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April 18, 2023

British Columbia Utilities Commission
Suite 410, 900 Howe Street
Vancouver, B.C.
V6Z 2N3

Attention: Patrick Wruck, Commission Secretary

Dear Patrick Wruck:

Re: FortisBC Energy Inc. (FEI)

Revised Renewable Gas Program Application – Stage 2 (Application)

Response to the British Columbia Utilities Commission (BCUC) Information Request (IR) No. 1 on FEI's Rebuttal Evidence to the Evidence of Kurt G. Strunk filed by the City of Vancouver et al. (Strunk)

On December 17, 2021, FEI filed the Application referenced above. In accordance with the amended regulatory timetable established in Exhibit A-47, FEI respectfully submits the attached response to BCUC IR1 on FEI's Rebuttal Evidence to Strunk.

If further information is required, please contact the undersigned.

Sincerely,

FORTISBC ENERGY INC.

Original signed:

Sarah Walsh

Attachments

cc (email only): Commission Secretary
Registered Parties

1.0 Reference: REBUTTAL EVIDENCE OF JOHN REED, CONCENTRIC ENERGY

Exhibit B-68, Appendix A, A13, p. 12

Gas Sold by Marketers

On page 12 of Appendix A to Exhibit B-68, Mr. Reed states that "it would be equally implausible to assume that a customer electing to receive gas from a competitive marketer would be delivered different "marketer" gas instead of system gas".

1.1 Please confirm that gas marketers sell the same product (i.e. conventional natural gas) as FEI. If not, please explain the differences between the gas sold by FEI and the gas sold by marketers.

1.1.1 If yes, please explain whether gas marketers sell the same product at different rates than FEI.

Response:

Confirmed. The physical product supplied to customers from gas marketers is provided through the same gas system as the product supplied by FEI, is intermingled and is indistinguishable.

Gas marketers are required to deliver gas to FEI's interconnection points with upstream pipelines that conform with specifications set out by upstream pipeline operators and FEI. FEI then takes physical possession of the gas and transports it across its system to the customers' premise.

While FEI is not privy to the contract terms and sales prices between customers and their gas marketers, it is likely that gas marketers' gas prices are not equal to FEI's cost of gas charges. For instance, gas marketers may offer daily or monthly index prices and are unlikely to have secured the same portfolio of resources as FEI, such as firm capacity on the T-South system and gas storage.

1.1.1.1 If gas marketers sell the same product at different rates than FEI, please discuss which ratemaking principles support such price differentiation/discrimination for the same product.

Response:

The following response is provided by Concentric Energy Advisors, Inc. (Concentric):

The BCUC engaged in a substantial and collaborative regulatory effort to unbundle gas service starting in the late 1990s. Unbundling of the gas supply function allows marketers to offer gas supply to customers on a competitive basis within the requirements of the BCUC's Code of

Conduct for Gas Marketers and licensing requirements. Unbundling programs aim to harness market forces for those portions of the utility service that are workably competitive in order to permit a choice of provider, the potential for lower prices and / or terms that customers prefer. Once the ground rules are established for the service and overseen by the regulator, this competitive framework serves as replacement for the ratemaking principles that otherwise apply. Ratemaking principles are meant to simulate the benefits of competition and curb the exercise of monopoly market power, so re-applying regulatory ratemaking principles to the unbundled service would be inconsistent with the nature of the unbundling program itself.

2.0 Reference: REBUTTAL EVIDENCE OF JOHN REED, CONCENTRIC ENERGY

Exhibit B-68, Appendix A, A17, p. 16

Notional Renewable Natural Gas (RNG)

On page 16 of Appendix A to Exhibit B-68, Mr. Reed states that "these costs [incurred to help meet social decarbonization goals] may be incurred off-system in Vermont, or Wisconsin, or Ontario to increase the flow of RNG into a gas system there, with that renewable gas never entering the Company's system."

2.1 Please confirm, or otherwise explain, that even if the RNG costs are incurred off-system and the RNG never enters FEI's system, those costs are nonetheless incurred by FEI and will be reflected in FEI's rates of the various offerings of the RNG Program.

