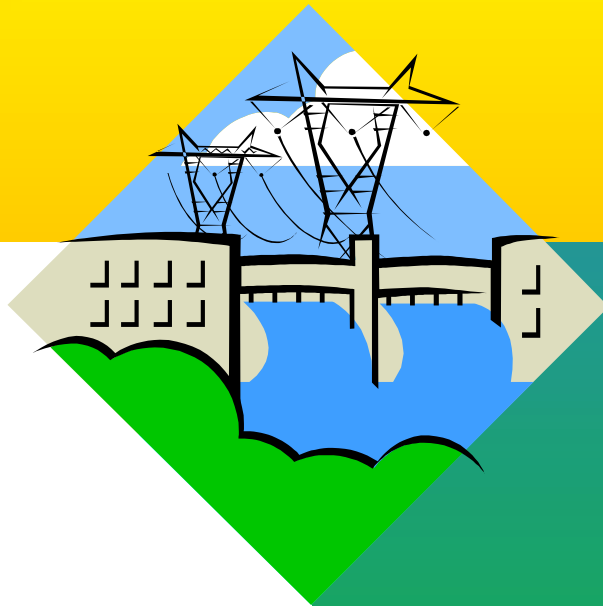


A NEW ERA OF PROSPERITY THROUGH POWER



***“Maintaining BC’s
Competitive Advantage”***

August 17, 2001



Joint Industry Electricity Steering Committee

BACKGROUND

The Joint Industry Electricity Steering Committee (JIESC) represents the major industrial users of purchased electric power in the manufacturing of pulp and paper, mining and processing, and industrial chemical production in British Columbia.

Each member company is listed below and collectively represents the direct employment of more than 17,000. On their behalf, the work of the JIESC includes:

- extensive contact with BC Hydro,
- active involvement in the proceedings of the BC Utilities Commission and government relations, and
- building public support for lower cost electric power.

The Council of Forest Industries provides the secretariat and administration of the JIESC. Current members include:

Abitibi Consolidated Inc.	Pope & Talbot Ltd.
B.C. Chemicals	Quesnel River Pulp Co.
Boliden Westmin Resources	Quinsam Coal Corp.
Canadian Forest Products Ltd.	Scott Paper Ltd.
Cariboo Pulp & Paper Co.	Skeena Cellulose Inc.
Celgar Pulp Co.	Sterling Pulp Chemicals
Council of Forest Industries	Teck Cominco Ltd.
Fording Coal Ltd.	Tembec Industries Inc.
Graymont Lime Ltd.	Texada Quarrying Ltd.
Highland Valley Copper	The Mining Association of B.C.
Homestake Canada Inc.	Thompson Creek Mining
Howe Sound Pulp & Paper	West Fraser Timber Co. Ltd.
Imperial Metals Corp.	Western Industrial Clay Products Ltd.
Luscar Ltd.	Westroc Inc.
Nexen Chemicals	Weyerhaeuser Company Ltd.
Norske Skog Canada Ltd.	Wheaton River Minerals Ltd.
Pacifica Papers Inc.	

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A NEW ERA OF PROSPERITY THROUGH POWER

"Maintaining BC's Competitive Advantage"

INTRODUCTION

For decades a major driving force behind British Columbia's economic growth and development has been the availability of abundant low cost electric power.

The creation of BC Hydro and the building of its electric power generation system in the 1960's gave BC industry a competitive advantage and helped to attract new investment throughout the 1970's and 1980's.

However in the 1980's, the provincial government increasingly viewed BC Hydro as an easy source of revenue. If this situation is allowed to persist, the long term value of BC Hydro as a vehicle for future growth and prosperity will diminish.

JIESC's PRINCIPAL GOAL:

Make Electric Power a Competitive Advantage in BC

It is the recommendation of the Joint Industry Electricity Steering Committee (JIESC) that government energy policy be focused on maintaining BC's competitive advantage through the delivery of low cost electrical power to businesses and residents.

RATIONALE

Purchased electricity accounts for between 5% and 25% of variable costs for mining and forestry operations, ranking in importance just behind raw materials and labour costs. For electrochemical companies, energy purchases can represent up to 75% of operating costs.

