

**GOVERNMENT RENEGES ON PROMISE TO ALLOW BC HYDRO'S
REGULATOR FULL INDEPENDENCE**

A new cabinet order (OIC 123/22) to the BC Utilities Commission (BCUC) extends the requirement that the BCUC set BC Hydro rates to generate a pre-determined net income of \$712 million.¹ In effect, the regulator is forced to continue to set BC Hydro's annual rates to achieve a profit target (or return on equity) set by cabinet, rather than by the regulator.

BC Hydro relies on rate regulated (deferral) accounting to manage its finances.² The national IFRS accounting standard requires that rate regulated accounting be regulated by an independent third-party. By directing the BCUC to set rates to achieve a pre-determined net income the government has violated the requirement for an independent regulator to oversee BC Hydro's deferral accounts.

Former BC Auditor General Carol Bellringer qualified the government's 2016/17 and 2017/18 financial statements in part because of the lack of an independent regulator overseeing the deferral accounts. She withdrew her qualification for 2019/20 after the government placed BC Hydro on the national accounting standard and promised to restore the BCUC's independence.

Will this negation of the promise to restore the Commission's independence compel her successor to also qualify the government's statements for the same reason?

**Previous Auditor General Cited Lack of an Independent Regulator in
Qualifying BC Government's Financial Statements**

The BC government has been active in directing the BCUC's interactions with BC Hydro for many years. . In 2011, the government exempted BC Hydro from the need for an independent regulator (the BC Utilities Commission) to approve regulatory (deferral) accounts.

Beginning in 2012, the BC government has set BC Hydro's annual electricity rate increases below the level required to match the increase in the utility's costs. In 2014, as part of a highly prescriptive cabinet order, the Crown corporation was required to record and defer unbilled and uncollected revenue in a new "rate smoothing" deferral account to continue the annual rate subsidy and still produce high net income levels. These

¹ https://docs.b cuc.com/Documents/Proceedings/2022/DOC_65965_B-17-BCH-submission-on-OIC123-AmendedDirective8-Compliance.pdf

² As of 31 March 2021, the net regulatory/deferral assets comprised 67% of BC Hydro's equity. Both Hydro Quebec and Manitoba Hydro utilize deferral accounting, but are much less dependent on this accounting practice.

prescriptive cabinet directives led Rowland Harrison, one of Canada’s experts on regulatory oversight, to state in November 2014 that the BC Utilities Commission was being reduced to acting as an agent of the BC cabinet.³

The highly prescriptive directive to the BCUC compelled Auditor General Bellringer to qualify the government’s 2016/17 and 2017/18 financial statements. She stated that the “prescribed” accounting practice at BC Hydro does not conform to generally accepted accounting principles.

Auditor General Withdraws Qualification for 2018/19 Based on Reforms and Commitment to Restore the BCUC’s Authority

Shortly after the NDP formed government in July 2017, Finance Minister Carole James acknowledged that BC Hydro’s finances needed to be cleaned up. In November 2018, the directive exempting BC Hydro from national accounting standards was deleted, and BC Hydro wound-up the highly questionable Rate Smoothing deferral account in December.

In early 2019, in conjunction with the release of the Comprehensive Review Phase 1 staff report, the government rescinded the highly prescriptive Direction 7 to the BCUC and replaced it with a less restrictive Directive 8. The new directive did not fully restore the BCUC’s independence because it was still required to set rates to generate \$712 million in net income until 2022/23.⁴ It was assumed that beginning in fiscal year 2023/24 the BCUC would have full discretion to set an appropriate ROE and the resulting net income.

Ms Bellringer noted these positive changes in her July 2019 explanation as to why she withdrew her qualification of the government’s 2018/19 financial 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.” 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** [my emphasis], we agree with government’s assessment that BC Hydro’s use of rate-regulated accounting is now appropriately reflected in the SFS [summary financial statements], and have therefore removed our qualification for this year.”⁵

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http://www.bcpolicyperspectives.com/media/attachments/view/doc/occasional_paper_no_15_bcuc_independence_27_october_2016/pdf p. 3.

⁴ The government stated that the net income requirement needed to be extended so as not to disrupt the government’s three-year fiscal plan.

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https://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_auditor_general_removes_qualification_19_july_2019/pdf/commentary_auditor_general_removes_qualification_19_july_2019.pdf

The statement is forward looking. The withdrawal of the qualification was based on the government's commitment to restore the BCUC's authority to determine the net income commencing in fiscal year 2023/24.

In fact, BC Hydro's three-year rate request for the 2022/23 to 2024/25 period, filed on 31 August 2021, assumed that once the BCUC was free to determine an appropriate return on equity (ROE) the approved net income for 2023/24 and future years would vary from the \$712 million specified for 2022/23. The BCUC was intending to launch a study on the appropriate ROE for BC Hydro and had already begun a generic review of the cost of capital.⁶

Will Michael Pickup Pick Up the Gantlet?

The effect of the cabinet order is to preserve the \$712 million net income from BC Hydro in the government's revenue calculation for 2023/24 and 2024/25. However, as explained previously, no actual cash is transferred to the government's discretionary accounts.⁷ However, the decision to continue to curtail the independence of the BCUC with respect to regulating BC Hydro's rates poses a direct challenge to Michael Pickup, the new provincial auditor general. His predecessor was clear that the government's directions to the BCUC constituted clear interference in its independence.

The national IFRS accounting standards require an independent third-party to oversee and approve rate regulated accounting. Ms Bellringer relied on the government's commitment to fully restore the BCUC's independence when she was persuaded to withdraw her qualification on the government's 2018/19 financial statements.

It now appears that Mr. Pickup has no option but to call out the government on its "bait and switch" tactics, and to qualify the government's 2021/22 statements because of the lack of an independent regulator for BC Hydro's regulatory/deferral accounts.

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

⁶ <https://www.bcuc.com/OurWork/ViewProceeding?ApplicationId=849>

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https://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_budget_distortion_february_23_2022/pdf/commentary_budget_distortion_february_23_2022.pdf

