

NO: R125

COUNCIL DATE: **JULY 7, 2014**

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## REGULAR COUNCIL

TO: **Mayor & Council**

DATE: **July 2, 2014**

FROM: **Acting General Manager, Engineering**

FILE: **5514-102**

SUBJECT: **Surrey City Energy (District Energy System Utility)  
Appointment of Expert External Rate Review Panel**

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## RECOMMENDATION

The Engineering Department recommends that Council:

1. Receive this report as information;
2. Appoint Robert Hobbs as the Chair of the Expert External Rate Review Panel for three (3) years; and
3. Appoint both Alison Rhodes and Michael Wilson as members to the Expert External Rate Review Panel for two (2) years.

## INTENT

The purpose of this report is to obtain approval for the appointment of three individuals to the district energy Expert Rate Review Panel (the "Panel").

## BACKGROUND

At its Regular meeting on December 12, 2013 Council adopted the recommendations of Corporate Report No. R246; 2013, that authorized the principles and a related methodology to regulate the rates and the rate structure that will be used by Surrey City Energy (SCE), the City's district energy (DE) utility, in relation to its business operations and further authorized staff to proceed with a public Request for Expressions of Interest for the purpose of establishing an Expert Rate Review Panel based on the Terms of Reference provided. A copy of the DE Rate-Setting Policy is attached as Appendix I.

## DISCUSSION

SCE is a municipally-owned utility and, as such, is exempt from the regulatory oversight of the British Columbia Utilities Commission (BCUC). Similar to the City's water, sewer, drainage and solid waste utilities, Council is tasked with the responsibility of regulating the pricing of services being delivered under the utility and ensuring that the public interest is served.

Where SCE differs from the City's other utilities is that it is a new utility providing a new service in the City, it is relatively complex and there are private utility operators who offer similar service under the regulation of BCUC. While the City is exempt from the regulatory oversight of BCUC, an external rate review panel is being established to assist Council in the oversight of SCE's rates and rate structure. The City of Vancouver has established such a panel as part of the DE utility that services development in their Southeast False Creek community and their experience has been that it is worthwhile.

### **Expert External Rate Review Panel**

It is recommended that the Panel be made up of 3 members appointed by Council, with one member being appointed as the Chair. The Panel members shall have expertise in the context of the Panel's responsibilities. The Panel will be tasked with providing objective expert advice to the City regarding the rates that should be charged by SCE in relation to the rate-setting principles for SCE established by City Policy.

To ensure a balanced review process the panel should be made up of individuals with a variety of expertise. Expertise in the following areas is considered desirable:

1. Utility Pricing and Regulation: Demonstrated expertise and experience in the area of utility finance/pricing, ideally with past experience working for or reporting to British Columbia Utilities Commission or another similar regulatory body;
2. Finance: A professional understanding with demonstrated expertise and experience in finance and financial modelling, ideally in the field of utility finance and pricing; and
3. Renewable, Low-Carbon Energy: Demonstrated expertise in the area of renewable energy production and demand management.

Each panel member should be able to carry out the work objectively, have the demonstrated ability to make complex decisions that equitably balance the interests of various stakeholders, and be perceived as a credible, objective expert by SCE stakeholders.

In the interest of avoiding any conflicts of interest, panel members shall not be:

- a) an employee of the City of Surrey;
- b) an elected official for the City of Surrey;
- c) a customer of SCE;
- d) an employee or major shareholder of an energy utility; or
- e) in any position or role that would be perceived as being in a conflict of interest in relation to the responsibilities described in these Terms of Reference.

### **Rate Review Process**

A full rate review will be conducted annually. The rate review process will include:

- The updating by City staff of the financial model for SCE including proposed rates, rate escalation factor and any other changes to the financial structure of SCE considered necessary by staff;

- The panel will review the updated financial model and the proposed rates and rate structure;
- The panel will prepare a report that either supports the rates and rate structure as proposed in the updated financial model or recommend revisions to the model and/or rates and/or the rate structure; and
- With the panel's report as background staff will prepare a report to Council recommending the financial model for SCE including any proposed rate or rate structure changes.

Through this process, SCE will be held to a high level of accountability in its rate structure and related reporting.

The panel's review will include consideration of the following factors:

- Long-term forecasted cost of inputs, including forecasted fuel costs and the utility's cost of capital, including debt charges and return on equity premiums;
- Revenue forecasts;
- Rate stabilization reserve requirements; and
- Comparisons of the rates and rate structure to other energy benchmarks.

### **Panel Review and Selection**

Staff issued a public Request for Expressions of Interest which concluded on May 5, 2014. In total 11 submissions were received. Based on the objectives of the Panel and based on the expressions of interest received it is recommended that the following individuals be appointed to the Panel:

- Robert Hobbs, LLB, MBA (as Chair);
- Alison Rhodes, LLB, MBA; and
- Michael Wilson, P.Eng.

A brief summary of each of the recommended appointees qualifications and experience is attached as Appendix II.

