2	57.0	57.9

The preceding table only shows what we have already contracted to purchase. In light of the Province’s directive that in future energy will be purchased from the private sector, there will be significant increases in private power purchases every year from now on. Costs will escalate accordingly.

As the table also shows, these contracts are long term. We understand that most of these contracts are for 10 years or more. Thus BC Hydro is committing itself – and the citizens of BC – to the purchase of extremely expensive energy for many years into the future. The guarantee of long term sales to BC Hydro is providing these private interests with the financial security they need to build new electricity generation assets. BC Hydro is effectively underwriting their capital costs. However, BC Hydro is not acquiring any assets for the money it expends on these contracts.

Volume 2 of BC Hydro’s application includes tables that estimate the growth of electricity consumption in BC in the period up to 2023/24. Obviously there are many variables associated with making projections that far into the future. However, given that these are the best estimates that BC Hydro has, we have calculated the additional amount of energy that would be required compared with this year (2004/05).

BC Total Energy Sales are estimated to be 49,844 GWh and total Gross Domestic requirements 55,657 GWh in 2004/5. The comparable figures for 2023/4 are 65,523 GWh and 73,191 GWh. Thus energy sales – and energy costs from IPP purchased energy would increase as the following table illustrates.

	<b>Projected Energy Sales GWh</b>	<b>Gross Domestic Requirements GWh</b>
2004/5	49,844	55,657
2023/4	65,523	73,191
Increase	15,679	17,534
Cost at IPP price of \$57 MWh	<b>\$894.7 million</b>	<b>\$999.4 million</b>

In other words if we assume current prices with no inflation adjustment, the additional purchases from IPPs could add almost a billion dollars to the cost of BC's energy over the next two decades.

And, if we add in the costs of IPP power that BC Hydro has already contracted to purchase and assume, very optimistically that the price will not increase over the period, the amount being spent on IPP power will be between \$1.4 billion and \$1.5 billion by 2023/4. And, if we built in an inflation factor the numbers would be correspondingly higher.

Moreover, after existing and future contracts have expired, private interests, not BC Hydro, will have full ownership of the generation facilities. BC Hydro (and the residents of BC) will continue to need electricity and will have to purchase it, either through renewed contracts with these IPPs, or from the market. In either case, the price of electricity will be at market rates, which effectively means the price of electricity in the U.S. energy market.

While none of us can predict with accuracy the price of energy in 20 or 30 years time, it is very likely that prices will be far higher than today. Yet without ownership of generation assets, the public will be forced to pay whatever the market will charge for its energy at that point in the future. Otherwise, these IPPs will be free to sell it in the US. And this is despite having effectively supported private IPPs for a decade or more through BC Hydro's contracts to purchase energy power from them.

It may be argued that IPP power is much more expensive than BC Hydro's power because many IPP generation facilities are of much more recent provenance than BC Hydro's major hydro generation facilities. Hence their prices reflect inflation that has occurred in the intervening years. However, in another decade, this power will also appear cheap – except that the benefit of price increases will go to private owners, not the public. In blending the cheaper electricity from older facilities with electricity from more

---

recently built facilities, BC Hydro has kept average energy prices at cost, which means low prices for customers.

Of course the cost of power generated from past investments does not mean that future generation will be at the same price and we are not arguing this case. We realize that the costs of new generation by BC Hydro would not likely be as low as it currently enjoys from the major investments of the 1960s, 1970s and early 1980s. However, we believe that BC Hydro could provide additional power to the province at much lower rates than IPPs, if it were permitted to do so.

Regrettably, the cost comparisons that are needed for this to be properly demonstrated are simply not available. So a major reason for the revenue increase request is to enable BC Hydro to plug the predicted gap in power supply by purchasing high cost power from private producers and suppliers rather than generating its own which we believe would be a much lower cost.<sup>6</sup>

It is also true that some of the facilities are relatively small and therefore do not achieve the benefits of economies of scale that BC Hydro enjoys. But this too speaks to the question of why B.C. is supporting more expensive power from such facilities if cheaper public options are available.

Private IPPs also require a significant rate of return on the investment made by their owners and this gets built into the prices charged to BC Hydro. The public is paying for the investment returns of the shareholders.

Another factor pushing up the cost of IPP produced power is that IPPs do not have the same credit rating as BC Hydro. Put simply, their costs of borrowing are significantly higher than those of BC Hydro. With its AA- rating by Standard and Poors and AA2 by Moody's, BC Hydro is well positioned to borrow the capital required for new generation investments. However, IPPs are clearly not in the same position. They must pay a premium when they borrow. And this premium can be substantial. Given that we are dealing with capital projects where the cost of borrowing is a large proportion of the overall costs, this additional premium can add very significantly to the overall costs of generating new electricity.

---

<sup>6</sup> We also note the long term consequences of owning generation assets. The reason citizens of B.C. are able to enjoy very low cost power today is that the public acquired generation assets during the 1960s, 1970s and early 1980s. At the time, these investments represented a major commitment on the part of the public to the future of BC Hydro. Moreover, the public paid a substantial amount of interest on many of the loans – in some cases as much as 20% - on long term bonds.

---

The extra costs of borrowing are included in the price being charged to BC Hydro for energy. They are another significant factor in driving up the price that BC Hydro pays for IPP generated power. This argument also applies to power purchased from private energy providers out of province as well. Even the very large U.S. private utilities do not have credit ratings as high as BC Hydro and they, in turn must pass on the additional costs of borrowing to their customers, including BC Hydro when it purchases power from them.

For customers, the high cost of IPP energy has been largely obscured in recent years because it has been blended in with the much greater volume of inexpensive, cost-based cost BC Hydro-generated electricity. (See Appendix B for comment on Heritage Contract). However as the proportion of electricity from IPPs grows, BC Hydro will have to pass on these costs to customers through ongoing rate increases. Otherwise it will fail to meet its dividend obligations to the Province. In our view this is a major factor in BC Hydro's request for a revenue increase.<sup>7</sup>

The adoption of a 'blended price' approach that merges the low cost public power with high cost private power in the hydro bills of consumers effectively obscures the higher costs of new private power. For example, none of the IPPs which are contracted through BC Hydro must justify their costs to the BCUC. The public has a right to know the costs of publicly generated versus privately generated power.

Accordingly, we recommend that the BCUC direct BC Hydro to provide full disclosure of these costs in customer bills in the future. It could do this by clearly stating the costs of the public power component and the costs of the private IPP power component and labeling it accordingly.

### **The Impact of Projected Power Smart Subsidies on BC Hydro Customers**

BC Hydro is proposing to spend approximately \$690.6 million over the next decade on a variety of Power Smart initiatives<sup>8</sup>. While we support initiatives that result in lower energy consumption and are strongly in favour of conserving energy, we are very concerned that the specific programs that BC Hydro intends to fund are based on an approach that is fundamentally flawed.

---

<sup>7</sup> This issue was addressed in a letter dated March 18<sup>th</sup>, 1999 from former President and CEO of BC Hydro, Mr. Michael Costello to former Minister Farnsworth which we provided to the BCUC in the hearings dealing with the Heritage Rate. See Appendix A for a copy of the letter.

<sup>8</sup> Vol. 2 Appendix I., Power Smart 10 Year Plan p.3

Power Smart is essentially a subsidy program to encourage electricity users to reduce consumption of electricity and thus limit the environmental and financial costs associated with the production of electrical energy.

Originally, Power Smart was based on the assumption that BC Hydro, as a vertically integrated single supplier of electricity in B.C. would be able to capture the benefits of conservation initiatives by avoiding costly new capital investments. The calculation was as follows. Given the major capital costs of new generation, if BC Hydro could encourage customers to reduce usage, it could offset the costs of Power Smart through avoidance of these capital costs. In its role as a single supplier of electricity, it could also assess the impact of Power Smart in reducing the overall growth of electricity consumption in the province.

However, as noted above, the Province has directed BC Hydro not to make investments in new generation facilities (other than replacing existing equipment and facilities and some upgrades to its current system). Thus it will not make any savings by avoiding new capital investments because it will not be making any capital investments. It therefore cannot capture the benefits. The basic financial rationale for Power Smart has been largely eliminated.

