

Business 478

Section D200

Case Synopsis for FortisBC



Heather Sanford

Jane Kuang

Victor Siu

November 6, 2013

BACKGROUND

FortisBC is a British Columbian electric power and gas distribution company, indirectly wholly owned by Newfoundland-based Fortis Inc. In 2004, Fortis Inc. began their operations in British Columbia by acquiring all distribution, transmission, and generation assets of the West Kootenay Power and Light Company, and renamed it FortisBC. In 2007, Fortis Inc. acquired Terasen Gas, a major natural gas distributor and emerging leader in alternative energy production. In 2010, FortisBC and Terasen Gas began sharing the same leadership team, and the two divisions began operating under the FortisBC brand name in 2011.

COMPANY TODAY

Today with over 2,200 employees, the two FortisBC divisions (electricity and natural gas) together produce over 21% of the total energy consumed in British Columbia. Their core business services, electricity and natural gas transmission and distribution, provide energy to over 1.1 million customers in over 135 communities, as exemplified in Figure 1. FortisBC has operated and maintained hydroelectric power plants in British Columbia for the past 100 years. Their four hydroelectric plants are situated on the Kootenay River. The proposed construction of a fifth hydroelectric plant on the endangered Similkameen River is currently facing considerable criticism from conservation and Aboriginal groups.

In addition to its core business services, FortisBC provides alternative energy services, such as geexchange systems for heating and cooling, and district energy systems serving entire communities with sustainable energy sources. They also produce locally sourced renewable gas made from landfill and agricultural wastes. Their current projects include research in bioenergy production, and developing energy solutions for remote communities.

Their 2012 financial results report a net income of \$49 million from the electricity division, an increase from the previous year's \$48 million, and \$138 million net income from gas operations, an increase from the previous years \$137 million (FortisBC, 2013a).

GOALS AND OBJECTIVES

FortisBC's organizational goals and objectives include (1) addressing the social, economic, and cultural interests of First Nation communities, (2) fostering community growth, (3) promoting electric and natural gas health and safety awareness, (4) minimizing the environmental impact of its operations, and (5) promoting healthy work-life balance for their employees.

GENERAL ENVIRONMENT

While there are a number of environmental factors that have the potential to affect FortisBC, there is three of primary concern: political, economic, and socio-cultural.

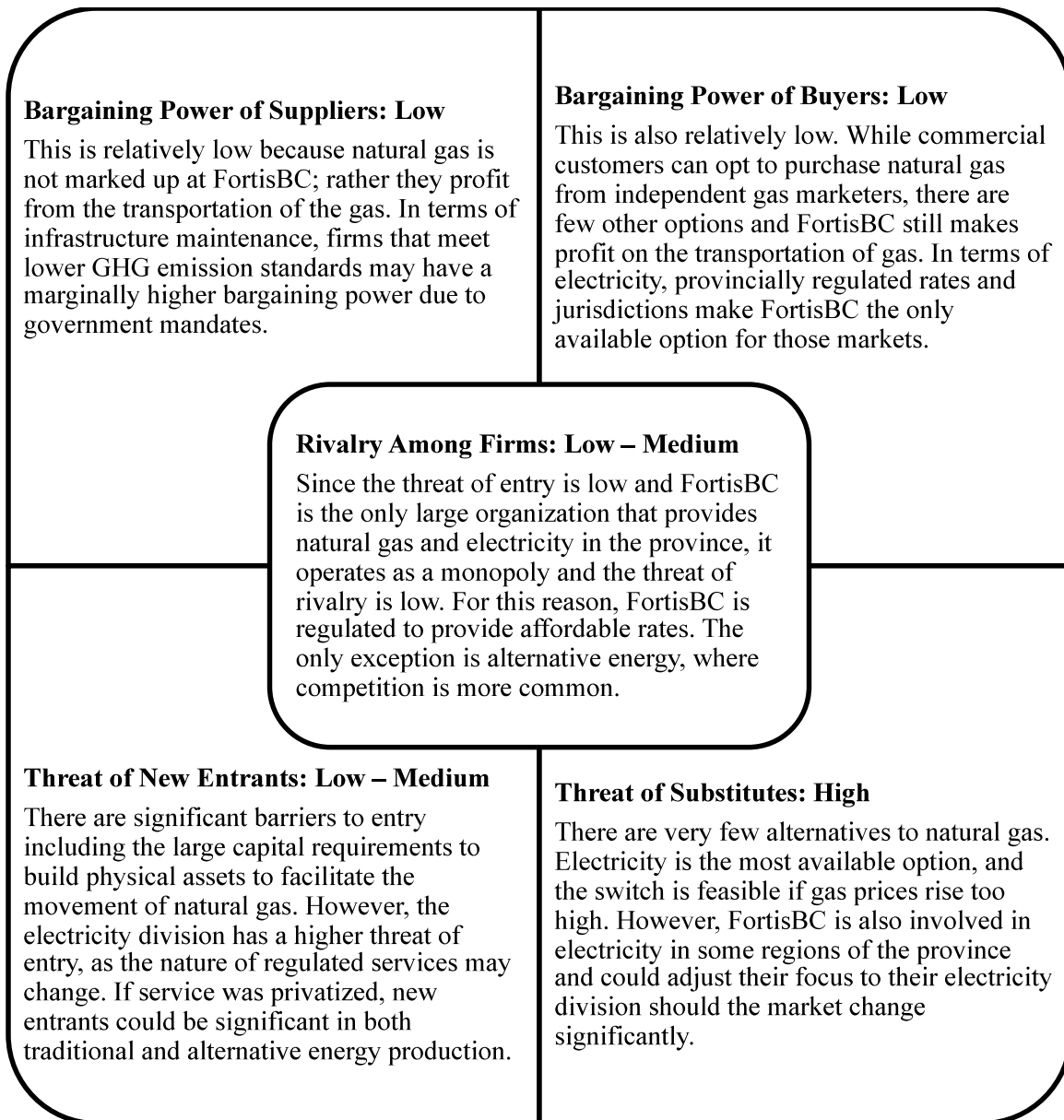
Political: The political segment is important to consider for FortisBC – they rely on the British Columbia Utilities Commission (BCUC), which provides a framework for rates, service, and performance-based regulation for gas and electricity. This commission is an independent regulatory agency, which operates under the British Columbian government, and is therefore influenced by political decisions and changes.