BC's inherently low cost power resources can create a natural competitive economic advantage for the Province. Power is one of the few potential major competitive advantages we have for industry. By comparison forestry and mining in British Columbia have relatively high raw materials, labour and transportation costs.



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Energy competitiveness is essential to industry and has a significant impact on operating and investment decisions. A reliable long-term supply of low cost power is a key consideration in choosing a site for the establishment or expansion of major industrial developments. When an important component of production comes with a competitive advantage, it creates direct economic opportunities and related indirect and induced economic benefits. The essential issue is how BC can maximize this advantage today, ensure it continues in the future and provide flexibility for change.

If properly managed and appropriately priced, electricity as a publicly owned resource can create a substantial competitive advantage for business in British Columbia. Unfortunately power is not nearly the advantage it could be for the province. BC can create a meaningful economic advantage in electricity, but only if our existing power resources are operated efficiently and priced at or close to cost.

JOINT INDUSTRY ELECTRICITY STEERING COMMITTEE

The Joint Industry Electricity Steering Committee (JIESC) was formed in the early 1980's shortly after BC Hydro became regulated by the BC Utilities Commission (BCUC). The principal purpose of the JIESC was originally to coordinate and consolidate industries' efforts before the BCUC to maintain reasonable cost based rates under BCUC regulation. Through the years it became apparent that maintaining low rates is a public issue requiring input at additional governmental forums if the JIESC is to be successful. With government adding revenue requirements in various forms to BC Hydro's "costs", a voice in these decisions became more important than the BCUC regulatory proceedings.

The major industry sectors represented by the JIESC include pulp and paper, mining, and electrochemicals. These industries are dependent on low cost electric power for their very existence. As illustrated in Chart 1., prices for the commodities produced by JIESC member firms have not increased in line with the cost of electric power in BC. Therefore, power costs in BC have accounted for an increasing share of the value of industrial production over the past two decades. Many of the JIESC members would be unable to maintain operations in BC if electric power prices reached the levels recently seen in Alberta and the US west.

The mining sector requires electric power for material handling, size reduction, and pumping and processing. Typical power cost in a copper mine and concentrator would be 9¢ per pound. This represents 14% of the typical production cost in BC.

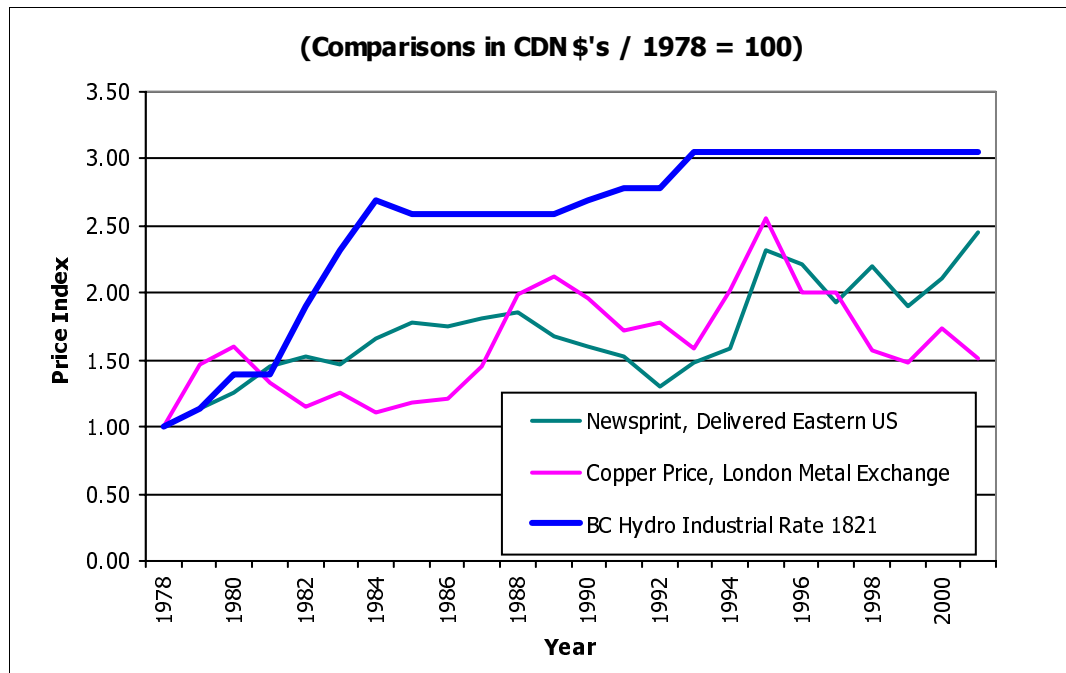
In the pulp and paper sector, power consumption varies greatly with product line. Bleached and unbleached kraft pulp products are less power intensive and also have a greater opportunity for internal cogeneration than newsprint and BCTMP. The power intensive grades, newsprint and BCTMP, represent about 40% of BC pulp and paper production. Electrical power consumption for these grades is typically 2,500 kwh per tonne. At current power and exchange rates, the cost of this power in BC is about \$90 per tonne and 20% of the production cost of newsprint produced in BC.