<u>Response:</u>

Confirmed. FEI's customers pay the cost and receive the benefits, in the form of GHG reductions, for all of the renewable natural gas that FEI acquires. Please also refer to the response to BCUC IR1 34.2 (Exhibit B-17) for a discussion on the displacement model of delivery.

3.0 Reference: REBUTTAL EVIDENCE OF JOHN REED, CONCENTRIC ENERGY

Exhibit B-68, Appendix A, A26, p. 24; Exhibit B-11-1 (Errata Application), Figure 7-1,

p. 85; Utilities Commission Act (UCA), section 59(1)

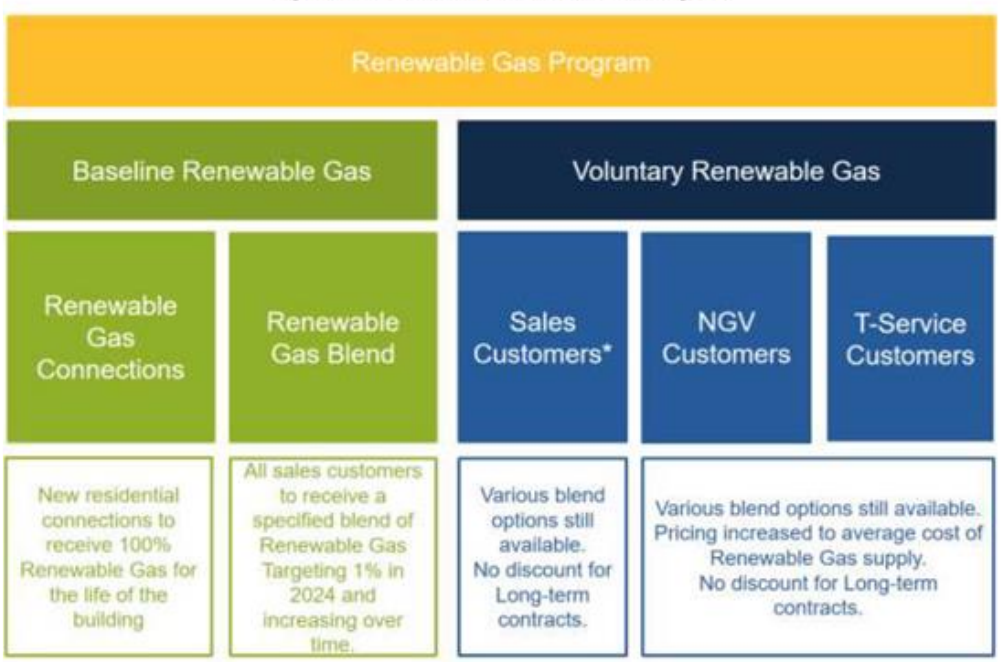
Voluntary RNG Programs

On page 24 of Appendix A to Exhibit B-68, Mr. Reed states:

> […] RNG programs that are voluntary allow customers to opt-in or opt-out and provide consumers with a level of choice over how much of their energy dollars will support the policy behind the program. <u>There is no issue of unduly discriminatory pricing if you offer all customers a nondiscriminatory cost-based rate but also allow them to choose a higher rate as an alternative</u>. Such an offering would not violate the obligation to provide just and reasonable rates to customers and provides no support for Mr. Strunk's contention that the proposed rolled-in pricing is inappropriate under the Connections program. [*Emphasis added*]

In Figure 7-1 of the Errata Application, FEI presents its Revised Renewable Gas Program as follows:

Figure 7-1: Revised Renewable Gas Program



<u>Note</u>
* Does not include NGV customers

As depicted in Figure 7-1, only the sales customers, amongst all voluntary customers, are offered a non-discriminatory cost-based rate. The Natural Gas Vehicle (NGV) customers and Transportation Service (T-Service) customers can opt-in to the Voluntary Renewable

Gas offering and pay the average cost of RNG supply, while the sales customers can opt-in to that offering and pay a lower rate of $7/gigajoule (GJ) premium over the price of conventional natural gas.

