

IN THE MATTER OF
the Utilities Commission Act,
S.B.C. 1980, c. 60, as amended

and

IN THE MATTER OF
an Application by
Inland Natural Gas Co. Ltd.

DECISION

June 17, 1987

Before:

M. Taylor, Chairman
J.D.V. Newlands, Deputy Chairman
N. Martin, Commissioner

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ALLWEST REPORTING LTD.	Court Reporters

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1.0 BACKGROUND

The background to the Inland Natural Gas Co. Ltd. ("Inland", "Applicant") Application spans two years since the first government announcement that a competitive market for natural gas sales would develop in British Columbia. Prior to the summer of 1985, all natural gas producers in British Columbia sold their gas to the British Columbia Petroleum Corporation ("BCPC"). The Corporation in turn sold gas to Westcoast Transmission Company Limited ("Westcoast") for delivery to distributor utilities in British Columbia and for export to the United States. On March 28, 1985, the Governments of Canada, British Columbia, Alberta and Saskatchewan entered into an Agreement, commonly known as the Western Accord. The Western Accord initiated a process of replacing government-set prices of oil and natural gas with prices set by the market. The Natural Gas Price Act was proclaimed in British Columbia effective July 1, 1985. This Act provided sweeping changes to the marketing system for natural gas within British Columbia, and along with revisions to the Petroleum and Natural Gas Act, established a new royalty system and authorized producers to sell their natural gas to customers other than BCPC.

In late October 1985, an agreement was struck between the Governments of Canada, British Columbia, Alberta and Saskatchewan on Natural Gas Markets and Prices. This Agreement reinforced the earlier provincial initiatives by signalling the governments' intent that immediate steps be taken to enable consumers to enter into supply arrangements with producers at negotiated prices. The agreement fosters a competitive market for natural gas in Canada.

As part of the Agreement on Natural Gas Markets and Prices, the Government of Canada established a Pipeline Review Panel to undertake an all-encompassing review of the role and operations of interprovincial and international pipelines engaged in the buying, selling and transmission of gas. The Pipeline Review Panel issued its report in June 1986. The report sets out the Panel's views on many aspects of interprovincial trade in natural gas. The Panel also came to conclusions with respect to distribution services within Canada.

Inland was the first utility in British Columbia to file Transportation Rate Schedules with the Commission. Rate Schedules 15 and 16 were accepted by the Commission for filing on an interim basis, effective October 11, 1985. In accepting the filings on an interim basis the Commission recognized in Order G-82-85 that changes to the tariffs would be required.

In December 1985 the Commission issued an Order requiring Inland to amend its Transportation Tariffs to remove any reference to net income indemnification. In 1986, complaints by Industrial customers and producers persisted with respect to the Terms and Conditions in the Inland tariffs. The Commission responded to these concerns and the need to establish Transportation Tariffs for all major gas utilities in the Province by issuing a letter in July 1986 requiring all utilities to file Transportation Tariffs with the Commission in September 1986.

In October 1986 the Commission heard several complaints regarding the Inland Transportation Schedules pertaining to the availability and appropriateness of those Schedules for particular negotiated agreements to be effective November 1, 1986. At that time there was an urgent need to deal with the individual contract arrangements since some Industrial customers were eligible to commence transportation services effective the start of the gas contract year, November 1, 1986. As a result of these hearings several Industrial customers, represented by Mr. R.B. Wallace, accepted the Inland Transportation Schedules on an interim basis so that transportation service could commence. However, the Industrial customers made it clear that they took exception to many of the Terms and Conditions in the Transportation Schedules and would press for changes to the Schedules without prejudice of them having entered into transportation service November 1, 1986.

Considering the need for a final review of the transportation services offered by Inland, the Commission determined that the transportation service functions of the utility would be reviewed in full as part of the Inland Rate Design Application. The Commission set that hearing to commence on

February 10, 1987. At a pre-hearing conference in December 1986, the Producer and Industrial intervenors intending to participate in the hearing requested the Commission to provide a facilitator/mediator to assist the parties in negotiating changes to the Transportation Schedules before commencement of the hearing. Inland accepted this proposal and a consultant was made available to assist the parties. Certain hearing participants later requested a delay in the hearing commencement so that new information could be assimilated. The Commission postponed the hearing until March 3, 1987 to commence in Prince George, B.C.