The sector which is most dependent on electric power is electrochemicals, with BC producers spending as much as 75% of production costs on purchased electric power.

For these sectors of BC's economy the current and, particularly, expected future costs of electric power greatly influence investment plans for expanded production and future growth.



**Chart 1. Comparison of Commodity Price Indexes
Newsprint, Copper, Electric Power - 1978 - 2001**



CONSIDERATIONS

FUTURE CAPACITY

There is concern among industrials over BC Hydro’s ability to meet future demands for the delivery of low cost power. According to BC Hydro’s February 2000 Integrated Electricity Plan (IEP), at current growth projections, we will reach BC Hydro’s existing and committed resource capacity in 2007. This assumes that the demand for electricity in BC will increase 18% within ten years. Higher demand growth rates will see us reaching capacity as early as 2005 or perhaps sooner. Once capacity is reached, BC Hydro will have to purchase market power or develop domestic capacity. New supply sources will likely be more expensive than existing capacity and consequently push costs higher.

One of the key conclusions of Hydro’s IEP is that the next major resource to be added around 2007 is likely to be a 640 MW natural gas-fired combined cycle gas turbine (CCGT) on Vancouver Island. This would be driven by the need to retire aging components of Hydro’s Vancouver Island/Mainland HVDC transmission system. However, it is not clear that this would be a prudent decision, in view of the associated natural gas price risk exposure which would ultimately be reflected in power rates. Large-scale hydroelectric projects and alternative major thermal projects, while involving higher capital costs, may offer a better option for minimizing total costs over the long run. BC Hydro needs to actively maintain and fully assess options such as the Peace River Site C project and Hat Creek coal development among others. Assigning the Columbia River downstream benefits (DSB) to BC Hydro is another acquisition option that should be considered. A diversified resource acquisition strategy is fundamental to providing low cost stable rates.