UCA section 59(1) related to discrimination in rates stipulates that:

> **59** (1) A public utility must not make, demand or receive
>
> (a) an unjust, unreasonable, unduly discriminatory or unduly preferential rate for a service provided by it in British Columbia, or
>
> (b) a rate that otherwise contravenes this Act, the regulations, orders of the commission or any other law.

3.1 Please explain why the proposed differential RNG pricing between Sales Customers on the one hand and NGV and T-Service Customers on the other hand is not unduly discriminatory, based on Bonbright ratemaking principles, and why the BCUC should approve them as just and reasonable under the UCA.

Response:

The following response is provided by Concentric:

At its core, this question asks why it is appropriate to offer the proposed Voluntary Renewable Gas service to sales customers at a $7 premium, while offering a service to NGV and T-Service customers at the average cost of RNG supply. The reason that this is not unjustly discriminatory hinges on the key fact that both NGV and T-Service customers operate in different markets than sales customers and, importantly, that these markets are workably competitive. For example, NGV customers are able to choose from multiple suppliers and multiple product offerings, and potentially monetize the carbon reduction value of their fuel elections. Sales customers cannot do that in FEI's regulated market. Similarly, T-Service customers have chosen to participate in competitive supply markets, for either conventional natural gas or RNG, even though regulated service offerings are available to them.

Moreover, the $7 premium paid by Voluntary Renewable Gas customers is not a matter of economic efficiency or ratemaking principles (i.e., Bonbright), but rather, a matter of public policy; namely, enhancing the development of an RNG offering within FEI's regulated service offerings. Such an offering is not unjustly discriminatory when compared to other RNG offerings provided in workably competitive markets.

Please also refer to Concentric's response to BCUC IR1 13.2. As discussed in that response, customers who choose to participate in the Voluntary Renewable Gas service have recourse to their otherwise applicable gas supply service provided through FEI's Renewable Gas Blend service. The ability of Voluntary Renewable Gas participants to switch back to this traditional cost-based rate that is just, reasonable, and non-discriminatory renders the different pricing of the Voluntary Renewable Gas program itself just, reasonable, and non-discriminatory.

4.0 Reference: REBUTTAL EVIDENCE OF JOHN REED, CONCENTRIC ENERGY

Exhibit B-68, Appendix A, A27, p. 25

General RNG Program in Washington State

On page 25 of Appendix A to Exhibit B-68, Mr. Reed describes that Washington state allows gas utilities to implement a general RNG program for all customers to replace a portion of conventional gas supply with the general program costs–including those for the RNG supply–to be recovered from all customers. The program is described as follows:

> RCW 80.28.385, which allows each natural gas utility to propose a program to replace a portion of its conventional natural gas supply with RNG for all retail customers, permits regulated natural gas utilities to acquire RNG through purchased gas agreements or other Commission-approved contracts, and ***to recover those costs from all*** retail gas customers consistent with existing Commission rules and policies.

4.1 Please confirm, or otherwise explain, that the program described above is most like FEI's proposed RNG Blend offering, rather than the proposed Renewable Gas Connections offering.

<u>Response:</u>

The following response is provided by Concentric:

The proposed Renewable Gas Blend service and the Washington state utility optional supply program are similar in that they comingle RNG with conventional natural gas for all customers and recover costs from all customers. However, consideration of the Washington state program is still relevant to the issues presented by the Renewable Gas Connections service because Washington does not single out new customers for any special rate treatment.

5.0 Reference: REBUTTAL EVIDENCE OF JOHN REED, CONCENTRIC ENERGY

Exhibit B-68, Appendix A, A28, p. 27

Incremental Pricing and Economic Efficiency

On page 27 of Appendix A to Exhibit B-68, Mr. Reed states:

> […] I agree that incremental cost pricing – standing alone as an economic principle – leads to economic efficiency, but as applied to utility service, incremental cost pricing would need to be applied to all gas customers, not just new customers, and to competing utility services as well to achieve the efficiency goals. <u>Mr. Strunk does not extend this rationale for incremental cost pricing to the delivery function of the gas system, nor to all gas customers, nor does he recommend that it be applied to the electric utility market</u>. As noted by economist Alfred Kahn, "Thou shalt not optimize piecemeal." That is because under piecemeal use of incremental cost pricing consumer consumption choices will shift to the service priced at average embedded costs and erode hoped for efficiency gains in the market. [*Emphasis added*]

5.1 Please clarify how incremental cost pricing could be applied to the delivery function of the gas system (e.g. On what basis? Which components of the natural gas rates would be affected?).

