

HIGHER TRADE REVENUE AND INTEREST RATE INCREASES POWER BC HYDRO'S POSITIVE THIRD QUARTER RESULTS

BC Hydro recently released its third quarter financial report for the period 1 April to 31 December 2022. The results showed a positive result, as the \$1.38 billion in net income before transfers to regulatory accounts was \$985 million higher than the Q3 result for the prior year.¹ BC Hydro operates with many regulatory deferral accounts which practically eliminate the risk to the budgeted net income. Thus, most of the net income growth had the effect of reducing the outstanding balance in the regulatory accounts rather than increasing the net income.

Domestic Revenue and Costs

The nine-month Q3 domestic revenues were \$ 3.72 billion, which was approximately \$300 million lower compared to the same periods in the prior fiscal year. The decrease was primarily due to \$320 million of one-time rebate issued to residential and commercial customers after the announcement on cost-of-living credits by Premier Eby in November 2022.²

Domestic power sales increased by 1.7%, but the effect on revenue was negated by a general rate reduction of approximately 1.4% beginning 1 April 2022.

The cost of energy for Domestic requirements decreased by approximately \$200 million while the change in the cost of water rentals and Independent Power Producers electricity was relatively stable.

Trade Income

BC Hydro recorded an increase of \$1.14 billion (up 79.8%) in Trade revenue. This result was a combination of higher prices (up 63%) and higher sales (up 21%). The cost of Trade energy rose by \$577 million compared to the prior period. The net Trade income for the nine months increased by \$565 million compared to the prior period.

¹ <https://www.bchydro.com/content/dam/BCHydro/customer-portal/documents/corporate/accountability-reports/financial-reports/quarterly-reports/bchydro-f23-q3-report.pdf> p. 18.

²

https://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_bcuc_independence_5_december_2022/pdf/commentary_bcuc_independence_5_december_2022.pdf

The rise in Trade prices reflects the increase in natural gas prices in the United States during the first nine months of the year. The same increase was reported by Quebec Hydro in its January to December 2022 annual report.³

Of note is the realized price per MWh of \$115.69 for the first nine months; well above the average price for the Domestic customer classes. This may prompt BC Hydro to reconsider its objective of reducing surplus Domestic sales to increase Large Industrial sales (at \$61.75/MWh). Exporting excess Domestic power is more profitable.

Interest Rate Increase –Hedging

The increase in interest rates during the nine months had a significant impact on BC Hydro's results. The future interest rate hedging program, which had accumulated a loss of \$709 million (owed by ratepayers to BC Hydro) by 31 December 2021, was now in the black.⁴ By 31 December 2022 a swing of \$744 million resulted in a gain (owed to ratepayers) of \$35 million. Approximately \$2.7 billion in notional principle was hedged as at 31 December 2022.

Interest Rate Increase –Non-Current Pension

The increase in interest rates has increased the discount rate on pension obligations which reduces the cash requirement. This was partly offset by a decrease in the rate of return on pension assets. The \$61 million regulatory liability (owed to ratepayers) for 2021 has jumped to a regulatory liability of \$917 million as of 31 December 2022.

Interest Rate Increase –Borrowing Costs

The increase in interest rates will negatively affect the cost of borrowing, but the impact has not had much effect yet. The bulk of BC Hydro's \$26.5 billion in long-term debt, which was issued during the period of relatively low interest rates, will take a number of years to mature. The new borrowing discussed in the Q3 report is at 4.0%, compared to 2.4% for the prior period.⁵

Regulatory Account Balance

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https://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_hydro_quebec_2022_25_february_2023/pdf/commentary_hydro_quebec_2022_25_february_2023.pdf

⁴ The Debt Management Regulatory Account.

⁵ <https://www.bchydro.com/content/dam/BCHydro/customer-portal/documents/corporate/accountability-reports/financial-reports/quarterly-reports/bchydro-f23-q3-report.pdf> p. 26.

The strong Q3 results have significantly reduced the net regulatory assets (owed by ratepayers), which totalled \$1.54 billion as of 31 December 2022, compared to \$4.0 billion as of 31 December 2021. Most of the change is explained by the changes in non-current pension costs, debt hedging and trade income discussed earlier.

TABLE 1 –Net Regulatory Account Balance (\$=million)

	Q3 2021	Q3 2022	Difference
Regulatory Assets	4,825	3,856	(969)
Regulatory Liabilities	(797)	(2,313)	(1,516)
Net Assets	4,028	1,543	(2,485)

Source: BC Hydro Q3 reports for 2021 and 2022.

Will the surplus in the Trade Income Deferral Account prompt the government to order the BC Utilities Commission to order another rebate? The surplus in this account from the 2021/22 fiscal year was the source of the \$320 million rebate ordered in November 2022. BC Hydro had budgeted for a surplus of some \$125 million in this deferral account for the 2022/23 fiscal year, so there would appear to be funds available for a second rebate to aid in achieving the government’s affordability goal.

The alternative would be to use the apparent windfall to retire some of BC Hydro’s accumulated debt.

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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 is an intervener in the BC Utilities Commission’s reviews of ICBC’s and BC Hydro’s rate requests.