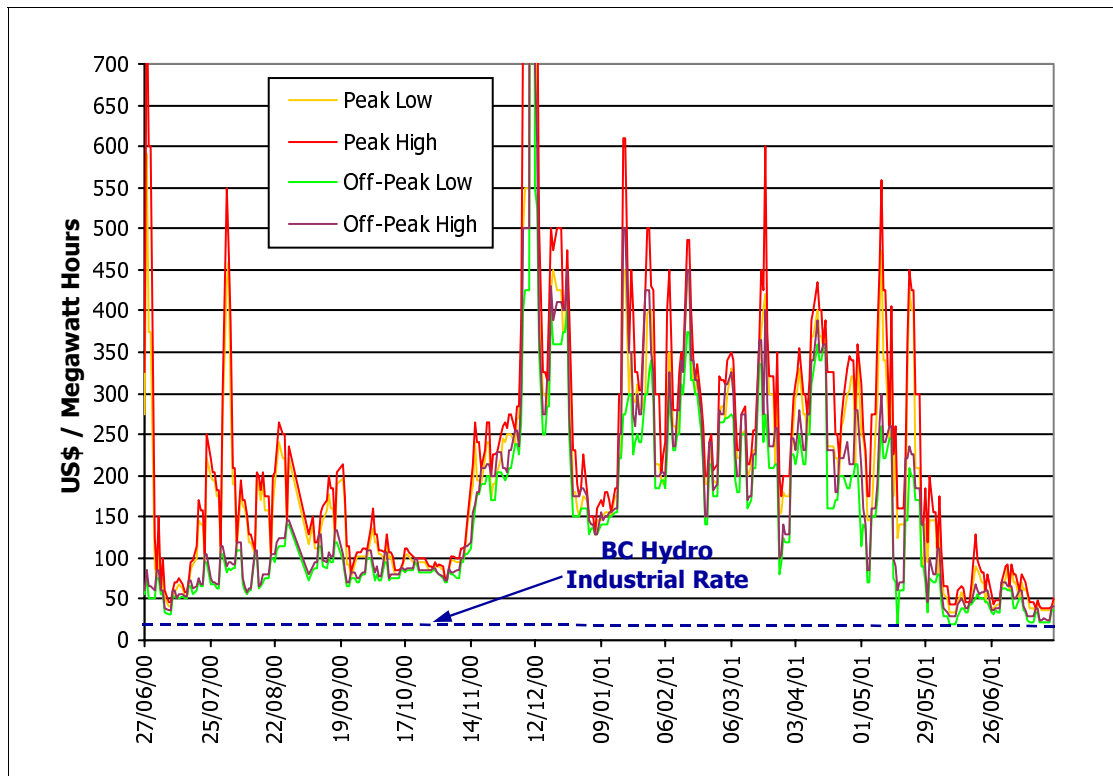
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To help meet the increase in demand, BC Hydro has examined various resource options including the CCGT, large and small hydroelectric, market purchases and wood-waste. Primarily for competitive commercial reasons, resource costs are described by BC Hydro in its IEP only by a qualitative ranking of these options. BC Hydro's plans for acquiring new resources and its evaluation of resource alternatives to supply electricity in the future should come under closer public review and scrutiny. This includes the opportunities to advance acquisition of new resources ahead of domestic requirements if there are associated economic benefits.

LESSONS FROM OTHER JURISDICTIONS

New electricity market structures have recently been introduced in other jurisdictions, including California and Alberta. This involved moving from a traditional regulated electricity market toward a competitive market and an open-access transmission system. The experience of these jurisdictions clearly indicates the difficulty of introducing a workably competitive market in electricity for various technical and economic reasons. The extraordinary power prices and volatility recently experienced in the US west (Chart 2.) and the associated economic and social impact have been well publicized.

Chart 2. Mid-Columbia Electric Power Prices



Numerous recent examples can be cited where industrial operations have closed or relocated and new opportunities have not materialized because of power prices. This includes markets adjacent to British Columbia in the US Pacific northwest, California and Alberta. For example, the aluminium industry in the Pacific northwest has essentially been completely shut down for an extended period as a result of power prices.



Shifting of production from Alberta is occurring (e.g. Lafarge Cement announced a shift to Richmond, BC earlier this year) and complete plant shut downs are under evaluation. Estimates of the Alberta industrial load currently at risk due to shutdown or closure owing to power prices are in the 400 MW range. Many of these firms now face purchasing from the power pool at unpredictable spot prices.

BC is in a strong position to distinguish itself from these and other jurisdictions, and offer an attractive environment in which to invest and operate. By ensuring power rates are cost based, stable and predictable – not subject to non-cost related market fluctuations – British Columbia can offer business much less risk and uncertainty over the cost of a key factor of production.

SPECIFIC RECOMMENDATIONS

To turn BC's economy around and re-establish the province as a leading economy in Canada, we set forth the following short term and long term recommendations:

SHORT TERM

- 1.** Articulate an unequivocal commitment to the maintenance of an ample supply of low cost power for the foreseeable future.
- 2.** Remove the PST on the purchase of electric power used for manufacturing and processing, as BC is the only province in Canada with such a tax.
- 3.** Extend the current rate freeze until a thorough review of BC Hydro revenue requirements can be completed before considering any revision to BC Hydro rates.
- 4.** Initiate a long-term resource acquisition and transmission expansion strategy that will assure the availability of ample supplies of low cost power, provide opportunities for private sector participation and establish a diversified portfolio of generating resources.

