***Consumers Council of Canada and the Vulnerable Energy Consumers Coalition (CCC) and (VECC) INTERROGATORY #7 List 1***

***Interrogatory***

Ref: B1/T3/S1 p. 14

Issue 4.0
Issue: Cost of Capital/Capital Structure

Topic: Performance Based regulation

Request:

a) Please indicate whether the BCUC's move to performance based regulation has in her judgment increased or decreased the ability of either FortisBC or Terasen Gas to earn their allowed ROE. Have either company failed to earn their allowed ROE while under PBR?

b) Please indicate ands discuss in detail any jurisdiction in Canada that has introduced PBR and exposed a utility to material losses in terms of under earning their allowed ROE by more than 1.0%.

***Response***

a) To date, the utilities have been able to earn their allowed ROEs, except in unusual circumstances. Terasen failed to earn its allowed return in 1998 due to employee severances paid as result of a major corporate restructuring effort. FortisBC's 2002 actual ROE was below the allowed level primarily due to integration expense and software write-offs. Nevertheless, it should be noted that (a)the PBR plans in question retain many features of cost-of-service regulation; (b) FortisBC's productivity off-sets (which are applied to capital and certain operating and maintenance costs) are lower than they were historically; and (c) the ability to achieve incremental cost efficiencies becomes more difficult over time; and (d) FortisBC noted in its 2005 Annual Report to Shareholders in discussing regulatory risks the challenges to the company of the implementation, financing and customer rate impacts of its large capital expenditure program.

b) Ms. McShane is not aware of any specific cases. The approach that has been taken in BC and at the NEB has typically been by way of settlement between the companies and their customers/shippers, rather than by a plan whose parameters have been determined by the regulator. In Ontario, because of the rate freeze, the impacts of price cap regulation for the distributors cannot be fully assessed. Union Gas' price cap plan that was in place between 1999 and 2003 was

accompanied by a symmetric earnings sharing mechanism that limited the downside risk to its earnings. The company is not operating under a price cap methodology at this time, so the longer-term impacts cannot be evaluated.