Under the current Government, Power Smart has been transformed from a program that had a rational, economic basis (in the context of a vertically integrated utility) to a program that is essentially a subsidy to energy users. While some of the proposed subsidies, such as improving the energy efficiency of schools, universities, municipalities and other public institutions may provide a pay back to taxpayers in the form of lower electricity use, some of the most costly Power Smart subsidies are being allocated to “load displacement” programs. These do not necessarily reduce the overall amount of energy used or entail an effective form of conservation. Rather what they do is shift production of energy from BC Hydro to the industrial or commercial plants that develop their own (i.e. self) generating facilities.

Shifting the location of the production of electricity is not the same thing as reducing energy use. Moreover, the Power Smart program disproportionately subsidizes major industrial and commercial users, many of whom are highly profitable and can well afford energy conservation expenditures without subsidies from BC Hydro.

The major planned areas of Power Smart Expenditure are as follows:

- 39% or \$265.6 million for the industrial sector;
- 25% or \$171.9 million for the commercial and government sector;
- 16% or \$112.4 million for the residential sector;

- 8% or \$52.4 million in public education and communications with customers;
- 12% or \$88.3 million in administration, overhead costs and management.

The table below provides further details on the year by year projected Power Smart Expenditures:

**Table 4.5 Total BC Hydro Costs (excluding GHG credits, \$000's)**

	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	10 Year Totals
<b>Industrial Sector</b>											
Power Smart Partners	\$ 14,499	\$ 5,572	\$ 7,817	\$ 11,179	\$ 19,041	\$ 19,435	\$ 18,650	\$ 18,956	\$ 19,369	\$ 20,457	\$ 154,975
Load Displacement	\$ -	\$ 21,828	\$ 28,880	\$ 20,928	\$ 10,708	\$ 6,694	\$ 6,426	\$ 5,092	\$ 1,621	\$ 389	\$ 102,778
Sector Enabler Costs	\$ 1,338	\$ 964	\$ 897	\$ 1,035	\$ 1,167	\$ 855	\$ 384	\$ 394	\$ 394	\$ 394	\$ 7,852
<b>sector total</b>	<b>\$ 16,837</b>	<b>\$ 28,364</b>	<b>\$ 37,606</b>	<b>\$ 33,141</b>	<b>\$ 30,916</b>	<b>\$ 26,984</b>	<b>\$ 25,472</b>	<b>\$ 24,442</b>	<b>\$ 21,684</b>	<b>\$ 21,240</b>	<b>\$ 265,606</b>
<b>Commercial &amp; Government Sector</b>											
Power Smart Partners	\$ 5,812	\$ 14,895	\$ 17,562	\$ 19,510	\$ 15,513	\$ 6,037	\$ 199	\$ 199	\$ 199	\$ 199	\$ 79,923
SUCH	\$ 7,274	\$ 13,992	\$ 7,473	\$ 4,150	\$ 1,776	\$ 271	\$ 88	\$ 88	\$ 88	\$ 88	\$ 35,289
Traffic Light Program	\$ 5,632	\$ 5,022	\$ 128	\$ 128	\$ 128	\$ 128	\$ 128	\$ 128	\$ 128	\$ 128	\$ 9,626
Power Smart Express I & II	\$ -	\$ 1,964	\$ 3,193	\$ 3,295	\$ 1,553	\$ 100	\$ -	\$ 100	\$ -	\$ -	\$ 10,206
Lighting Redesign	\$ -	\$ -	\$ 3,381	\$ 2,530	\$ 2,560	\$ 50	\$ -	\$ -	\$ -	\$ -	\$ 8,521
Small Business Coupon Offer	\$ -	\$ 1,532	\$ 25	\$ -	\$ 180	\$ 25	\$ 160	\$ 25	\$ -	\$ -	\$ 1,828
New Construction Program	\$ -	\$ 1,976	\$ 2,329	\$ 2,850	\$ 2,968	\$ 3,163	\$ 202	\$ 202	\$ 202	\$ 202	\$ 13,883
Sector Enabler Costs	\$ 2,024	\$ 1,215	\$ 1,059	\$ 1,428	\$ 1,733	\$ 1,663	\$ 848	\$ 844	\$ 844	\$ 844	\$ 12,503
<b>sector total</b>	<b>\$ 20,742</b>	<b>\$ 40,396</b>	<b>\$ 34,896</b>	<b>\$ 33,434</b>	<b>\$ 26,136</b>	<b>\$ 11,180</b>	<b>\$ 1,368</b>	<b>\$ 1,330</b>	<b>\$ 1,204</b>	<b>\$ 1,204</b>	<b>\$ 171,888</b>
<b>Residential Sector</b>											
New homes	\$ 390	\$ 525	\$ 736	\$ 726	\$ 743	\$ 820	\$ 832	\$ -	\$ -	\$ -	\$ 4,773
Home Energy Upgrade	\$ 330	\$ 501	\$ 459	\$ 482	\$ 505	\$ 505	\$ 505	\$ -	\$ -	\$ -	\$ 3,287
ECM	\$ -	\$ 111	\$ 189	\$ 189	\$ 189	\$ 246	\$ 246	\$ 246	\$ 303	\$ 303	\$ 2,022
VI New Homes furnaces (f.switch)	\$ -	\$ 360	\$ 510	\$ 806	\$ 678	\$ 731	\$ 551	\$ 564	\$ 567	\$ 568	\$ 5,134
DWH conversions (f.switch)	\$ -	\$ -	\$ 427	\$ 772	\$ 772	\$ 772	\$ 554	\$ 554	\$ 554	\$ 554	\$ 4,958
Dryer conversions (f.switch)	\$ -	\$ -	\$ 102	\$ 240	\$ 338	\$ 328	\$ 328	\$ 258	\$ 258	\$ 258	\$ 2,110
Range conversions (f.switch)	\$ -	\$ -	\$ 124	\$ 331	\$ 424	\$ 304	\$ 436	\$ 426	\$ 448	\$ 448	\$ 2,940
Refrigerator Buy-back	\$ 1,082	\$ 4,183	\$ 4,183	\$ -	\$ -	\$ -	\$ -	\$ 2,808	\$ 2,808	\$ 2,808	\$ 17,870
Seasonal LED	\$ 598	\$ 810	\$ 789	\$ 553	\$ 204	\$ 229	\$ 229	\$ 229	\$ 229	\$ 229	\$ 4,043
CFL	\$ 6,690	\$ 13,408	\$ 8,400	\$ 5,375	\$ 5,375	\$ 5,685	\$ 5,191	\$ 3,637	\$ 3,717	\$ 750	\$ 56,227
CFL multifamily	\$ 154	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 154
CCQ	\$ 1,292	\$ 879	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 2,171
Sector Enabler Costs	\$ 1,462	\$ 866	\$ 716	\$ 716	\$ 898	\$ 716	\$ 450	\$ 600	\$ 150	\$ 150	\$ 6,682
<b>sector total</b>	<b>\$ 11,966</b>	<b>\$ 21,642</b>	<b>\$ 14,614</b>	<b>\$ 9,989</b>	<b>\$ 10,094</b>	<b>\$ 10,335</b>	<b>\$ 9,322</b>	<b>\$ 9,320</b>	<b>\$ 9,032</b>	<b>\$ 6,067</b>	<b>\$ 112,381</b>
<b>Portfolio Level Costs</b>											
Public Awareness & Communications	\$ 3,599	\$ 9,176	\$ 8,441	\$ 7,873	\$ 7,828	\$ 7,963	\$ 4,071	\$ 2,076	\$ 1,059	\$ 540	\$ 52,445
Indirect and other enabling costs	\$ 13,219	\$ 15,412	\$ 10,586	\$ 10,797	\$ 11,013	\$ 6,946	\$ 5,389	\$ 5,346	\$ 4,986	\$ 4,602	\$ 88,296
<b>subtotal</b>	<b>\$ 16,818</b>	<b>\$ 24,688</b>	<b>\$ 19,026</b>	<b>\$ 18,470</b>	<b>\$ 18,840</b>	<b>\$ 14,929</b>	<b>\$ 9,460</b>	<b>\$ 7,423</b>	<b>\$ 6,044</b>	<b>\$ 5,142</b>	<b>\$ 140,740</b>
<b>Portfolio Total</b>	<b>\$ 66,363</b>	<b>\$ 116,010</b>	<b>\$ 106,140</b>	<b>\$ 95,036</b>	<b>\$ 86,984</b>	<b>\$ 63,427</b>	<b>\$ 45,622</b>	<b>\$ 42,815</b>	<b>\$ 37,865</b>	<b>\$ 33,663</b>	<b>\$ 690,614</b>

As the above numbers illustrate, the Power Smart program is heavily skewed towards providing investment subsidies to industrial customers. Much of this is either to capture load displacements or investments in the Power Smart Partners Programs. While these investments may result in reduced energy use, the benefits of the investments are enjoyed by the industrial customers, both in terms of the new equipment/technology/facilities and in terms of ongoing reductions in their electricity bills. While this is good for the many of the firms involved, we believe this is not a good deal for BC Hydro and for the taxpayers of B.C.