LONG TERM

1. Maintain Regulated, Cost Based Rates

BC Hydro should be regulated by the BC Utilities Commission based on the principle of cost based rates, as was the case prior to special directives 2 and 8.

To ease public concerns and to ensure stability and certainty regarding the immediate future, it is our recommendation to continue the current rate freeze until BC Hydro updates its integrated resource plan and the provincial government establishes new policy directives to guide BC Hydro and enhance its operating efficiency.

2. Develop Ample Low Cost Power

BC has the resources to maintain an ample supply of electric power for domestic requirements. Additional resources must be developed in a timely fashion to assure the ability to meet power needs at



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reasonable prices. The provincial government, through BC Hydro, should add major low cost electric power sources to meet domestic needs as BC's population and economy resume normal growth.

3. Utilize Downstream Benefits

The Columbia River Treaty downstream benefits (DSB), which began to revert to BC in 1998, were earned through the construction and operation of dams in British Columbia. This power supply is currently about 800 MW and by 2003 there will be up to 1,200 MW of capacity and 4,300 GWH of energy – equal to more than four years of normal load growth for BC Hydro – available annually from the DSB until 2024.

The downstream benefits belong to British Columbia and agreements have been reached with US authorities that give BC free return of the DSB over existing transmission lines. The DSB surplus to BC's needs are being marketed in the US by Powerex on behalf of the province and are available to BC Hydro at "market prices". Accordingly under current arrangements, the DSB represent a source of supply similar to other market purchases that is available to BC Hydro to purchase for delivery in BC.

Rates for electric power from BC Hydro have included a return on the investment in the dams providing the downstream benefits. The JIESC and other customers maintain that they have paid for these benefits and, therefore, are entitled to the return of these benefits directly to the BC Hydro system.

Maintaining an adequate power supply and low rates will eventually require BC Hydro to develop additional resources. To ensure that BC Hydro is able to continue to meet current demand and pay for the expanded capacity needed to meet future demand, the DSB should be considered part of BC Hydro's resource base and made available to support domestic customers in a fashion similar to existing generation resources.

4. Provide a Role for the Private Sector

The competitive power cost advantage which BC has will be eroded unless the new generation resources BC Hydro will eventually need to acquire are the most economic available and take into account essential environmental and other considerations. Normally in the case of a monopoly, ratepayers are assured that good decisions are being made through a transparent planning process or through competitive market acquisitions. It is not clear that we currently have either in British Columbia.

To ensure that BC Hydro is acquiring resources efficiently, BC Hydro should introduce an open competitive process for new generation requirements which would ensure that BC Hydro resources would be developed only if they are the most economic alternative available. To do this, British Columbia should make BC Hydro resource acquisition decisions timely, fully competitive, public and transparent.

5. Maintain Adequate Transmission Facilities

Additional transmission facilities should be built to provide service or, where justified, to access low cost supplies or profitable trading opportunities for BC Hydro and Powerex. Providing reliable long term service to Vancouver Island likely requires a major upgrade of the marine transmission system from the mainland. Northwest BC and the major north-south transmission corridor will require further expansion to facilitate economic growth and the development of additional sources of generation.