Economic: The economy has the potential to affect FortisBC – particularly as the Canadian and US natural gas market operate as one large integrated market. Given economic concerns for both countries, and the historical volatility of the natural gas market that is influenced by the economy, this creates risk (National Energy Board, 2013). End users tend to be protected from this volatility through regulation and through the overall cost of the supplier's portfolio, which puts the risk on the supplier – FortisBC. The economy would also likely affect tax rates and the end-users sensitivity to price.

Socio-cultural: British Columbia is viewed as a benchmark for sustainability and environmental concern. The recent public outcry concerning pipeline expansion in the province is an example of this trend. This has the potential to affect both expansion and existing operations if FortisBC does not monitor its reputation and maintain its community and stakeholder involvement.

INDUSTRY ENVIRONMENT

Porter's Five Forces Analysis applied to FortisBC:



COMPETITIVE ENVIRONMENT

FortisBC is the largest supplier of natural gas in British Columbia. Because of regulation and their significant existing infrastructure, they essentially operate as a monopoly with only a handful of other firms supplying similar services in British Columbia on a much smaller scale. However, the competitive environment has the potential to change as technology and energy

priorities shift over the coming years. The political environment has the capacity to change regulatory policy. In particular, the privatization of energy can affect the organization's electricity production and distribution, as new organizations enter the market and pricing changes. However, because FortisBC distributes natural gas and electricity through an established network of pipelines that represent significant capital, the deregulation of natural gas prices will likely have little effect on new entrants. Instead, this may create an environment in which consumers opt to switch from gas to electricity due to price fluctuations. This threat of substitution makes BC Hydro a significant threat.

The alternative energy sector also provides strict competition as sustainable energy solutions gain popularity. This popularity results from British Columbia's aggressive climate change and energy policies, which support innovation through funding programs, such as the Innovative Clean Energy Fund. Carbon taxing also promotes growth in the industry.

MAIN STRATEGIC CHALLENGES

Maintain Profitability with a Cost-Leadership Strategy

FortisBC focuses on providing high-quality energy products at low costs, and has become the largest energy distributor in BC. They focus their resources on cost control and reduction. However, this strategy can be effective only when the company can remain positioned as a price leader in the industry. FortisBC is more likely to attract buyers based on low cost, rather than loyalty. If regulations change and electricity becomes a cheaper option, FortisBC's gas division may face trouble. Additionally, to limit the use of fossil fuels and their GHG emissions, the BC government implemented a carbon tax on fossil-based fuels for end-users in 2008 (Ministry of Environment, 2012). With annual increases, the tax for natural gas reached 5.70 cents per cubic meter last year (Province of British Columbia, 2013). This tax raises the cost of natural gas, which consequently increases the risk of switching to substitutes.