In response to our request for information on Power Smart subsidies of over \$1 million that have been awarded from 2001 onwards, BC Hydro indicated that it has given \$49 million to Canfor for a turbogenerator in Prince George, \$18 million to Weyerhaeuser for a turbogenerator in Kamloops and \$4 million to UBC for lighting and HVAC. It also indicated that there were four other Power Smart subsidies totaling \$6 million that it had made commitments to, but could not disclose as they had not been “publicly announced”. Canfor had revenues of \$2.95 billion in 2003. Weyerhaeuser had revenues in 2003 of \$19.9 billion U.S.

There is a further point regarding Power Smart spending by BC Hydro. It is that the taxpayers will not be gaining any assets. The capital improvements will be entirely to the benefit of the private interests receiving the subsidies.

If the government wants to subsidize business to reduce its energy consumption, we believe it should do so directly, rather than requiring BC Hydro to pay the costs of the subsidies. This would be a more transparent approach and would enable the citizens of BC to decide whether they believed that such subsidies were justified, or not.<sup>9</sup>

### **The Additional Costs Resulting from Restructuring BC’s Electricity System**

We believe that the second major reason for BC Hydro’s request for additional revenue at this time is the cost of restructuring the corporation to implement a radically different approach to the generation and transmission of electricity based on a competitive, privatized, market model.<sup>10</sup>

The additional costs associated with this restructuring can be broken down to a number of elements as follows:

---

<sup>9</sup> Of course this also raises the question of whether a program ostensibly designed to conserve energy should be focused entirely on electrical energy when subsidies, to the extent they are seen as justifiable, might well have a greater impact in reducing the use of other forms of energy (coal, natural gas, diesel fuel etc.)

<sup>10</sup> In response to an information request that we made, BC Hydro noted the impact of the BCUC’s earlier directive in shaping its policies in this area. It noted that in the 1988 Wholesale Transmission Services (WTS) Decision, the Commission had approved BC Hydro’s application for a “FERC Order 888-type tariff. However, the Commission went beyond this to state the following (we are quoting from the BC Hydro reply to us)

“...to follow North American industry standard terms and conditions (including those prescribed for U.S. electricity utilities by the FERC) and Commission requirements (including standards of conduct) in implementing, operating, or utilizing OASIS [the Open Access Same-Time Information System used to book and schedule transmission service on BC Hydro’s WTS Tariff.

“...So that the Commission’s wishes in this regard are unambiguous, the Commission directs BC Hydro to comply with the current Standards and Communication Protocols for Open Access Same Time Information Systems as may be issued by FERC from time to time except where to do so is patently unreasonable.”

- The Government's decision to break up BC Hydro, in the process losing the economies, synergies and other advantages of a vertically integrated, single supplier of electricity;
- The impact on BC Hydro of providing – and absorbing the costs of - a wide range of new market based services to private IPPs and marketers as part of the introduction of a competitive energy market;
- The cost of new infrastructure investments to support access to, and use of, B.C.'s public transmission system by IPPs and energy marketers;
- The \$17.5 million in start up costs to establish the BC Transmission Corporation to manage BC's transmission system and the estimated additional \$17.8 million annual additional costs to operate it – costs not needed if BC Hydro were kept as an integrated utility;<sup>11</sup>
- The costs – and potential future liabilities – associated with supporting a process, through RTO West, to create an integrated electricity market throughout the Pacific northwest – a process that may result in significant policy decisions – and their costs - being determined by parties not responsible to the citizens of B.C.;
- The costs of restructuring and privatizing key administrative functions to Accenture.

B.C.'s public electricity system is being radically transformed by the provincial government. This restructuring is not being done primarily to make BC Hydro more efficient as a vertically integrated utility whose primary purpose is to serve the needs the citizens of B.C., or to guarantee that prices for customers will be kept down in the future through a rate structure based on the average cost of publicly generated electricity. Rather, it is being done to create a new, competitive energy market in which private generators and marketers will be given a much larger role at the expense of BC Hydro.

The outcome of the restructuring process will be the elimination, over the next decade, of many of the advantages currently enjoyed by the public as a result of its investment in BC Hydro. Our system of cost-based publicly owned electricity, which has given us the third lowest priced electrical energy in North America, will be gradually phased out so that private interests can profit from the generation and sale of electricity at market prices in B.C. and in export markets.

---

<sup>11</sup> In response to our request on the costs of establishing the BCTC (including its additional functions) BC Hydro indicated that it spent \$5.5 million in 2001 for WTS tariff development and administration, an additional \$12 million in capital investment in 2002 for settlements and billing, scheduling and dispatch and compliance and monitoring capabilities. This is the source of the \$17.5 million figure. The ongoing \$17.8 number was also provided in response to the same request. (These numbers do not include the costs of RTO participation or the \$1.5 million annual cost associated with the 2002 settlements and billing investments)

---

As a vertically integrated utility, BC Hydro has enjoyed many advantages that, cumulatively, have resulted in keeping costs down and allowing the corporation to maintain very high standards of reliability and service to all areas of the province.

Additionally, as a vertically integrated utility, BC Hydro has been sufficiently large to benefit from major economies of scale in planning, administration, personnel management, training, engineering, customer service and other areas of its operations. The fragmentation of the corporation is gradually undermining these benefits. For example, key elements of the company's 'intellectual capital', namely the skills and expertise of its workforce, have been transferred out of BC Hydro as part of the contracting out arrangement with Accenture.

BC Hydro has also benefited from the advantages of being able to operate its hydro-based system in an integrated manner. Historically, public ownership and control of the transmission system meant that investments in the grid and related control systems were made to leverage the maximum benefit to BC Hydro (and the Province) from its generation, transmission and storage facilities.

As a vertically integrated utility, BC Hydro was also able to plan the timing and the amount of its investments based on projected provincial energy needs and the fact that it was a single supplier of electricity.<sup>12</sup> The creation of a new electricity market is introducing new variables – and new risks – that are beyond the control of BC Hydro. It may also result in BC Hydro making major investments to meet potential needs of private parties located inside and outside the province, without assurance that the investments will be fully utilized.

While BC Hydro and the BC Transmission Corporation are still planning to make certain investments for its own benefit, a growing share of its new investments are designed primarily to give private interests access to its grid for electricity trading activities. Such investments are being made to give IPPs the opportunity to connect their new private generation facilities to the existing transmission system, either for sale to BC Hydro (or other customers within B.C.) or to export it to other jurisdictions.

The move to an electricity market also means that the price of energy will no longer be directly connected to the cost of production. Consequently, the future costs of acquiring electricity for BC Hydro and its customers (given the constraints it is now required to operate under) are far less predictable.

---

<sup>12</sup> The exception is the area formerly serviced by privately-owned West Kootenay Power which, until the mid-1990s, was the single supplier in that area of the Province.

---

Similarly, the introduction of third parties who are not ultimately responsible for the supply of electricity to the people of B.C. makes planning of future transmission capacity (and the use of the transmission system) more complex. And, the anticipated future shift to market rates poses significant cost uncertainties for BC customers and the provincial government – a problem that will grow as the share of market priced electricity increases over time.

Shifting to an electricity market greatly increases transaction costs. We cautioned against the proposals of the BC Task Force on Energy Policy which recommended establishment of an independent transmission entity for this reason. At the time we quoted Dr. Mark N. Cooper of the Consumer Federation of America (August 2001), who said the following:

*“Introducing competition into retail transactions not only undermines the base for long term utility financing, but also weakens the base for coordination and integration of supply and demand...Creation of markets for electricity services leads to a huge growth in transactions and retards co-operation in the industry.”*  
(p. 12)

Our concern is that the enormous increase in transactions in the system requires significant new investments in a number of critical areas – investments which are required only because of the decision to open up the energy market and support an increasing role for IPPs and power marketers. The fact is that BC Hydro – and the citizens of BC – are paying the costs of this investment which is not needed to maintain its traditional servicing arrangements, but rather is required to allow the many new market participants access to the transmission and distribution systems. The BCUC should not force ratepayers to finance this expenditure.