### **Panel Duration**

In an effort to have a broad and evolving range of experience on appointed panels, a common practice is to stagger the terms of appointments in the formative years of the panel, before commencing an annual rotation of one panel member. It is therefore recommended that the Chair be appointed for 3-years, and the other two members be appointed for 2-years.

At the end of the term of the two members initially appointed for 2-years, it is recommended that one new member be appointed for 2-years, and that all subsequent members are appointed for 3-years, thereby providing for an annual rotation of one panel member following the 3<sup>rd</sup> year of the utility's operation.

### **Panel Compensation**

Given the unique qualifications and experience of panel members it is recommended that a small honorarium be provided. It is recommended that the Chair be compensated \$3,000 per year, and the remaining members be compensated \$2,000 per year. This is consistent with the honorarium provided to members of the City of Vancouver's DE panel.

## **Next Steps**

SCE will be providing service to its 1st customer in the spring of 2015 and, as such, rates for 2015 are to be established by the end of 2014 or shortly thereafter. As such, the Panel will be convened in the coming months to commence their review and will be completed later this fall, and will include a report summarizing their opinion of the rates.

Following completion of the Panel report, staff will be meeting with a committee comprised of representatives of the Urban Development Institute and representatives of developers who have active development applications in each Service Area within the Surrey City Centre area in addition to the Development Advisory Committee in advance of bringing forward rates for Council's consideration.

## **Financial Services Review**

This report has been reviewed by the Finance & Technology Department.

## **SUSTAINABILITY CONSIDERATIONS**

The implementation of a DE system in the City Centre supports the Economic and Environmental Pillars of the City's Sustainability Charter under the following specific action items:

- EC8: Energy security by promoting the use of low-impact, renewable energy sources and promoting community energy solution;
- EN1: Energy efficiency by incorporating alternative energy systems such as geo-exchange and solar heating systems as potential heat sources; and
- EN10: Integrated Community Energy Master Plans by developing an Integrated Community Energy Master Plan for the City Centre and by working with property owners to promote and increase building energy efficiency through implementation of a DE system.

## **CONCLUSION**

Based on the above discussion, the Engineering Department recommends that Council:

- Appoint Robert Hobbs as the Chair of the Expert External Rate Review Panel for 3-years; and
- Appoint each of Alison Rhodes and Michael Wilson as members to the Expert External Rate Review Panel for 2-years.

Gerry McKinnon  
Acting General Manager, Engineering

VL/JA/JO/ras

Appendix I - City Policy No. H-53

Appendix II - Biographical Information on Recommended Panel Appointees



# City of Surrey Policy

APPENDIX I

No. H-53

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<b>Policy Title:</b>	<b>DISTRICT ENERGY (DE) RATE-SETTING POLICY</b>
<b>Approval Date:</b>	<b>2013 DEC 16 (RES. 13-2605)</b>
<b>History:</b>	<b>NEW</b>
<b>Department:</b>	<b>ENGINEERING FINANCE &amp; TECHNOLOGY</b>

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**TITLE: District Energy (DE) Rate-Setting Policy**

Utility rates for thermal energy provided by the City of Surrey (the “City”) are regulated under the District Energy System By-law, 2012, No. 17667, as amended. This policy forms the basis for the establishment and adjustment of the City’s thermal energy utility rates.

#### **EXPERT EXTERNAL RATE REVIEW PANEL**

The City will establish an Expert External Rate Review Panel (the “Panel”) in accordance with the Terms of Reference attached as Schedule 1 to this policy. Information on the District Energy Utility (the “Utility”) rates and rate structure is to be reviewed by the Panel who will provide objective, expert advice to the City to ensure that the rates and rate structure are consistent with the following principles.

#### **RATE STRUCTURE AND RATE-SETTING PRINCIPLES:**

**1. COST RECOVERY**

The cost-of-service model is the accounting structure that will be used to establish the rates and rate structure for the Utility and will take into account all costs associated with financing, operating, and administering the utility.

**2. RATE COMPETITIVENESS**

Rates will be established and maintained such that they are competitive with the costs that Utility customers would incur if they were using other thermal energy options that are available in the market, such as electricity and natural gas.

**3. RETURN ON INVESTMENT**

The rates over time will be set to include a rate of return on investment. In this regard, the rate of return on the City’s investment over time will be no less than the City’s cost of borrowing to finance the development of the Utility and no more than the rate of return established for private utilities regulated by the British Columbia Utilities Commission.

**4. *SHORTFALL RECOVERY***

If by virtue of the rates and rate structure that emanates from this policy, the Utility incurs a shortfall in any year including debt servicing, operations, administration and capital replacement, such a shortfall will be recognized as debt against the Utility and will be taken into account in relation to future rate adjustments.

**5. *LOW-CARBON / RENEWABLE ENERGY SOURCES***

The Utility will seek to maximize the proportion of low-carbon, renewable heat sources within its energy supply mix as early as possible while ensuring that the other rate-setting principles are respected.

**6. *FAIRNESS***

Utility rates will be structured such that the rates charged to different user types are fair and equitable. The Utility will not charge one user type a higher rate as a means to charge a different user type a lower rate that is not commensurate with the cost of providing utility service to that user type (i.e., cross-subsidization will not occur across user types).