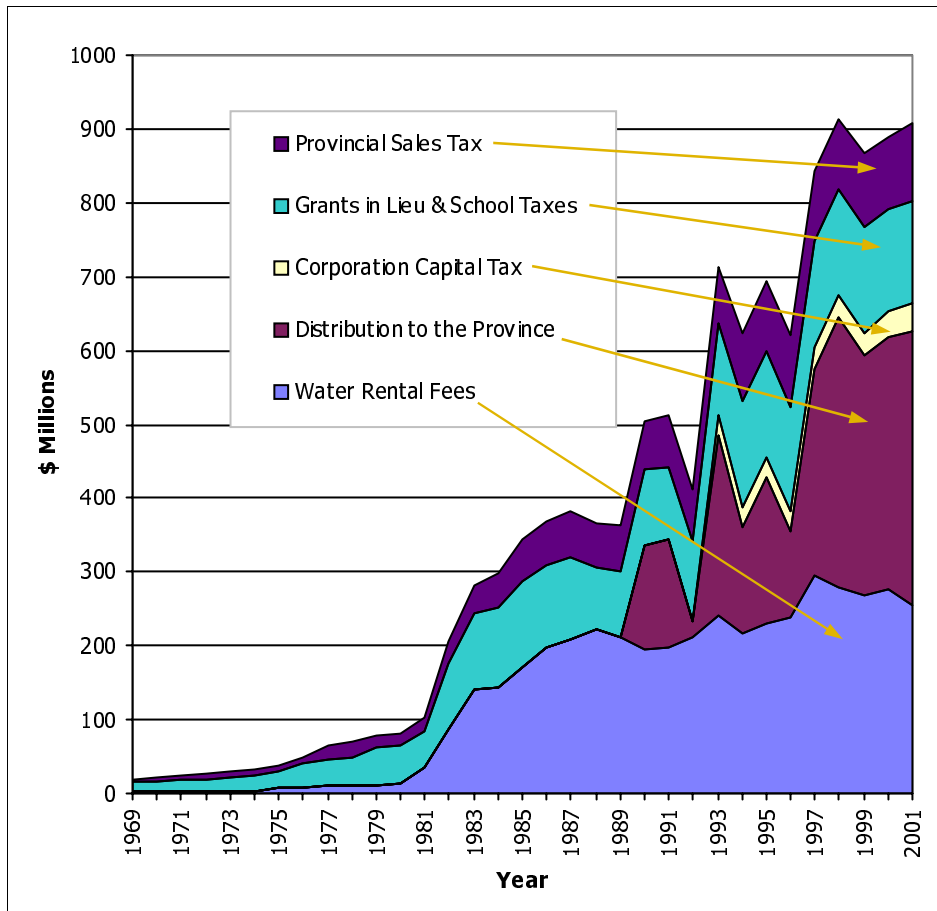
6. Reduce Government Revenues

Through water rentals, payments in lieu of taxes, dividends, etc., BC Hydro contributes about \$900 million to government revenues. (Chart 3.) This amount is double the level of contribution in 1990 and has grown very rapidly in recent years. It is time this trend is reversed.

There is room to object to the excessiveness of the amounts being transferred with respect to any of the revenue components. However, there is one element in particular that is so far out of line, it should be corrected immediately. That is, BC Hydro's net income of \$400 million which drives the provincial dividend. This level of income is a direct result of BC Hydro's legislated extraordinary return on equity.

BC Hydro's return on equity, calculated in accordance with special legislation, is in the range of 17%. However, this calculated return is misleading because it includes earning a return on capital costs paid by customers. For example, BC Hydro "earns" a return on customers' contributions in aid of construction. When BC Hydro's after-tax return on equity is calculated in a manner similar to that used for other utilities, its return on shareholder's equity jumps from a very high 17% to the extraordinary level of about 30%. Other comparable utilities earn around 10% on equity after tax. By comparison over the last 10 years, BC's forest and mining industries have earned about 5% on shareholders' equity.

Chart 3. BC Hydro Payments to the Province



7. Instill Customer Driven Management

Customer Focus

The focus of BC Hydro management is primarily on the needs of its owner, not its customers. Despite repeated attempts by industrial customers to develop alternative rates and services that would be mutually beneficial, the lack of support from BC Hydro has resulted in minimal progress.

BC Hydro Mandate

BC Hydro's mandate from the previous government was confused and included many socio-economic and environmental objectives outside the normal role for a utility. The focus of this organization needs to be clear and greater emphasis placed on the objective of efficiently delivering low cost, reliable, electric power to consumers in BC. Where opportunities exist in external markets, the returns from serving those markets should reduce the cost of power for BC consumers.

BC Utilities Commission

In order to change BC Hydro to a customer driven focus, the capacity of the BCUC must be expanded to provide appropriate regulation. Additional expertise and leadership is required for this organization to effectively serve the interests of electric power consumers.