### **BC Hydro Dividend to Government**

The Province is making BC Hydro and its customers bear the costs of the restructuring agenda it has initiated. We do not think this is fair or justified. Because a number of the cost increases now facing BC Hydro and BCTC are a direct result of the province’s policies, we believe the province should accept responsibility for the financial costs by reducing its dividend (i.e. lowering the rate of return expected from BC Hydro and BCTC).

If the Province wants to spend money on creating the infrastructure to implement a new electricity market structure, it is appropriate that the Province, not customers of BC Hydro pay for the costs of this restructuring. Reducing the dividend requested would address this issue.

### **The Costs of Providing New Services to IPPs**

A number of the cost items identified in the submission involve new investments to provide IPPs with better access to the current BC Hydro system. Some of these involve new transmission investments. Some involve new financial security arrangements to protect the Province from credit and other problems arising from the financial side of market transactions by third parties, many of whom may not be located within the Province. Some involve new investments to facilitate the further development and operation of an open electricity market in B.C.

We believe that these costs are being incurred to enable BC Transmission Corporation to handle the much more complex management system that is required to accommodate the anticipated increase of large numbers of new participants in the B.C. electricity market – a system that would not be needed if BC Hydro were to remain a vertically integrated utility.

While these investments may be beneficial to the private interests that want such a market, our concern is that they are being funded by ratepayers through BC Hydro, with no commensurate benefit to the public or customers in B.C.

### **The Costs of Contracting Out Administrative Services to Accenture**

As the BCUC is aware, BC Hydro has entered into a 10 year, \$1.28 billion contract with the Bermuda-based Accenture Business Services (ABS) corporation, formerly known as Andersen Consulting. The contract is to provide what are described as ‘back office services’ (Revenue Submission vol. 1 p.1-18). Significantly, Accenture will also provide similar services to the newly formed BC Transmission Corporation and to two subsidiaries of BC Hydro, Powerex and Powertech Labs Inc.

According to the Revenue submission, *“The ABS contract represents a total minimum aggregate spend, over the 10 year period, of \$1,282 million (nominal dollars). Total savings to BC Hydro over this term are determined through several specific one-time and recurring benefits and costs.”*(Vol. 1, Ch 9, p. 63)

The submission also makes the following claim:

*“As discussed above, the total net present value of this transaction is estimated to be \$110.4 million, based on a discount rate of 8% over the term of the contract. From an*

---

*accounting perspective, BC Hydro's annual net income is expected to improve each year throughout the length of the contract, starting with a positive contribution to net income of \$2 million in F2004 and increasing to a contribution of \$40 million in F2013. During the test periods, the positive contributions to net income are \$8 million and \$12 million respectively. As a result of these benefits, BC Hydro's rates will be roughly 1.5% lower in F2013 than if these functions remained within BC Hydro and service and expenditure patterns were maintained at F2003 levels." (Vol. 1, Ch 9, p. 64)*

What is striking about this claim is how far into the future the anticipated gains have been pushed. It would appear from this quotation that \$40 million (or 36%) of the claimed benefits will occur in the last year of the 10 year contract. Given the numerous variables that can impact on the contract over this period, it seems odd that over a third of the projected benefit does not occur until the final year of the contract.

We are concerned that this contract was arranged with very little public scrutiny and debate. The rationale for making such a major change in BC Hydro's organizational structure never been satisfactorily explained. Nor has the rush to put it into place so quickly, a truncated process that contrasts sharply with many other public policy decisions which involve lengthy evaluations and comprehensive due diligence. Many of the details of the contract have still not been made public, a policy justified on the basis of the need to maintain 'commercial confidentiality'. The entire process has lacked transparency and effectively excluded the public. For example, in BC Hydro's document that provided the business case to pursue the Accenture deal, key comparisons and financial data are blacked out.

Moreover, the long term nature of the contract appears to be designed to preclude a future provincial government from re-evaluating the deal and determining whether to continue with it or bring these services back 'in house'. This may protect the shareholders of Accenture, but we are not persuaded that it protects the interests of the public.

BC Hydro has claimed significant future savings from its 10 year deal with Accenture. However, it has included very little documentation to support this claim in the material it has provided to the BCUC or in response to our questions. While it mentions the anticipated savings, compared with what it says would have been the costs for in-house provision of the services, where so many variables in this arrangement that it will be almost impossible in a few years time for the public to compare the costs of the Accenture contract with what it would have cost if BC Hydro had continued with the services on an 'in house' basis. Moreover, given the ongoing – and major – reorganizations that have been taking place, such as the creation of the BC Transmission Corporation, it is difficult to see how the public will be able to confirm any of the claims regarding cost savings in the future.

We are concerned that this massive contracting out of over one third of the workforce – and their skills, expertise, knowledge and corporate history - will have significant negative impacts on the overall operation of BC Hydro. It establishes different lines of authority for this group of employees. They will be responsible not to the public of BC (through BC Hydro) but rather to the owners of Accenture. This means that their primary duty will be to ensure that the shareholders of Accenture maximize the return on their investment. It is our view that co-ordination between Accenture employees and the employees of BC Hydro will be a major issue, because there are now two parallel lines of authority. Synergies will be lost. Information that would readily flow between BC Hydro employees may be screened to protect the commercial interests of Accenture. And the fact of two organizations co-habiting within the operations of BC Hydro will itself exercise a chilling effect on the flow of information.

Naturally, companies like Accenture are dedicated to maximizing the returns to their shareholders. They expect to make a profit. However, this raises the question of where the money to pay for the profit will come from. Will it arise from major reductions in future staffing levels? Will it arise from skimping on the services that are provided to BC Hydro? Or will it come from some combination of the two?

As an intervenor, we asked BC Hydro to provide us with additional details of the Accenture contract in a number of areas. For example we asked what guarantees BC Hydro had negotiated to ensure that jobs would remain in B.C. BC Hydro indicated that Accenture has made a commitment to keeping jobs dedicated to BC Hydro work in the province. However, it appears that the contract does not specify a number of jobs that will be kept in B.C., but only that jobs providing service to BC Hydro will be kept in the province. Moreover, given that Accenture may have other business activities, and that it can always argue that due to the efficiencies it has implemented, it requires fewer workers to do BC Hydro's work, determining whether, or not, jobs have left the province will be extremely difficult.

This submission for a revenue increase would have been a suitable time for BC Hydro to open the books on the Accenture deal and provide answers to the many questions raised by members of the public since its announcement. Regrettably this has not occurred. Instead, BC Hydro continues to maintain a veil of secrecy concerning many of the key terms of the contract. It contends that the confidentiality clauses in the contract preclude detailed public scrutiny of the deal. And it remains committed to the argument that commercial confidentiality overrides the right of the public to know what is being done in its name. Far from being an example of open, transparent governance, the Accenture deal is effectively denying citizens their Access to Information rights – rights which existed when BC Hydro provided the same services 'in-house'.

Finally we would note that once the contract has been in place for a number of years, BC Hydro will have lost the intellectual capital that it once had from the employees that have been transferred to Accenture. As a result, the utility will be very dependent on Accenture for these services. It will not be in a position to outsource to other operators, because of the barriers to entry associated with establishing an operation with almost 2000 employees specialized in service to BC Hydro. In other words, it will effectively have no choice but to continue with the contract.

If it chooses to cancel the contract, how will BC Hydro be able to acquire the skills and knowledge of the workforce that it requires? How could BC Hydro recruit and train this large number of workers in a reasonable period of time to enable it to continue to provide a seamless delivery of services to the people of the province? All these are significant questions which we believe point to the questionable nature of this contract. A rate increase to finance the restructuring costs of the Accenture contract with BC Hydro is inappropriate and unfair to BC Hydro's customers.

