

GOVERNMENT IMPROVEMENTS TO ACCOUNTING PRACTICES AT B.C. HYDRO CONVINCES AUDITOR GENERAL TO REMOVE PREVIOUS QUALIFICATION

Auditor General Carol Bellringer cited the non-standard accounting practices at B.C. Hydro as a reason to qualify the province's 2016/17 and 2017/18 financial statements. Following the government's decision to require B.C. Hydro to adopt public sector accounting standards and restore most of the regulatory authority to the B.C. Utilities Commission (BCUC), Ms Bellringer has decided that the B.C. Hydro portion of the 2018/19 public accounts are now acceptable.¹

While the government has yet to provide the regulator with full authority to set B.C. Hydro's return on equity (net income), the auditor general decided to lift her qualification based on the government's assurance that BCUC's full authority to set rates and the net income will be will be allowed starting in 2021.

What Accounting Practices Failed the Test?

In essence, the auditor general determined that the government had been circumventing national public sector accounting standards by allowing B.C. Hydro to use rate-regulated accounting without an independent third-party regulator. The previous Liberal government had been restricting the discretion of the BCUC to oversee the operation of B.C. Hydro for some time prior to the cabinet direction of 2012 that required the Commission to set rate increases at levels determined by the government. In 2014, the government issued highly prescriptive directions to the BCUC which set rate changes for five years, and included the requirement to approve a new deferral account to record future unbilled and uncollected revenue.²

Such an action contravened the requirement that regulatory accounting could only be practiced where there was an independent third-party regulator. B.C. Hydro's profitability and dividends to government depended on the extensive use of regulatory

¹ https://www.bcauditor.com/sites/default/files/publications/reports/OAGBC_ROTO-2018-19_RPT.pdf

² <https://ojs.library.ubc.ca/index.php/bcstudies/article/view/187787/186354> The Rate Smoothing Regulatory Account (RSRA) allowed B.C. Hydro to record and defer the variance between the required revenue and the revenue allowed by the approved rates. The allowed rates were lower than what was required to achieve the net income, so the difference was added to the RSRA to allow B.C. Hydro to show a higher profit than would have been possible without the revenue deferral.

or deferral accounts. But in 2010 the government had exempted B.C. Hydro from the requirement to have the regulatory accounts approved by an independent regulator.³

Following a detailed 2016 query by Adrian Dix, who was then the NDP critic for B.C. Hydro, Auditor General Bellringer reviewed the accounting practices at B.C. Hydro.⁴ The result was her qualification of the governments financial statements for 2016/17 and for 2017/18, which was explained in a special report on rate-regulated accounting issued Ms Bellringer in February 2019.⁵

The Government's Response

The NDP government agreed that the accounting practices at B.C. Hydro, and the tight control over the BCUC, did not conform to the accounting rules. In November 2018, it repealed the 2010 exemption from the requirement for an independent third-party regulator. The government ordered B.C. Hydro to end the use of the Rate Smoothing regulatory account as of 31 December 2018, and in February 2019 the government rescinded the highly prescriptive Direction 7 to the BCUC and reduced the restrictions on the BCUC's rate setting authority.

The BCUC is Still Not Independent

The government has made many important improvements to the accounting practices at B.C. Hydro, and has removed most of the prescriptive directives to the BCUC (including ending the revenue deferral account). However, it still requires the BCUC to set the 2019 and 2020 rates to generate an annual net income of \$712 million. It has stated that this requirement will be removed starting in 2021, and the auditor general has accepted this pledge to fully restore the rate-setting independence of the BCUC.

In her explanation of her opinion on the 2018/19 statements Ms Bellringer stated that her withdrawal of the qualification was based on the promised independent "framework" for the BCUC; "Government's plans provide for an appropriate regulatory framework, and allow BCUC to provide the scrutiny and authority required by the accounting standards."⁶ Later in the document she again referred to the planned independence of the regulator: "With these changes in government regulation and direction, the removal of the RSRA, and government's commitment to restore the authority of the BCUC, we agree with government's assessment that BC Hydro's

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http://www.bcpolicy Perspectives.com/media/attachments/view/doc/occasional_paper_no_63_1_october_2018/pdf/occasional_paper_no_63_1_october_2018.pdf

⁴ https://thetyee.ca/News/2016/06/10/BC-Hydro-Misleading-Accounting/?utm_source=daily&utm_medium=email&utm_campaign=100616

⁵ https://www.bcauditor.com/sites/default/files/publications/reports/OAGBC_RRA_RPT.pdf

⁶ https://www.bcauditor.com/sites/default/files/publications/reports/OAGBC_ROT0-2018-19_RPT.pdf p. 10.

use of rate-regulated accounting is now appropriately reflected in the SFS [summary financial statements], and have therefore removed our qualification for this year.”⁷

B.C. Hydro Intends to Continue to Count Future Revenue

In her criticism of the “Fair Hydro” accounting scheme the Ontario auditor general was clear that recording future unbilled revenue was not permitted. Ms Bellringer has not been as explicit about this issue as her Ontario counterpart, but she highlighted the RSRA as an example of the excess of the deferral practices at B.C. Hydro and called the recognition of the revenue as “premature.”⁸

Despite the closure of the RSRA and the auditor general’s comments, B.C. Hydro has stated that it will continue to record the annual difference between the budgeted revenue and the actual revenue in a deferral account.⁹ This helps ensure that the net income target for the shareholder is achieved. This was the practice used from 2011/12 to 2015/16 when over \$850 million in domestic revenue shortfalls were added to this account.

B.C. Hydro was asked if its new external auditor (the auditor general) had been consulted on the plan to record unbilled and uncollected revenue in a deferral account. It replied that it had not consulted with the new external auditor, but she would have an opportunity to comment as part of her audit of the 2019/20 year. It noted that its current external auditor had provided a clean opinion on the 2017/18 statements, which included the recording of hypothetical revenue.¹⁰ It failed to note that Auditor General Bellringer was assuming the role of B.C. Hydro’s external auditor because she believed that there was significant room for improvement in the financial oversight of the public utility.

As the new external auditor of B.C. Hydro, Ms Bellringer will be required to decide if this revenue recording practice meets the national public sector accounting standards.

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The writer is a retired senior BC government public servant whose paper describing the BC government’s manipulation of the finances of BC Hydro from 2008 to 2014 was published by *BC Studies* in November

⁷ Ibid. p. 11.

⁸ https://www.bcauditor.com/sites/default/files/publications/reports/OAGBC_RRA_RPT.pdf p. 17. See also http://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_bc_hydro_says_the_bcuc_is_independent_25_june_2019/pdf/commentary_bc_hydro_says_the_bcuc_is_independent_25_june_2019.pdf

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http://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_bc_hydro_says_the_bcuc_is_independent_25_june_2019/pdf/commentary_bc_hydro_says_the_bcuc_is_independent_25_june_2019.pdf

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http://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_bc_hydro_says_the_bcuc_is_independent_25_june_2019/pdf/commentary_bc_hydro_says_the_bcuc_is_independent_25_june_2019.pdf

2016. *BC Studies* published his paper on the 40-year financial history of ICBC in 2013. He is an intervener in the BC Utilities Commission's current reviews of ICBC's and B.C. Hydro's rate requests.