Uncertainty of Delivery Charges and Energy Pricing

The distribution and transmission rates are set annually and differ between the three customer groups (residential, commercial, and industrial). Normally, the more energy consumed, the less expensive the unit price (see Appendix Figure 3). Therefore, the commercial and industrial consumers receive greater discounts than residential users. Moreover, FortisBC has regional gas price discrepancies due to localized charges and service rates (FortisBC, 2013b). For example, FortisBC's natural gas division has three subsidiaries: FortisBC Energy Inc., FortisBC Energy Vancouver Island Inc., and FortisBC Whistler Inc. The FortisBC Energy Inc. is divided further into four areas and has set different rates for each of the regions. The resulting complicated price system leads to pricing issues. Although FortisBC has established the Customer Price Stability Fund and the Price Risk Management Plan to reduce the negative impact of price fluctuations, these plans were not approved by the BCUC in 2011 due to the lack of a formal price risk management system and high natural gas price volatility (BCUC, 2011).

Environmental Impact and Conservation Concerns

The BC government set GHG reduction goals in 2010 in response to climate change concerns. Since then, GHG emissions have decreased from 2001 to 2010, from 68,000 kilotons to 62,000 kilotons of carbon dioxide (see Appendix Figure 2). In 2010, the transportation sector contributed to the largest proportion of GHG emissions in BC at 38.4%. Compared with traditional gasoline and diesel-based transportation systems, a natural gas-based system can reduce GHG emissions by at least 20%. However, since natural gas use in the transportation sector requires significant resources in terms of both knowledge and facilities, FortisBC faces a challenge in switching the conventional channels to the new transportation infrastructure.

Recent plans to construct the Similkameen River hydroelectric plant have also raised immediate concern from conservation and Aboriginal groups. Given this and the strong overall environmental focus in British Columbia, stakeholder engagement and communication will prove key in managing the challenges that these concerns pose for new projects moving forward.

APPENDIX

Figure 1:

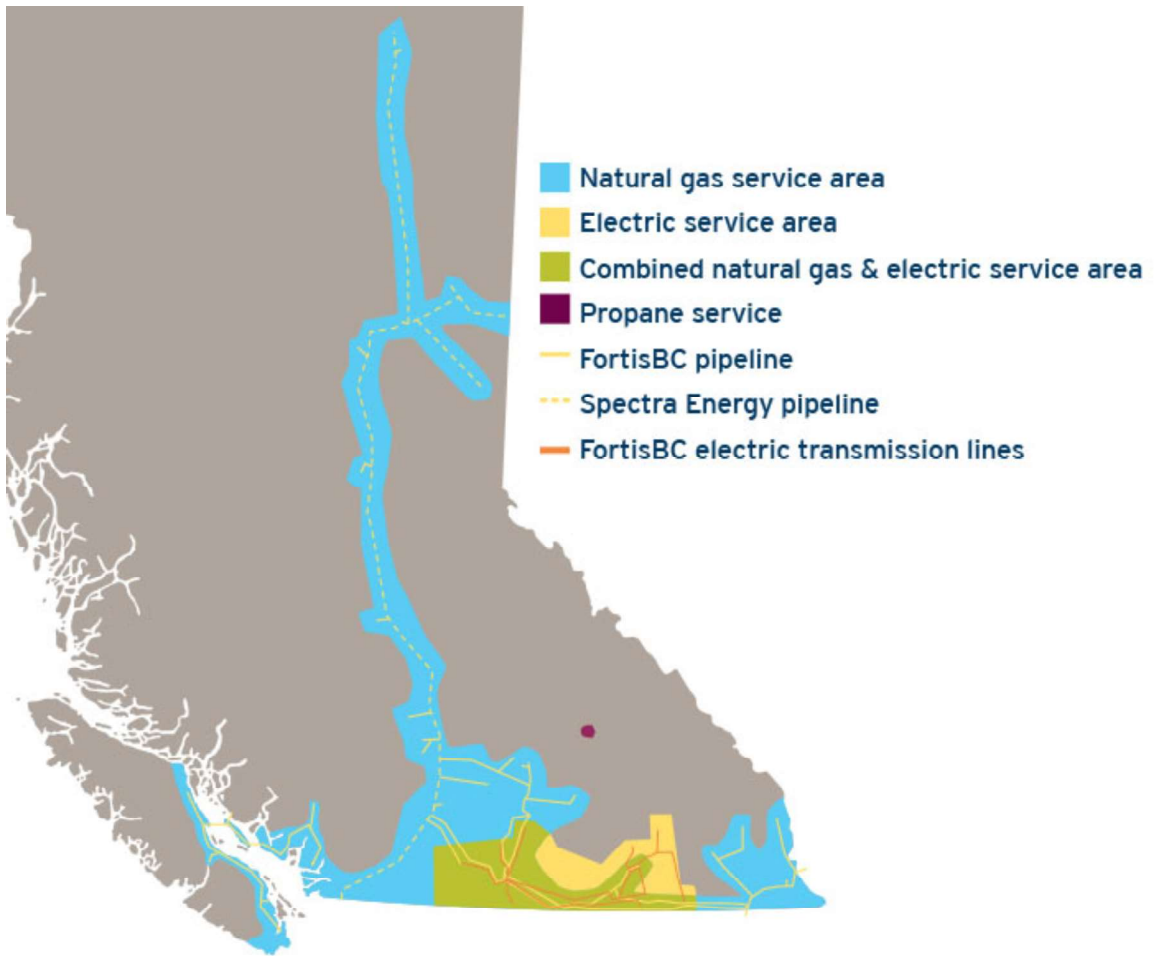


Figure 2:

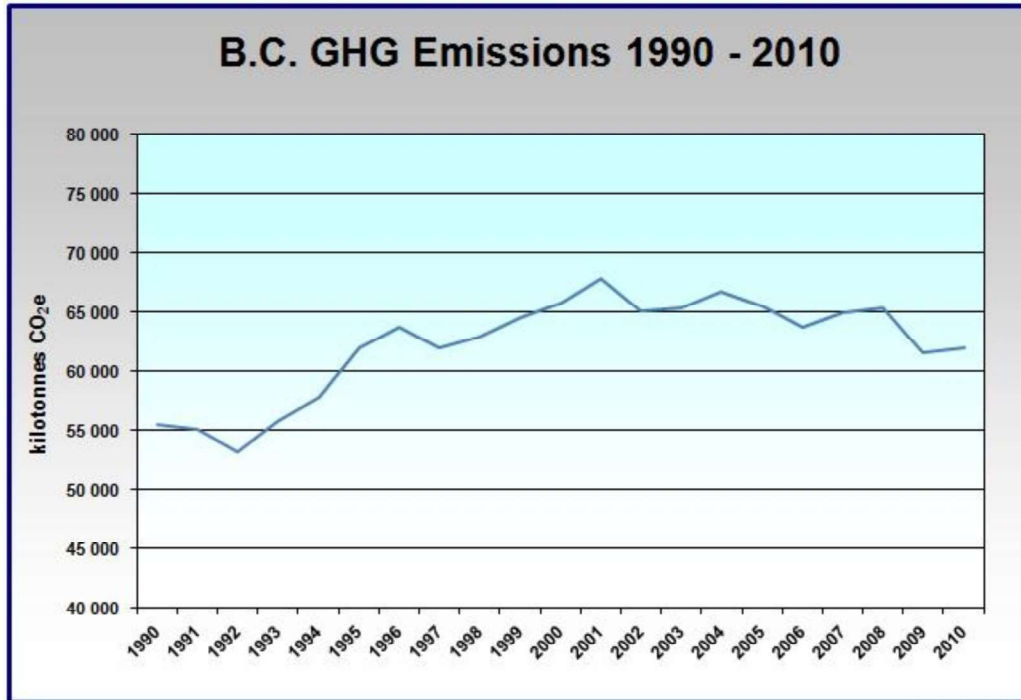
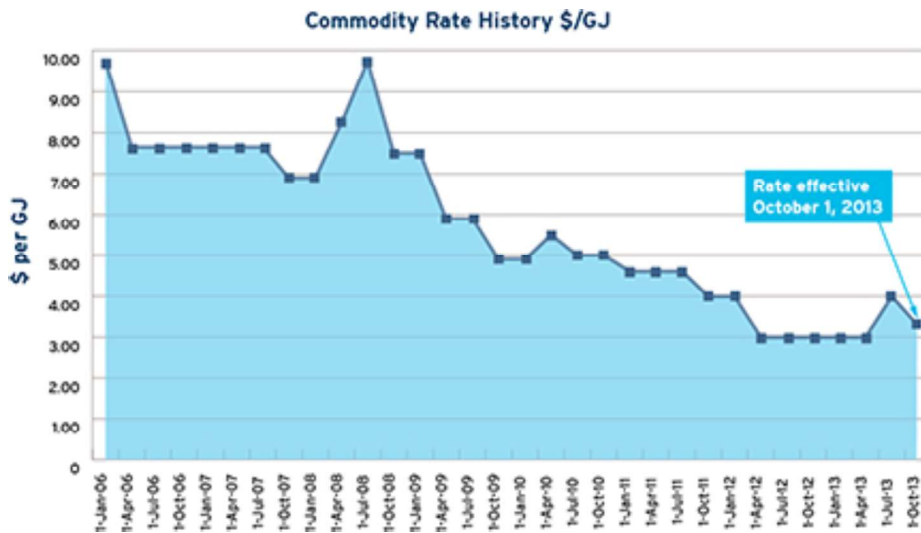


Figure 3:



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