### **The Costs of Establishing and Operating the New BC Transmission Corporation**

As noted above, the rationale for establishing a separate transmission corporation is to facilitate the opening up of a competitive electricity market in B.C. The 1998 BCUC directive regarding OASIS has been interpreted very broadly by BC Hydro and BCTC – much more broadly than we believe is actually required. Nevertheless, the decision to voluntarily adopt some of the more recent FERC directives to U.S. utilities, has created the need to make major new investments in transmission and distribution infrastructure to accommodate the key elements of FERC's Standard Market Design (SMD) model.

We noted earlier in this submission the capital costs and the projected ongoing operating costs for this new corporation. We do not believe that BC Hydro ratepayers should be carrying these costs. Moreover, despite the significant costs to the public system, revenues from private users of the system have been exceedingly modest.

According to a table provided to us in response to one of our questions, BC Hydro received \$6.7 million in fees under the WTS in 2003, \$9.5 million in 2004 and an anticipated \$12.7 million in 2005. We note that these are funds paid to BC Hydro (or BCTC) for ongoing services rendered on behalf of these customers. As far as we are aware, they are not being used to compensate BC Hydro for the significant investments it made in previous years in the new infrastructure needed to expand the electricity market in B.C.

The separation of transmission from generation and the establishment of a separate new company to operate the transmission system are not needed for BC Hydro to provide electricity to the citizens of B.C. nor to export electricity to the United States. It already has the capacity to do this. Manitoba, for example, continues to export power to the U.S. without incurring the costs of establishing a whole new corporate structure. B.C. ratepayers are not well served by this restructuring and should not be required to finance it.

In addition, we note that many public utilities in the U.S. have expressed opposition to the direction in which FERC is pushing utilities south of the border. These utilities have been energetically lobbying their state legislators, the U.S. Congress and various parts of the US Executive to restrain FERC.

All of this raises the question of why we are pursuing policies that will further integrate us into a continental energy market when BC Hydro claims we are in no way obligated to do so. In response to a question from us on whether BC Hydro had any legal opinions indicating that it was required to follow the directives of FERC, we were told the following:

*“As a United States Regulatory Body, FERC has no jurisdiction in B.C. Instead, BC Hydro and BCTC are obligated to follow the provisions of FERC Orders and policies only to the extent that these are consistent with tariffs approved and orders issued by the BCUC.*

*In its 1998 Wholesale Transmission Services (WTS) Decision, the BCUC approved BC Hydro’s application for a FERC Order 888-type tariff. At the time, adoption of this type of tariff was judged by the BCUC to be in the best interest of British Columbia ratepayers. The BCUC’s decision followed evidence led by BC Hydro demonstrating a clear link between continued trade benefits (which act as an offset to the domestic revenue requirement) and the adoption in BC of an Order 888-type tariff.*

In the same decision, the BCUC ordered BC Hydro:

*“...to follow North American industry standard terms and conditions (including those prescribed for US electricity utilities by the FERC) and Commission requirements (including standards of conduct) in implementing, operating, or utilizing OASIS [the Open Access Same-Time Information System used to book and schedule transmission service on BC Hydro’s WTS tariff].”*

The BCUC went on to say:

*“So that the Commission’s wishes in this regard are unambiguous, the Commission directs BC Hydro to comply with the current Standards and Communication Protocols for Open Access Same-Time Information Systems as may be issued by FERC from time to time except where to do so is patently unreasonable.”* (Reference A16.0 of BC Hydro’s response to request for information from Citizen’s for Public Power)

It seems that BC Hydro is interpreting these rulings to mean that the BCUC requires it to adopt FERC policies that were not even developed in 1998 when the BCUC directive was made. While, the language of this directive might be interpreted in different ways, we do not feel that the BCUC would direct a provincial Crown corporation to adopt future standards developed in another jurisdiction without even assessing what their impact might be on our electricity system in B.C.

We also question BC Hydro’s claim that the changes it has implemented have no impact on rates. In its submission, BC Hydro argues that *“The initial and most expensive steps in the large restructuring BC Hydro has undertaken will be complete in F2004. These steps have had no effect on rates.”* (vol. 1, p. 1-22). To say that the costs have ‘had no effect on rates’ thus far is not the same thing as saying they have had no financial impact on BC Hydro or that they will not impact on rates in the future. According to Table 2.2, restructuring costs have amounted to \$37 million in fiscal 2003 and another \$11 million in 2004.

A number of the costs associated with establishing the new BC Transmission Corporation are specifically identified in BC Hydro’s revenue application, including start up capital of \$20 million and the need for new insurance type accounts to deal with the new risks brought by the introduction of the market. These risks include reliability, security of supply and credit concerns. Expenditures on these new items are needed as part of the process of establishing the new electricity market.

In its revenue submission, BC Hydro indicated that one of the major cost drivers for the transmission system was the:

*“increasing complexity of transmission services. When the WTS tariff was introduced, wholesale access was managed as an adjunct to standard utility transmission service. The wholesale transmission business is now more complex and demanding as a result of the significantly higher volume and complexity of trade. Computer systems have required major upgrades to respond to Commission requirements, market demands for wholesale transmission service,*

*and to provide timely billing, settlement and audit services. Professional staff are required to administer tariff operations and respond to customers.” (vol. 1 Chapter 6, p. 4)*

BC Hydro goes on to note \$17.8 million of ‘incremental transmission costs that are included in the rates for 2005’. In response to our next question on the same issue, BC Hydro did provide some additional information as follows:

*“In F2001, BC Hydro expanded its scheduling capabilities and technical support to address the increasing volume and complexity of work and established its WTS tariff development and administration and client services capabilities, at a cost of \$5.5 million.*

*In F2002 BC Hydro implemented the capabilities from the Grid Operations Upgrade Project, a \$27 million initiative that included capital investment of \$12 million for the settlements and billing, scheduling and dispatch and compliance monitoring capabilities. To support these capabilities, \$1.5 million was provided for additional staff, technology support and license fees.*

*In F2004, as part of the establishment of BCTC incremental ongoing funding of \$17.8 million has been provided to cover the costs associated with an independent business entity, including regulatory costs.” (Reference A7.0 of BC Hydro’s response to request for information from Citizen’s for Public Power)*

BC Hydro also notes that it has been spending funds in support of the development of RTO West, amounting to \$2 million in F2002 and another \$0.5 million in F2003. Further on in its revenue requirement submission, BC Hydro notes the following:

*“The third change in the transmission cost structure is the establishment of BCTC. BCTC is built upon BC Hydro’s former transmission line of business. However, as an independent utility, it faces a number of costs that were not part of BC Hydro transmission’s cost structure within a vertically integrated utility.” (Vol. 1, Chapter 6, p. 4)*

Following up on this statement, we asked how much of the additional costs have been paid for by new users of the system and how much by BC Hydro. The following answer was provided:

*Transmission costs are not allocated between new users of the system and BC Hydro. The transmission costs, net of recoveries, are included in the transmission revenue requirement and go toward determining the rates that are charged to all*

---

*users of the transmission system. To the extent that these costs have been incurred during the period following the most recent setting of transmission rates, BC Hydro has borne these costs.” (Reference A8.0 of BC Hydro’s response to request for information from Citizen’s for Public Power)*

This clarifies what is perhaps the most important issue is the way in which new transmission investment will be funded. The BC Transmission Corporation will build the costs into the fees users pay for accessing the system. On the surface, this looks like a fair approach. Everyone will pay equally for the use they make of the system. However, the practical impact of this arrangement is that BC Hydro will be shouldering virtually all of the costs in the short and medium term because it is – and will continue to be for a considerable time into the future – the dominant user of the system.

So effectively, BC Hydro will be paying transmission charges to fund major new investments in the transmission system that it does not need and whose benefits are going almost entirely to private IPPs, energy marketers and other out-of-province utilities. Moreover, given the Province’s desire to expand private production of power, this will mean that new transmission capacity will be built specifically to accommodate the required hook-ups of new private generation facilities to the system and to make transmission upgrades to facilitate export of privately generated electricity to the US or Alberta border.

According to BC Hydro’s revenue requirement submission, (Vol 1., Table 6-17) investments for new transmission capacity are projected to be \$7 million in F2004, \$8 million in F2005 and \$24 million in F2006. These escalating costs reflect the growing amount of privately produced electricity that BC Hydro anticipates it will need to purchase from IPPs in the years indicated. While the information provided does not go beyond F2006, we assume that major transmission investments will continue to be required as the number of IPP contracts (and new generation facilities) increases in future years.