Following a week in Prince George, the hearing moved to Kelowna the week of March 10, 1987. At the end of the Kelowna session the Applicant and some participants requested that the Commission adjourn the hearing for two weeks so that further negotiations on Transportation Schedules could be undertaken by the participants. The Commission acceded to this request and the hearing was adjourned. Thereafter, the participants requested additional time to continue negotiations and the hearing did not resume until May 19, 1987 at Vancouver. In an attempt to expedite the hearing this session was to deal solely with issues arising out of the provision of transportation services by Inland. The hearing continued without interruption until conclusion of the argument of the transportation phase of the hearing on June 3, 1987.

Inland initially proposed three Transportation Schedules (15, 16 and 17). These schedules provide for various types of transportation service coupled with utility sales of interruptible gas. Inland later filed, at the request of the Commission, Documents 1 and 2 which allow for the use of interruptible transportation gas and Document 3 which provides for transportation service solely on Inland's system requiring the transportation customer to make separate arrangements with Westcoast. Inland now proposes that Documents 1 and 2 become Schedules. At the further request of the Industrial intervenors Inland filed Documents 4 and 5 which provide for other types of transportation service on the Inland system where the customer arranges his own transmission with Westcoast. Inland opposes Documents 3, 4 and 5 for reasons discussed in this Decision.

The hearing of this first phase of the Inland Rate Design Application required nineteen sitting days. The next phase of the hearing commences June 22, 1987 in Kelowna, B.C.

2.0 UTILITY ENVIRONMENT

As the participants in this hearing and the Applicant will no doubt attest, the development of Transportation tariffs to meet the diverse interests of all the parties involved has been a lengthy and difficult task. One should not be surprised that it has been difficult for Inland and its Industrial customers to agree on the mechanisms and conditions of gas service in the new era of competitive marketing. The extent of change over the past two years has been profound, and many structural impediments continue to exist which frustrate the evolution of a truly competitive market for natural gas.

In the past year the price of natural gas purchased by Inland from BCPC has fallen from a single price of \$1.86/gigajoule ("GJ") prior to November 1, 1986, to a three-tiered price in effect this current gas year. The Industrial price of natural gas has seen the greatest decline, to a price of \$1.03/GJ. While the price of gas Inland is able to offer through utility sales has fallen substantially, the utility is not yet able to purchase natural gas directly from producers due to contractual commitments to Westcoast and BCPC. Inland is therefore concerned that producers selling directly to Industrial customers may undercut the fixed utility price of natural gas.

Inland has also seen a substantial change in the manner in which it pays for transmission services from Westcoast. Westcoast has altered its rate structure to provide for full demand/commodity pricing. The incorporation of the new price structures into Inland's rates has been accomplished on a load factor basis so that the high load factor Industrial customers have seen a reduction in transmission charges, while the low load factor customers have seen their transmission rates increase.

Not only have the new policies changed the method of doing business by the utility and its customers substantially, but the existence of many interrelated contracts between the parties has exacerbated the situation so that as one party becomes free from contractual obligations he may attain an advantage over other market participants who are bound by longer term contracts or other restrictions.

3.0 DECISION ISSUES

The Commission's intention in issuing a Decision following this phase of the ongoing Inland Rate Design hearing is to assist all parties participating in the hearing by clarifying the Commission's views on certain matters regarding the terms and conditions embodied within the Transportation Schedules proposed by Inland. Various participants have made it clear that the final determination by customers in choosing between utility sales and transportation service, or potential future by-pass of the Inland system, will depend on a total package of terms, conditions and rates offered in the various schedules. The Commission recognizes this fact but finds that it is able to give relatively clear direction to the parties with respect to many of the proposed terms and conditions in the new Transportation Schedules. With regard to pricing issues, the second phase of the Rate Design hearing commencing June 22, 1987 in Kelowna will consider in detail the quantity of the rate which is just and reasonable, and the method by which that rate is structured in each Schedule. At this time the Commission is only able to give conceptual direction to the participants on pricing matters as they relate to utility sales versus transportation service.

Following are 14 issues which the Commission has considered and on which the Commission is prepared to give direction at this time. Inland is instructed to revise its Transportation Schedules to incorporate the views of the Commission from this Decision in new filings to be made on or before June 26, 1987.