# SCHEDULE 1

## Terms of Reference District Energy Utility Expert External Rate Review Panel DRAFT

### BACKGROUND

Surrey City Energy (SCE) is a municipally-owned utility and, as such, is exempt from the regulatory oversight of the British Columbia Utilities Commission (BCUC). Similar to the City's water, sewer, drainage and solid waste utilities, Council is tasked with the responsibility of regulating the pricing of services being delivered under the utility and ensuring that the public interest is served.

Where SCE differs from the City's other utilities is that it is a new utility providing a new service in the City, it is relatively complex and there are private utility operators who offer similar service under the regulation of BCUC.

While the City is exempt from the regulatory oversight of BCUC, an external rate review panel is being established to assist the City in the oversight of SCE's rates and rate structure.

### Expert Rate-Review Panel Structure

The Panel will be comprised of 4 members that are appointed by Council. Council will appoint one member as the Chair. The Panel will provide objective, expert advice to the City regarding SCE utility rate structure and rates consistent with the rate-setting principles articulated in this policy.

### SCOPE OF WORK

Staff proposes that a full rate review would be conducted once every 3 years or more frequently if the Panel deems such a more frequent review as being necessary. The rate review process will include:

1. The updating by City staff of the financial model for SCE including proposed rates, rate escalation factor and any other changes to the financial structure of SCE considered necessary by staff;
2. The Panel will review the updated financial model and the proposed rates and rate structure;
3. The Panel will prepare a report that either approves the revised rates and rate structure as proposed in the updated financial model or recommend revisions to the model and/or rates and/or the rate structure; and
4. With the Panel's report as background staff will prepare a report to Council recommending the financial model for SCE including any proposed rate or rate structure changes.

Through this process, SCE will be held to a high level of accountability in its stewardship of the utility and related reporting. The approval of the SCE rates and rate structure will be conducted in a fully transparent manner.

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The Panel's review will include consideration of the following factors:

- a) Long-term forecasted cost of inputs, including forecasted fuel costs and the utility's cost of capital, including debt charges and return on equity premiums;
- b) Revenue forecasts;
- c) Rate stabilization reserve requirements; and
- d) Comparisons of the rates and rate structure to other energy benchmarks.

### **PANEL EXPERTISE**

The Panel should have within its membership a variety of expertise to ensure a balanced review process. Expertise in the following areas is considered desirable:

1. Utility Pricing and Regulation: Demonstrated expertise and experience in the area of utility finance/pricing, ideally with past experience working for or reporting to British Columbia Utilities Commission or another similar regulatory body;
2. Finance: A professional understanding with demonstrated expertise and experience in finance and financial modelling, ideally in the field of utility finance and pricing; and
3. Renewable, Low-Carbon Energy: Demonstrated expertise in the area of renewable energy production and demand management.

Each Panel member should be able to carry out the work objectively, have the demonstrated ability to make complex decisions that equitably balance the interests of various stakeholders, and be perceived as a credible, objective expert by SCE stakeholders.

In the interest of avoiding any conflicts of interest, Panel members should not be:

- a) an employee of the City of Surrey;
- b) an elected official for the City of Surrey;
- c) a customer of SCE;
- d) an employee or major shareholder of a competing energy utility; or
- e) in any position or role that would be perceived as being in a conflict of interest in relation to the responsibilities described in these Terms of Reference.



## APPENDIX II

### **Biographical Information on Appointees to the District Energy System Utility (Surrey City Energy) Appointment of Expert External Rate Review Panel**

#### **Robert Hobbs, LLB, MBA**

Mr. Hobbs was previously a Vice-President with a utility, and was responsible for regulatory matters in both Alberta and British Columbia. Mr. Hobbs also served five years as chair and CEO of the British Columbia Utilities Commission (BCUC). Mr. Hobbs is considered as one of the foremost experts in utility regulation in the province, and is a leading lawyer in the area of energy regulatory law. He currently represents clients in matters before the BCUC.

#### **Alison Rhodes, LLB, MBA**

Ms. Rhodes has a Bachelor of Arts degree with a major in economics from UBC and a Law degree and MBA from the University of Western Ontario. Ms. Rhodes practiced law for 20 years in Vancouver, specializing in the defence of professionals. Most recently, Ms. Rhodes served under two three year Order-in-Council appointments with the BCUC. Ms. Rhodes chaired or was a member of numerous panels dealing with issues relating to utility applications for Certificates of Public Convenience and Necessity, revenue requirements, rate design, commercial disputes, service agreements and other issues. Ms. Rhodes is currently a member of a three person panel providing independent advice to the DE utility that services development in the City of Vancouver's Southeast False Creek community.

#### **Michael Wilson, P.Eng.**

Mr. Wilson is Principal of Enerficiency Consulting, providing consulting services in energy and greenhouse gas planning. He has been involved in energy management for over 25 years. Mr. Wilson's experience includes energy engineering, demand side management, and community energy planning for both municipalities and First Nations.

Mr. Wilson is a Professional Engineer with the Association of Professional Engineers and Geoscientists of British Columbia and a LEED Accredited Professional.