

**BC HYDRO QUIETLY RELEASES ITS SECOND QUARTER FINANCIAL REPORT**

In the third week of December 2020, BC Hydro posted its half year (1 April to 30 September) financial results for the current fiscal year.<sup>1</sup> This paper will outline the key features of the Q2 report.

In general, the half-year results were significantly affected by lower electricity sales resulting from the government's efforts to contain the COVID-19 pandemic. These were reflected in lower Domestic sales and revenue. The sharp decline in interest rates that occurred in March 2020 continued into the Q2 period. This dramatically worsened BC Hydro's pension liability, and slightly worsened the future interest rate hedging liability.

BC Hydro added to its regulatory accounts asset balance to off-set the revenue loss and the increase in its balance sheet pension liabilities. Using deferral accounts in this way protects the net income target but increases the liability burden for future generations of ratepayers.

**Revenue**

For the first six months total Domestic revenue was \$138 million (or 5.8%) less than the revenue for the same period in 2019/20. An increase of 8.9% in Residential GWh sold was more than offset by a 5.9% decline in Light Industrial and Commercial sales, and a 10.1% decline in the Large Industrial category.

A 1.6% decline in the BC Utilities Commission's approved rates for the 2020/21 year also contributed to the overall decline in Domestic revenue. Trade revenue, however, increased by \$203 million due to greater sales.

**Deferring Revenue Variance**

In compliance with an order from the BCUC, BC Hydro is now reporting the difference between the budgeted and actual revenue in a "Load Variance" regulatory account. The balance in this account was \$223 million as of 30 September 2020, and includes the revenue shortfall (lower sales) resulting from the COVID-19 control measures.

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<sup>1</sup> <https://www.bchydro.com/content/dam/BCHydro/customer-portal/documents/corporate/accountability-reports/financial-reports/quarterly-reports/bchydro-f21-q2-report.pdf>

## **Energy Costs**

Domestic energy costs for the first six months were \$861 million, \$21 million (or 2%) lower than the same period in the prior fiscal year. The costs to purchase IPP power increased by \$30 million (4.3%) despite the total GWh purchased declining by 7.7%.

## **Operating Costs**

Of note in the Q2 results was a \$386 million (45%) decrease in finance charges compared to the same period in the prior year. This was due to the losses in the future interest rate hedging program plateauing in the first half of the current year compared to the major growth which occurred in 2019/20. The losses are recorded as finance charges.

The losses from the hedging of future interest rates are offset on the balance sheet by deferrals to the Debt Management regulatory account. This account protects the notional equity level from the large liabilities incurred by the program to hedge future interest rates.<sup>2</sup>

## **Capital Expenditures and Debt**

For the first six months capital expenditures totalled \$1.55 billion (\$854 million for Site C), compared to \$1.46 billion (\$770 million for Site C) for the first six months of the prior year.

As of 30 September 2020, the long-term debt totalled \$24.70 billion, an increase of \$1.01 billion from the 31 March 2020 total. Compared to a year earlier the long-term debt increased by \$1.62 billion.<sup>3</sup>

## **Net Deferral Assets Now Comprise 100% of Equity**

As of 30 September, BC Hydro reported assets of \$40.58 billion and liabilities of \$34.91 billion, and equity of \$5.67 billion, a slight increase from the 31 March 2020 figure. The net regulatory assets increased by \$711 million, and now total \$5.72 billion, or 100.8% of BC Hydro's equity.<sup>4</sup>

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[http://www.bcpolicy Perspectives.com/media/attachments/view/doc/commentary\\_bc\\_hydro\\_hedging\\_gamble\\_17\\_september\\_2020/pdf/commentary\\_bc\\_hydro\\_hedging\\_gamble\\_17\\_september\\_2020.pdf](http://www.bcpolicy Perspectives.com/media/attachments/view/doc/commentary_bc_hydro_hedging_gamble_17_september_2020/pdf/commentary_bc_hydro_hedging_gamble_17_september_2020.pdf)

<sup>33</sup> <https://www.bchydro.com/content/dam/BCHydro/customer-portal/documents/corporate/accountability-reports/financial-reports/quarterly-reports/F20-Q2-Report.pdf> p. 16.