3.1 Pricing Methodology between Schedules

In considering the matter of pricing at this stage in the Inland hearing the Commission can give guidance on the following two matters:

3.1.1 Consistency in Pricing

The Transportation Schedules proposed by Inland provide for a level of parity in pricing between similar types of utility sales and transportation service. Inland argued that the only difference between the transportation service rates and the utility sales rates should be a reduction from the sales rate to incorporate avoided costs, and an addition to recognize added costs to the remaining utility sales customers. The Producer groups and the Industrial customers have agreed with Inland on this rate determination philosophy with the conditions that the costs should be identifiable and Inland should not consider added gas purchase costs to the core market* as an added cost. In recent drafts, Inland has not included indemnification for increased gas purchase costs to the core market in its pricing proposal, and has stated that type of extra cost would not be caught up in the indemnity.

Inland has also made the point that those parties who benefit from the new policies of competitive marketing should also bear the risk. Inland put forward that principle in Exhibit 56, at Tab I, page 7, paragraph 10 and further stated in evidence that "the Residential and Commercial customers have not benefitted from deregulation and transportation service while the Industrials have benefitted enormously". There were no serious arguments by other parties against the general principle that those who benefit from the competitive market environment should absorb the risk which may accompany this competitive environment although other parties did not agree with Inland's characterization of who had benefitted from deregulation, or the magnitude of that benefit.

The Commission strongly believes that the base rate for comparable sales and service schedules should be consistent. In fact, the rates proposed by Inland are essentially identical, with any added costs being recovered through the indemnification clause.

* The core market comprises all residential and commercial customers plus those industrial customers choosing to purchase sales gas from Inland.

The Commission further believes that when it considers benefits or added costs which may adjust the overall rate of a particular schedule, care must be taken to only incorporate real costs which a customer choosing transportation service imposes on the remaining sales customers. These costs should not be interpreted so broadly as to include any benefits which a customer may have previously provided to the overall system but is now taking with him in choosing to move to transportation service. For example, at one time Inland believed that to the extent that an Industrial customer damaged the overall load factor of the utility sales, and thereby made it more difficult for the utility to purchase gas at advantageous prices in the field, the customer choosing transportation service should indemnify Inland for those increased costs. This is a clear example where the Commission believes that the high load factor customer now choosing transportation service would simply be taking his inherent load factor benefits with him and should not be penalized for so doing.

As an example of added costs that a transportation customer may inflict on the remaining customers, the Commission views the current revenue credit indemnification as being an example of the type of cost which should be recovered.

The Commission feels obliged to also provide some direction with respect to the pricing of large Industrial interruptible sales versus interruptible service. It may be argued that interruptible service customers are making use of pipeline space paid for by the core customers. If this can be shown to be true at the Kelowna session, and if the interruptible service customers are no longer providing benefits to the core market from improved load factor, an argument may be made that the interruptible service transportation margin should include some payment to compensate the core market for the use of its space by the interruptible service customers.

3.1.2 Westcoast Demand Charge Allocations

In formulating its contract demand nomination with Westcoast each year, Inland typically sums the peak and contractual requirements of firm gas sales and reduces that sum by an amount of one-half of the contracted deliveries to large firm Industrial customers. The reduction in the nomination accounts for the fact that Inland can rely on curtailment of its large firm Industrial customers to 50% of their own nomination with Inland for a period of up to five days in each contract year. Recent adjustments in Inland's schedules of rates to account for changes in Westcoast charges have consistently allocated demand charges to the Industrial "firm" customers based on 50% of nomination.

The current Inland proposal is to adjust that portion of its rates attributable to Westcoast charges to account for a 100% allocation of demand and commodity costs from Westcoast. Commensurate with this increase in allocated Westcoast charges is an equal reduction in margin allocated for Inland services. Although this matter was not fully canvassed in this first phase of the hearing, the Commission wishes to register its concern that the current allocation methods may not correctly apportion costs from Westcoast. A problem may develop if future Westcoast cost increases, or decreases, are allocated on a percentage basis. For example, if exports were to increase dramatically in future years, the Westcoast charges could fall as a result of better utilization of the system. In such an event it will be important to have correctly allocated the costs of transportation between Westcoast costs and Inland costs. In this regard, the Commission expects Inland to further develop its allocation rationale in phase two of the hearing and demonstrate how future cost assessments from Westcoast would be passed on to Inland's various classes of customers.