Industry Restructuring

There may be alternative ways to restructure the industry in BC that would introduce competition and incentives for further efficiencies in the operations of this industry. Any major change must also recognize BC's unique situation and clearly provide advantages over the current system before being given serious consideration.

POTENTIAL RESULTS

A new electricity policy for British Columbia, one that is focused on making electrical power at a competitive advantage for BC businesses, will have a positive and profound long term effect on economic growth and development. Such a policy will generate substantial additional income and employment, attract investment, provide tax revenue and, in doing so, secure the future of our public services.

**British Columbia can have it all:
Lower and More Competitive Rates
Competitive Market for Additional Power Requirements
Fair and Reasonable Return to BC Hydro and the Province**



JIESC MEMBER COMPANIES

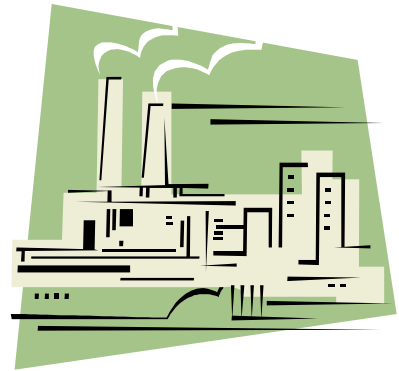
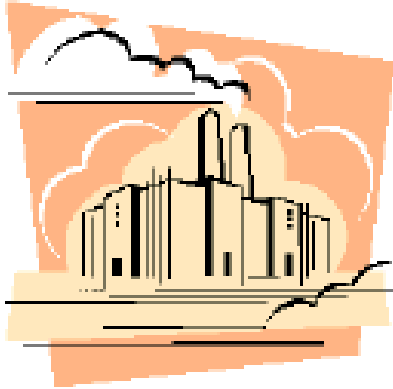
Number of Employees—2000

Committee Members	Operations	Number of Employees 2000
FORESTRY COMPANIES:		
Abitibi Consolidated Inc.	Mackenzie	258
Canadian Forest Products Ltd.	3 locations, Prince George	1,342
Cariboo Pulp & Paper Co.	Quesnel	390
Celgar Pulp Co.	Castlegar	431
Howe Sound Pulp & Paper	Port Mellon	685
Norske Skog Canada Ltd.	2 locations, Elk Falls, Crofton	2,500
Pacifica Papers Inc.	2 locations, Port Alberni, Powell River	*2,000
Pope & Talbot Ltd.	2 locations, Nanaimo, Mackenzie	785
Quesnel River Pulp Co.	Quesnel	144
Scott Paper Ltd.	New Westminster	658
Skeena Cellulose Inc.	Prince Rupert	660
Tembec Industries Inc.	Skookumchuck	313
West Fraser Timber Co. Ltd.	Kitimat	600
Weyerhaeuser Company Ltd.	Kamloops	540
ELECTROCHEMICAL COMPANIES:		
B.C. Chemicals	Prince George	30
Nexen Chemicals	2 locations, Vancouver, Nanaimo	201
Sterling Pulp Chemicals Ltd.	Vancouver	35
MINING COMPANIES:		
Boliden Westmin Resources	Myra Falls	432
Fording Coal Ltd.	3 locations, Coal Mountain, Fording River, Greenhills	1,269
Graymont Lime Ltd.	Pavillion	30
Highland Valley Copper	Logan Lake	952
Homestake Canada Inc.	Eskay Creek	120
Imperial Metals Corp.	2 locations, Huckleberry, Mount Polley	417
Luscar Ltd.	Line Creek	401
Quinsam Coal Corp.	Vancouver Island	39
Teck Cominco Ltd.	3 locations, Bullmoose, Elkview, Quintette, Sullivan	1,512
Texada Quarrying Ltd.	Texada Island	25
Thompson Creek Mining	Endako	225
Western Industrial Clay Prod.	Kamloops	32
Westroc Inc.	Annacis Island	25
Wheaton River Minerals Ltd.	Golden Bear	71
Total Employees		<hr/> 17,122 <hr/>

* COFI estimate



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We thank you for your interest.

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**Joint Industry Electricity
Steering Committee**

August 17, 2001