Aside from the costs of investments in the transmission system to accommodate IPP generators, the costs of operating a new electricity market in BC will be paid for by the users of the system, which means that BC Hydro will pay the lion’s share of these costs. This is because it is – and will continue to be – the major user of the system. However, the purpose of this market is not to support BC Hydro, but rather to provide new opportunities for the private sector.

Finally, it is by no means clear that BC Hydro – and the public – who own the transmission system in the Province will receive adequate compensation from private interests for the use they make of the transmission system. If the fees charged are based

on historic costs of constructing the system, rather than current replacement costs, the result will be to give private interests a major price subsidy – through cheap access to the system – in addition to all the other direct and indirect subsidies they are receiving through Power Smart, long term IPP contracts and the like.

In addition to new transmission investments, BCTC has also signaled that it intends to spend \$105 million on “the Definition Phase of its System Control Modernization Project.” However, the details of the very large capital expenditure are not yet available. In its words “... *BCTC has not yet defined fundamental elements of the project, such as the number and sites for new centre(s) and the configuration(s) for each centre.*” Further details will be submitted in its application for a CPCN for the project.

We recognize the need to replace aging centre equipment, some of which, we understand, is over 30 years old. However, without details on the specific items that the money will be spent on, we are not able to evaluate the extent to which this expenditure is focused on upgrades that are needed to modernize BC Hydro’s control system for its own use as opposed to investments which are being made to provide the new infrastructure necessary for the next phases of the emerging electricity market in BC. We are concerned that a part of the control centre expenditure is being proposed primarily for the benefit of private interests (IPPS, marketers, out of province electricity traders and utilities) rather than to strengthen the ability of BC Hydro to serve the electricity needs of residents of BC.

Another issue of concern to us as a result of the establishment of BCTC is the relationship between BC Hydro and BC Transmission Corporation. BC Hydro will be responsible for the physical infrastructure of the transmission grid. BC Transmission Corporation will operate the market system. This division may create several different types of problems and we would like to know how BCTC intends to resolve them.

One potential issue concerns coordination between the staff carrying out repairs and maintenance who work for BC Hydro and the staff operating the transmission system who work for BC Transmission Corporation. It is not clear to us how the safety of repair crews will be protected if their instructions are coming from a different company without an intimate knowledge of the physical conditions under which repairs are being made. This works now because the various staff members were all part of BC Hydro. But over time, and depending on the degree of independence of BCTC, this can change, creating a more significant coordination problem.

Another issue concerns the allocation of costs between BC Hydro and BC Transmission Corporation with respect to investments and maintenance on the transmission and distribution systems. If BC Hydro absorbs costs that should be allocated to the Transmission Corporation, this could result in BCTC charging less than the full

---

transmission costs to private users of the system, such as IPPs. Depending on the cost allocation mechanisms, BC Hydro could end up indirectly subsidizing IPPs by carrying some of the costs of transmission investments and maintenance.

We are not in a position, technically, to determine if the cost allocation process now in place is cost neutral. However, we see this as a significant issue and believe that the BCUC should monitor this very carefully to ensure that the public system is not subsidizing private use of the transmission system.

### **The Cost of Not Permitting BC Hydro to Invest in New Generation**

In its energy plan (*Energy for Our Future: A Plan for BC*), the provincial government has established the policy that new electricity generation will be private. This is clearly stated in Policy Action # 13 which reads: "*The private sector will develop new electricity generation, with BC Hydro restricted to improvements at existing plants.*" This directive effectively prevents BC Hydro from competing with private power producers in the development of new generation facilities within the province.

The most cost effective policy would involve rates based on cost of production rather than purchases from IPPs at market prices. It is one thing to say that private power producers should be allowed to compete with BC Hydro if they can show that they can produce power more cheaply. However, in this application rate payers are being asked to pay for the most expensive option without any comparisons or justification of these costs.

BC Hydro has a wealth of experience and expertise in developing generation facilities. It has highly skilled planning and engineering staff who are fully capable of building new generation in a cost effective and efficient manner. It has a proven track record. And yet the very people who could continue with BC's highly successful investment in public power generation are precluded from being directly involved in the future.

However, given the long life span of hydro-based generation assets, the public is now enjoying the benefits of assets purchased at prices fixed decades ago. It was sound public policy for BC Hydro to acquire assets then, and it remains sound public policy today.

However, if the policy of restricting BC Hydro from building new generation assets is not amended, the next generation of citizens in B.C. will not be in a position to enjoy comparable benefits. Instead, the advantages of asset ownership will accrue entirely to the private, IPP sector. Instead of being able to continue to purchase cost based power, the Government is committing BC residents to pay prices that will continue to rise in line

---

with market trends in the Pacific Northwest, and possibly California. Future price increases will accrue to the private sector at the expense of BC customers.

### **The Potential Future Costs of RTO West Membership**

For some time now, BC Hydro (and more recently, BC Transmission Corporation) has been in negotiations concerning the establishment of a new regional transmission organization (RTO) known as RTO West. The purpose of RTO West is to create a single entity that would oversee key aspects of the operation of all the transmission systems and related energy markets throughout the region.

According to its submission, BC Hydro has spent \$2.2 million in F2001, \$3.3 million in F2002 and \$2.2 in F2003. Anticipated expenditures will drop to \$0.5 million in F2004 but are expected to increase to approximately \$3.0 million for the following years. (Response to Information Request A24.0 from Citizens For Public Power)

In reply to a question we submitted, BCTC said the following regarding its participation in this new entity which we understand will be based on FERC's standard market design (SMD) or something broadly similar:

*“The purpose of the funding provided is to enable RTO West to retain experts and facilitators to further work toward the creation of an RTO. Funding Agreements provide that funding advanced by BC Hydro will be repaid with interest when sufficient third party financing is available to RTO West, and in any event not later than commencement of transmission services by RTO West over the transmission assets of one or more of the funding transmission owners. As at January 31<sup>st</sup>, 2004, the Loan Receivable from RTO West to BC Hydro was CAD \$1,569 million.”*

BCTC also indicated that discussions are currently being held to identify options for participation by the organizations (utility and non-utility) that may become full members of the RTO. It stated that BC Transmission Corporation would not likely join as a full member of RTO West, but rather that *“the relationship between BCTC and RTO West would be in the form of an agreement with respect to operating functions and services.”* (Response A29.0 to request for information from Citizen's for Public Power)

While the answers from BCTC and BC Hydro suggest that the relationship between RTO West and BC's Crown corporations may not involve any transfer of control to this U.S. dominated entity, the status reports on discussions posted on the web site indicate that a tighter form of integration is under consideration. For example, a discussion paper by the

---

RTO West Regional Representatives Group posted on February 3<sup>rd</sup>, 2004 entitled “A Regional Consensus Transmission Proposal” refers repeatedly to the notion of a new, independent, regional ‘Entity’. In the words of the paper:

*“The RTO Regional Representatives Group (RRG) expressed its **unanimous support** for a high-level framework (the “Regional Proposal”) based on the creation of a new independent transmission organization in the region.” (p. 1)<sup>13</sup>*

We recognize that there are significant issues associated with system reliability and system performance/standards that should be dealt with on a region-wide basis to ensure that we do not experience the black outs that have occurred in other jurisdictions such as California and Ontario, to cite only two of the many incidents in recent years.

BC clearly has an interest in ensuring that problems occurring in other jurisdictions do not cascade into this province. High standards of system reliability and performance are in everyone’s interest and it is appropriate for BCTC to have ongoing discussions – and agreements - with the utilities to which it is interconnected.

However, we have questions concerning how another set of priorities – those establishing and regulating a financial market in electricity trading – is also being incorporated into the concept of the proposed RTO West. We are concerned that full RTO membership – or even a contractual relationship, depending on its wording - would be a very significant further step to the full integration of BC Hydro’s transmission grid with that of the other utilities in the Pacific Northwest.