<u>Response:</u>

The following response is provided by Concentric:

Incremental cost pricing could be applied to the delivery function of the gas system by substituting replacement cost valuation for depreciated original cost (DOC) for each segment of rate base. The use of replacement cost (which sometimes is referred to as trended original cost) would apply to the transmission, storage, distribution and general costs on the system and would move all rates for all services to incremental cost. However, such an approach produces a revenue level that far exceeds that needed to produce a compensatory return when evaluated on a DOC basis.

5.2 Does Mr. Reed consider that BC Hydro's Residential Inclining Block Rate (Step 1 rate: 9.50 cents per kilowatt hour (c/kWh) for the first 675 kWh per month and Step 2 rate: 14.08 c/kWh for any additional kWh per month) represents "incremental pricing" of the type that would be required so that incremental cost pricing of RNG would lead to economic efficiency? Please discuss why or why not.

Response:

The following response is provided by Concentric:

No, the inclining block structure for BC Hydro does not reflect incremental cost pricing. First, if the higher cost block were set to the system's long run incremental cost, that price would need to be applied to all consumption, not just to consumption above a threshold level. Second, in general, inclining block rates are designed to promote energy efficiency by inducing a reduction in energy consumption as a conservation measure and may not necessarily be reflective of the incremental cost of additional resources or the incremental costs to serve new customers, which is how Mr. Strunk proposes to apply incremental cost pricing for renewable natural gas supply for Connections customers. Moreover, incremental cost pricing would need to be applied to both the supply as well as the delivery function (transmission and distribution) in order to achieve that correct incremental cost price signal. As noted in my Rebuttal Evidence to Mr. Strunk on PDF p. 28, I am unaware of any North American utility that has adopted that approach in ratemaking nor has FEI submitted such a proposal for consideration.

6.0 Reference: REBUTTAL EVIDENCE OF JOHN REED, CONCENTRIC ENERGY

Exhibit B-68, Appendix A, A29, p. 28; Exhibit C7-8, BCUC IR 3.1

Bonbright Principle: Effectiveness in Yielding the Total Revenue Requirement

On page 28 of Appendix A to Exhibit B-68, Mr. Reed states:

> […] Mr. Strunk's proposal – applied fully to both gas and electric services to avoid the economic hazard of piecemeal optimization – would yield revenues far above the revenue requirement based on depreciated original cost. […] If we are trying to solely achieve economic efficiency and we don't care about limiting utility revenues to embedded cost of service, then we should charge incremental price to all gas and electric customers. [*Emphasis added*]

In response to BCUC IR 3.1 in Exhibit C7-8, Mr. Strunk stated, in relation to the Bonbright principle of "effectiveness in yielding total revenue requirement under the fair return standard":

> Mr. Strunk anticipates that the Commission will set rates to provide FEI a reasonable opportunity to recover its total revenue requirement. Hence, under the FEI proposal, and under any alternatives or refinements that the Commission may approve, this Bonbright principle will be upheld for FEI.

6.1 Please explain why total revenues would automatically far exceed the revenue requirement if incremental pricing was applied fully to both gas and electric services.