<sup>4</sup> As of 31 March 2020, the net regulatory asset to total equity ratio was 88.5% (equity was \$5.65 billion while the net regulatory assets were \$5.0 billion).

The decline in interest rates will reduce BC Hydro's future borrowing costs, but it also immediately reduced the discount rate on the pension liability, which increased the solvency deficit.<sup>5</sup> This increase in the pension liability was offset by a \$553 million increase in the pension regulatory asset, a major component of the net \$711 million increase in the total deferrals for the first half year.

The 1.6% rate reduction for the current year was partly achieved by releasing some of the ratepayer credits (regulatory liabilities) accumulated in the Heritage and Trade Income deferral accounts. The reduction in the regulatory liabilities increased the net regulatory assets, and contributed to the increase in the ratio of the regulatory assets to equity.

### **Outlook to Year-End**

BC Hydro does not provide a year-end forecast with its Q2 report. However, on 22 December 2020, our public utility recently filed with the BCUC a general 1.6% rate increase request effective 1 April 2021, where the application included a financial forecast for the current year-end. The request forecasts net income of \$690.7 million for the current year, or \$11.3 million less than the \$712 million budget. The net balance in the regulatory accounts is forecast to reach \$6.27 billion, a \$1.26 billion increase over the 2019/20 amount. The net regulatory asset balance will equal 98.7% of the forecast equity of \$6.35 billion.<sup>6</sup>

It appears that rate affordability, and a high return on equity, will continue to be achieved by transferring a variety of cost variances and revenue shortfalls to future generations through enthusiastic use of the deferral (regulatory) 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 B.C. Hydro's rate requests.

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[http://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary\\_low\\_interest\\_rates\\_16\\_june\\_2020/pdf/commentary\\_low\\_interest\\_rates\\_16\\_june\\_2020.pdf](http://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_low_interest_rates_16_june_2020/pdf/commentary_low_interest_rates_16_june_2020.pdf)

<sup>6</sup> The regulatory account balance is from Chapter 7, Table 7-3 (Pdf 354/434) in [https://www.bcuc.com/Documents/Proceedings/2020/DOC\\_60299\\_B-2-BCH-F22-RRA-Application.pdf](https://www.bcuc.com/Documents/Proceedings/2020/DOC_60299_B-2-BCH-F22-RRA-Application.pdf) while the forecast equity is from Appendix A, Schedule 9.0 (Pdf 82/650) in [https://www.bcuc.com/Documents/Proceedings/2020/DOC\\_60301\\_B-2-2-BCH-F22-RRA-Appendices.pdf](https://www.bcuc.com/Documents/Proceedings/2020/DOC_60301_B-2-2-BCH-F22-RRA-Appendices.pdf)

## APPENDIX

The following summarizes the changes in the key regulatory accounts from the 2019/20 actuals to the forecast for 2020/21. The information was developed from Table 7-3 in Chapter 7 for BC Hydro's 2021/22 rate request application:

[https://www.bcuc.com/Documents/Proceedings/2020/DOC\\_60299\\_B-2-BCH-F22-RRA-Application.pdf](https://www.bcuc.com/Documents/Proceedings/2020/DOC_60299_B-2-BCH-F22-RRA-Application.pdf) p. 7-18 (pdf 354/434).

	A2019/20	Transfer	Add/Del.	F2020/21
Heritage DA	(300)	--	414	114
Non-Herit. DA	205	(353)	(117)	(265)
Load Variance	--	354	(165)	159
Trade Inc. DA	(174)	--	160	(14)
Total	(269)	1	262	(6)
Non-C. Pension	210	--	926	1,136
Debt Manage	953	--	197	1,150
Total All (30)	5,004	2	1,260	6,266

The major swings in the Heritage and Trade Income accounts reflect the credit to the ratepayers of the accumulated surplus during the current year.

The six regulatory accounts shown here reflect the main changes from 2019/20 to 2020/21.