Although there are ambiguities in the latest RTO West transmission discussion documents, what strikes us in reviewing them is the emphasis being placed on the concept, noted above, of a “Regional Entity” and the powers that this entity might eventually come to exercise. Moreover, the document makes clear that the project involves a step by step process towards greater integration. Here is how it envisages this process:

- *The beginning phase calls for changes that are intended to be significant improvements over current practices. Its objective is to respond specifically to many of the important regional transmission problems and opportunities identified and agreed-upon in this process.*

---

<sup>13</sup> RTO Regional Representatives Group, “A Regional Consensus Transmission Proposal: Background and Overview” Posted February 3, 2004. p.1. (from web site of RTO West)

- *The Regional Proposal contemplates that each new phase in the evolution of the Independent Entity should be workable in and of itself and should address remaining transmission problems that were not solved in the earlier phases, but without creating significant new problems by moving forward.*
- *The Regional Proposal is intended to create a path to an advanced target state where the region efficiently manages its transmission system by using financial methods subject to reliability constraints. Each phase along the path will evolve based on experience and circumstances at the time the changes are to be made, subject to a clear set of checks and balances to assure that the region has input about whether changes serve the region's interests.*
- *The Regional Proposal allows for an early voluntary consolidation of utility control areas (key centers for transmission system operations) into a single control area operated by the Independent Entity.<sup>14</sup> This approach is intended to provide each transmission owner the flexibility to make its own decision on consolidating its control area based on its needs and the experience of other consolidated control areas, rather than mandating consolidation as a prerequisite for joining the Independent Entity. (p. 3)*

Currently there are four 'work groups' looking at issues associated with the Regional Proposal for Transmission Services. These are: the Liaison Group (with core technical staff), Articles and Bylaws Group, Facilities Group and Pricing Group. Discussions are also being held with respect to the structure of RTO west, including the size of the Board, the categories of members to be represented, voting arrangements and so forth. While these matters are not yet complete, they indicate the scope and the direction of the planning process now underway.

In a footnote in the discussion paper, the authors indicate how they see Canada's participation in this evolving project:

*“the manner in which an independent transmission operator based in Canada would participate in early, voluntary control area consolidation is expected to follow the approach developed for the Stage 2 RTO West Transmission Operating Agreement. This approach contemplates agreements that would enable the Independent Entity and the Canadian independent operator to operate transmission facilities under their respective control as a single NERC-certified*

*control area. (These agreements could preserve, if desired, the ability of the Independent Entity or the Canadian independent operator to resume independent operation of its transmission facilities under emergency conditions.) The guiding principles are to (1) achieve the benefits of a single control area operation, (2) maintain consistency with orders of applicable regulatory authorities in the United States and Canada, and (3) provide a market structure with seamless, non-discriminatory open access transmission services across the facilities of the Independent Entity and the Canadian independent operator” (Footnote #2)*

We note, in particular, the final principle cited above, namely to “provide a market structure with seamless, non-discriminatory open access transmission services...” This suggests a high degree of integration with the US based system as defined by FERC.

When fully implemented, RTO West’s mandate could require BC to cede responsibility for determining a wide range of decisions about the operation of BC’s transmission grid and the functioning of BC’s electricity market. We are concerned that RTO West’s decisions will be based on “regional needs” as it defines them (which means predominantly the needs of US utilities, energy companies and marketers), rather than the needs of the public in BC. This is reinforced when we look at the membership of RTO West which includes numerous private sector entities.

We are not the only ones to express concerns about this approach. The Alliance of State Leaders Protecting Electricity Consumers has made the following criticism about FERC’s restructuring proposals:

*“Utilities must turn over all transmission assets to an “independent transmission provider” regulated by FERC. Utilities and state and local regulators would lose their ability to ensure that firm retail loads are served reliably. Utilities must compete for access to transmission that was built to serve their customers’ needs, reducing reliability, increasing cost, and possibly discouraging utilities from investing in new transmission. Extremely complex day-ahead and real-time and auction markets are unnecessary and overly expensive in many parts of the US. No competitive model for the wholesale market has yet been proven to work, especially when supplies are tight.”<sup>15</sup>*

The Alliance goes on to argue that FERC’s model “... creates numerous new gaming opportunities for parties that can monopolize new energy and transmission markets”<sup>16</sup>

---

<sup>15</sup> Alliance of State Leaders Protecting Electricity Consumers. From their web site [www.protectpowerconsumers.org](http://www.protectpowerconsumers.org). April 18, 2004 The alliance is a coalition of more than 50 state utility regulators and other public officials from 18 states advocating on behalf of America’s electricity ratepayers. See Appendix C.

<sup>16</sup> Ibid. same web site

And, it argues that basing utility capital investments on short term market prices is a fundamentally flawed approach to building new generation, given the risky nature of current power markets. (See Appendix C for further comment by the Alliance of State Leaders.)

As noted earlier, in response to a question we posed on this matter, BCTC replied that it would not likely become a member of RTO West, but rather would deal with it on the basis of contractual arrangements. This may be what eventually transpires, although both BCTC and the BCUC are among the entities listed in the group that drafted the “unanimous support” for the draft proposal cited above. However, even if BCTC did not become a full member, it could still contract with RTO West in a manner that required it to adopt policies similar to those of full members.

Whether through contract, voluntary agreement, membership, or “participation” in RTO West, the establishment of transmission market structures may not be favourable to B.C. customers.

We are seeking assurances from the BCUC and BC Transmission Corporation that the basis of its cooperation with the utilities involved in RTO West will be to maintain transmission system standards and security, but not to become part of an integrated RTO that effectively controls and manages a region wide electricity market.

## **Conclusion**

While we are not opposed in principle to additional revenue to BC Hydro, this brief argues that the current application should be rejected. BC Hydro and the BCTC are applying to the BCUC to approve an increase in rates to finance a number of expensive initiatives which provide questionable value, if any, to ratepayers. Ratepayers should not be forced to fund decisions that incur unnecessarily high costs when other lower cost options are available.

Therefore, we recommend that the BCUC do the following:

1. Direct BC Hydro to review the entire Power Smart program given that BC Hydro is no longer operating as a single supplier of electricity and, therefore, that the basic premise of the earlier Power Smart program – namely, ‘capturing’ the benefits of investments in energy conservation - is no longer valid;
2. Direct BC Hydro and BCTC to review the methodology used to determine the allocation of costs when new IPPs are added to the transmission system, to ensure

- that the public utilities are not subsidizing these private interests through under-charging for access;
3. Recommend to the government that its dividend be reduced to compensate for the additional costs now being borne by BC Hydro as a result of provincial legislation and policy;
  4. Direct BC Hydro and BC Transmission Corporation to develop a new proposal that prioritizes transmission arrangements which protect ratepayers' interests;
  5. Order the BC Transmission Corporation to limit its involvement in RTO West and resist pressure from the US to integrate our transmission system into the new regional "Entity" that is being established to facilitate creation of a single, seamless open electricity market;
  6. Direct BC Hydro to provide additional information concerning the 10- year agreement with Accenture Business Services (ABS);
  7. Clarify the BCUC's intention in its 1998 directive to BC Hydro (and now BC Transmission Corporation) that requires them to comply with FERC Order 888 and future FERC Orders;
  8. Direct BC Hydro to provide additional information about the contracts it has with IPPs, including information on the name of the company involved, the duration of the contract, how much BC Hydro is paying for the electricity, the net present value of the commitment BC Hydro has made in the contract, and the options available to BC Hydro when the contract expires;
  9. Direct BC Hydro to indicate clearly on its electricity bills the respective costs of publicly generated power and privately purchased power.

## Appendix A



THE POWER IS YOURS

Office of the President and  
Chief Executive Officer

**FAXED**  
18/3/99

March 18, 1999

Honourable Mike Farnworth  
Minister of Employment and Investment  
and Minister Responsible for BC Hydro  
PO Box 9046, Stn Prov Govt  
Victoria, BC  
V9W 9E2

Dear Minister:

The purpose of this letter is to request, on behalf of the Board of BC Hydro, that the province review and update the current IPP policy. Our rationale for the review, as well as our recommendation supported by the BC Hydro Board, is "to allow BC Hydro to take the lead in future generation investments in partnership with the private sector, where appropriate."

The current policy is based on the IPP Policy Statement issued by the province in October of 1992. This policy requires that BC Hydro provide an opportunity for private sector participation in satisfying BC Hydro's projected generation requirements through submission of IPP project bids under a Request for Proposal (RFP) process. BC Hydro believes that the scope of this policy is too narrow, since it places BC Hydro primarily in the role of a buyer of electricity and IPP's in the role of builder and owner of generation projects.