Response:

The following response is provided by Concentric:

The reason why total revenues would be above the revenue requirement is that pricing based on incremental cost would exceed prices based on historic depreciated cost (due to the effects of inflation and depreciation), and when applied to usage the resulting revenues would be all but certain to far exceed the revenue requirement. That would contravene the first Bonbright principle. Mr. Strunk does not elaborate on the ratemaking techniques he would employ to ensure that the revenue requirement would be effectively met, rather than exceeded, and instead, as Mr. Strunk noted in his response to BCUC IR 3.1 (Exhibit C7-8), defers to the BCUC to develop the needed ratemaking adjustments. There are no easy paths forward to implementing incremental cost pricing under the Bonbright principles. Under cost causation, selective incremental cost pricing entails the economic fiction that new customers impose new costs on the system, rather than existing customers who fail to use less or stay on the system rather than exiting. Given that incremental cost pricing would be much higher than depreciated historical cost, that would raise issues under principle 6, rate stability. Principle 4 requires customer understanding and acceptance and that may prove difficult for customers who are used to rates based on historic depreciated costs rather than marginal costs. Economic efficiency is not the only Bonbright principle to consider when setting rates, but rather each of the relevant principles must be examined and balanced.

6.2 If Mr. Strunk's proposal of incremental pricing for RNG was applied only to Renewable Gas Connection customers, please state whether the BCUC could set a rate that would be effective in yielding total revenue requirement under the fair return standard.

Response:

The following response is provided by Concentric:

As detailed in my Rebuttal Evidence, I find no support under the Bonbright principles for applying incremental cost pricing to just the commodity portion of the Connections customers bill. If Bonbright is deemed inapplicable, then the BCUC could set a rate that collects the costs of the renewable natural gas supply just from the Connections customers. The question asks about effectiveness in "yielding the total revenue requirement" but I interpret that to mean supply costs for the renewable natural gas for the Connections customers rather than the total revenue requirement for FEI as a whole.

6.2.1 Please clarify why fair return standard applies, considering that (i) section 18 of the Clean Energy Act stipulates that rates must allow FEI to "collect sufficient revenue" to recover the cost incurred of a prescribed undertaking and (ii) FEI's gas commodity rates are based on flow-through cost recovery.

Response:

The following response is provided by Concentric:

While I am not an attorney and offer no legal opinions on the interpretation of the *Clean Energy Act*, Section 18 (2) states that "In setting rates under the *Utilities Commission Act* for a public utility carrying out a prescribed undertaking, the commission must set rates that allow the public utility to collect sufficient revenue in each fiscal year to enable it to recover its costs incurred with respect to the prescribed undertaking." "Costs" for a utility include expenses as well as invested capital and a return on that capital. The BCUC sets rates to "ensure that the rates charged by a utility are just and reasonable which include a fair and reasonable return on capital." Big White Gas Utility Ltd., Decision and Order G-196-21, PDF p. 8 (June 25, 2021). To the extent that FEI has invested capital associated with the Connections program, it should recover a fair return on that capital as well as the capital itself.

The following response is provided by FEI:

FEI concurs with Concentric's response above and notes that where FEI has invested capital as part of a prescribed undertaking, e.g., for biogas upgrading facilities, rates were set to recover FEI's cost of capital, including a reasonable opportunity to earn its fair return.

7.0 Reference: REBUTTAL EVIDENCE OF JOHN REED, CONCENTRIC ENERGY

Exhibit B-68, Appendix A, A30, p. 29

Decarbonization Arising From FEI's RNG Program

On page 29 of Appendix A to Exhibit B-68, Mr. Reed states:

> […] Given the magnitude of the price difference between rolled-in pricing and incremental cost pricing for new Connections customers, the results of Mr. Strunk's proposal would be to unjustifiably curtail growth while doing nothing to further the decarbonization goals of the natural gas supply to help British Columbia transition to a cleaner energy future.

7.1 Please explain why Mr. Strunk's proposal of incremental cost pricing for the Renewable Gas Connection offering would curtail the growth of RNG in FEI's system when, in the absence of such program, the same quantity of RNG will flow in FEI's system through the RNG Blend offering, thus resulting in identical decarbonization levels.

Response:

The following response is provided by Concentric:

To clarify, the "growth" mentioned in the referenced evidence was meant to refer to customer growth. It is also not certain that the same quantity of RNG would flow through the system in the absence of such a program. That statement appears to presume that RNG purchases would be the same if made for the Blended gas program or for the Blended gas program and the Connections program.