A review of BC Hydro's IPP acquisitions to date indicates that the effect of limiting BC Hydro's role to that of a buyer has resulted in:

- social or financial benefits to the province, BC Hydro and the ratepayers not being maximized;
- IPP's enjoying the benefits of project ownership, while many or all of the significant risks of ownership are passed to BC Hydro;
- inflexible arrangements with IPP's which reduces the ability to maximize the efficiency of our system;
- IPP profits and value-added jobs often leaving the province;
- IPP projects usually being fully paid off by the end of the EPA term, thus leaving a debt-free project with ten (in the case of thermal projects) or thirty (in the case of hydro projects) or more years of economic life left, in which further revenues can be generated by the owners without any sharing occurring with BC Hydro and its ratepayers.

British Columbia Hydro and Power Authority, 333 Dunsmuir Street, Vancouver, B.C. V6B 5R3  
Telephone (604) 623-4490 Fax (604) 623-3901

BC Hydro also believes that requiring proposal calls for all future IPP additions is excessively costly and cumbersome, particularly in the few cases where small commercially viable projects exist and the IPP developer has invested significant time and risk capital to bring such projects to a stage where all licences and approvals are in place and negotiations on an EPA are ready to commence.

BC Hydro would like to work with government to update the policy so that the economic development benefits of specific project alternatives to meet BC Hydro's needs in the future are maximized for the province and BC Hydro's ratepayers. BC Hydro's recommended approach for acquiring additional resources to meet its needs is to proactively seek out new commercially viable generation opportunities. These opportunities should either be developed by BC Hydro itself, or in partnership with the private sector. BC Hydro would share in the upside and would have the ability to maximize B.C. economic development and job creation.

The partnerships with the private sector can bring expertise to such opportunities from which BC Hydro and its ratepayers can benefit. The joint partnership approach (as in the case of Fort Nelson with TransAlta) has the added advantage of sharing costs and risks, optimization of financial structures, and it is not monopolistic in that such approach provides joint private and public participation in energy resources of the province.

Within the context of the above approach, BC Hydro would be careful to develop any project participation structures to maximize their commercial attractiveness while being mindful of the projects risks, and to adequately address any control, oversight and governance issues from the shareholder and regulatory perspectives. Co-venturing will allow BC Hydro internal resources to develop the skills, knowledge, expertise and capability to develop projects rapidly and efficiently. After concentrating efforts on projects within B.C. and acquiring the necessary expertise, BC Hydro would eventually be in a position to seek similar profitable development opportunities outside B.C.

The electricity industry and market in North America has undergone dramatic changes since the current IPP policy was implemented. Utilities and other energy providers are no longer entering into long-term, fixed-price contracts, while at the same time shouldering the risks of ownership and none of the upside.

3

BC Hydro Board and management are strongly of the view that the policy needs change. With this in mind, BC Hydro staff are fully prepared to work with your staff to make this change. BC Hydro's key contact will be Mr. Kelly Lail at (604) 528-7838, Manager of our Resource Management Group.

Thank you for your attention to this issue. We look forward to your reply.

Yours very truly,



Michael Costello  
President and  
Chief Executive Officer

c: Brian R.D. Smith, Chair  
Blair Trousdell  
Kelly Lail

## Appendix B

### The Heritage Contract

The government has made a major issue of the Heritage Contract, claiming that this provides a guarantee of the benefits of BC's low cost public power for the future. We commented extensively in our earlier submission on this issue and will, therefore, only highlight our concerns in this submission.

The Heritage Contract does not provide any better protection to customers than what was already in place. The government has always had the capacity to ensure that the public benefited from the cheap public power generated by BC Hydro. After all the public, that is the citizens of BC, already own BC Hydro. They don't need to be protected from themselves. Moreover, any future government can enact legislation that changes this arrangement in any event. The legislation does not – indeed cannot - preclude a future government from using its statutory authority to make whatever changes it sees fit. Perhaps more significantly, the Heritage Rate legislation does not protect the public from ever increasing price hikes that the Government has committed BC Hydro to implementing as a result of its decision that all future new generation will be carried out by private interests.

Aside from providing no protection to the public from escalating prices, the Heritage Rate legislation has a sunset clause. It is to be reviewed in 10 years time. The legislation provides no guarantee, beyond this time, that BC Hydro will continue to provide low cost public power to its customers.

## Appendix C

### Summary of Alliance's Concerns with FERC'S Proposed Standard Market Design (SMD) as published on [www.protectpowerconsumers.org](http://www.protectpowerconsumers.org) April 20, 2004

#### **Forces all electric utilities throughout the US into a risky restructuring experiment**

Utilities must turn over all transmission assets to an “independent transmission provider” regulated by FERC. Utilities and state and local regulators would lose their ability to ensure that firm retail loads are served reliably. Utilities must compete for access to transmission that was built to serve their customers’ needs, reducing reliability, increasing cost, and possibly discouraging utilities from investing in new transmission. Extremely complex day-ahead and real-time and auction markets are unnecessary and overly expensive in many parts of the US. No competitive model for the wholesale market has yet been proven to work, especially when supplies are tight.

#### **Creates new problems with market power**

FERC’s approach creates numerous new gaming opportunities for parties that can monopolize new energy and transmission markets.

#### **Exposes consumers to volatile “boom and bust” cycles of generation investment**

Utilities and regulators are generally expected to rely on “independent power producers” or “merchant generation” to meet new resource needs. The all-merchant-plant approach relies on the notion that new plants will be built when justified by short term market prices. Unfortunately, we have seen that this approach does not ensure new capacity is built in advance of dire need. Also, the market capitalization of merchant generators has fallen 86 percent in the last fourteen months, and many merchant power plants have been cancelled. The financial resources of utilities may be needed to get new capacity built, but FERC proposed rules create serious financial risks for utilities contemplating such commitments.

### **Shifts many elements of retail rate-setting from states to FERC**

Under current law, all retail electric rates (and terms and conditions of service) are set by state regulators under state law. Many components of retail rates (new generation, new transmission, treatment of demand-side bidding) are shifted entirely to FERC, which either means pre-emption of state authority or conflict that leads to investment paralysis.

### **Undermines new utility resource investments**

Numerous features of SMD create cost recovery uncertainties for traditional utility investments in new supply, energy efficiency, and transmission. In each case, utilities may be required by FERC to take actions that are in conflict with state and local regulations and statutes. Those conflicts and uncertainties are more likely to lead to under-investment.

**ALLIANCE STATEMENT TO CONGRESS  
OPPOSING EXPANSION OF FERC AUTHORITY  
(Sept 16, 2002)**

Electricity is an essential service that is critically important to our economy and to the citizens and businesses in our states. Over the past decade, changing regulations and failed efforts to deregulate electricity service in some areas of the country have undermined the reliability of electricity service, the ability for utility regulators to ensure that consumers have affordable power, the stability of our electricity rates, and the investment climate for utilities and others to build needed generation and transmission in those regions.

We urge Congress to avoid actions that would further destabilize this critical industry and put consumers at risk. Federal policy should respect the decisions of the majority of states and municipalities, which have chosen not to deregulate electricity service. Those jurisdictions continue to have affordable, reliable electric service. Federal policy should preserve the full ability of states and municipalities to oversee reliable and reasonably priced electricity service to retail customers. Federal policy should protect consumers. The Standard Market Design rules proposed by the Federal Energy Regulatory Commission (FERC) run counter to these objectives.

We urge Congress *not to* include in the pending Omnibus Energy Bill any provision that expands the authority of the FERC to interfere with the ability of states and municipalities to preserve their chosen electricity service policies. Instead, we urge Congress to clarify that the authority of the FERC *does not* extend to impairing the ability of state or local government to regulate any component part of a fully bundled retail sale of electricity, or the siting of generation and transmission, that is subject to state or other local government regulation.

### **Resume of Dr. John Calvert**

John Calvert is currently an Adjunct Professor at Simon Fraser University where he teaches political science and public administration.

He was one of the two government representatives on the Task Force headed by Dr. Mark Jaccard which examined options for the future of BC's electricity system.

He also worked as a policy advisor in BC's Crown Corporations Secretariat for 5 years where he dealt with a variety of issues involving BC's Crown Corporations, including BC Hydro.

Before joining the Crown Corporations Secretariat, he worked as a policy advisor on trade issues for the BC government.

John Calvert has a PhD from the London School of Economics and a BA and MA from the University of Western Ontario.