3.2 Indemnities

Inland's indemnity provisions are found in Article VIII of the Schedule 15 Transportation Service Agreement, and similar provisions are in other Transportation Service Agreements. Under the Indemnity Inland proposes that a customer taking transportation service ("the Shipper") be required to indemnify Inland, if, as a result of the Shipper fully or partially meeting its natural gas requirements by means of transportation services, Inland experiences higher gas supply expenses than it would have had the Shipper satisfied its gas supply requirements by purchasing gas under Schedules 11 or 12 from Inland. Inland also provides for an indemnity under Article 6.2 of Schedule 15 for damages, amongst other things, incurred by Inland as a result of the shipper failing to meet its commitment to deliver gas under the Schedule.

Inland's philosophy is that those who gain the benefits from the direct purchase of gas should also bear the costs. Therefore, any increased gas supply expenses incurred by Inland should be borne by the Shippers. Inland identified four such expenses: franchise fees; any difference between a volume and a revenue credit on Westcoast's system if the National Energy Board does not grant a volume credit; any take-or-pay liability Inland incurs with Westcoast; and, unknowns. Franchise fees are covered elsewhere in the Schedules. Inland's blanket indemnity covers the other items.

The Producers and Industrial customers agreed that the core market should not bear the burden, if any, of a shortfall between a volume and a revenue credit and the risk of take-or-pay. With respect to take-or-pay, however, the Industrial panel stated the risk is simply too great for them to bear.

In general, the Producers and Industrials felt that the Indemnity is much too broadly worded and the unidentified risks are too great for them to accept. They urged that the Indemnity deal with specific items only and any unforeseen items be left until they arise.

The Commission agrees with Inland that the core customers should not bear the risk with respect to any shortfall of revenue credit and any take-or-pay liabilities. However, these items should be specifically itemized indemnities (similar to franchise fees) to be paid if they emerge. The Commission recognizes that the take-or-pay matter may be too large for either party to bear and for this reason hopes that it is resolved before the National Energy Board or between Inland and Westcoast so that direct purchases can, in fact, take place. The take-or-pay issue may be resolved for the 1987/88 gas year, but until it is permanently resolved between Inland and Westcoast it is so large a liability it cannot be accepted by the core customers alone.

With respect to the issue of the unknowns, transportation agreements have been in effect on the Inland system for the past nine months and the Commission would have thought there would be few, if any, unknowns. On the other hand, unknowns may surface that legitimately should be borne by the direct purchase customer. The Industrials' concern is that they be entitled to address who should be responsible for the liability and that the liability not be retroactive. Inland agreed with the hearing concept; however they argued that a clause needs to be in the Schedules to ensure any decision could in fact be retroactive.

The Commission is not prepared to accept a broad unspecified Indemnity and instructs Inland to remove reference to Indemnification for unknown reasons. The Commission will deal with specific new Indemnities as and when they occur. The Commission recognizes that additional operating costs or other expenses may develop as a result of Transportation service. Inland may wish to address how these costs could be recovered from Transportation customers so that core customers are not harmed. One method that could be considered is a specified allowance in the Transportation Schedules which would be credited directly to the core customers.

3.3 Curtailment Provisions

The present Tariff Schedule 11 of Inland provides for five days of curtailment to a 50% level. Inland proposes to increase the right of curtailment to 10 half-days, both for sales under Schedule 11, and for curtailable Transportation Service. Inland also proposes to change the wording in that provision slightly to increase its flexibility by setting out that a customer and Inland can agree to less than a 50% curtailment on a particular day, with the balance of the curtailment to be on another day. Inland has proposed a non-curtailable Transportation service under Schedule 17 but has not proposed a similar sales Schedule.

Inland argued that its proposal to increase the curtailment to 10 half-days provided a very low cost method of dealing with what Mr. Powell called a "needle peaking" situation. Inland provided evidence that theoretical studies undertaken by the utility demonstrated that under certain design conditions the 10 half-days of curtailment would be fully utilized by Inland. The evidence also showed that on a historical basis Inland could not identify any year in which its records showed that it had curtailed up to the current five half-day limit.

Mr. DeBiasio, on behalf of Cominco and Mr. MacMillan, on behalf of Prince George Pulp and Timber testified that they favoured retention of the current five half-days of curtailment but were willing to offer Inland peak-shaving services for an additional five half-days of curtailment, with Inland paying the fuel and other operating costs to effect the demand reduction. Mr. Howell, for Consumers' Packaging gave evidence to show that the nature of its operation was such that curtailment to 50% of its nomination on any day would result in a shut-down of manufacturing. Consumers' Packaging strongly opposed any increase in the curtailment right by Inland.

The Commission recognizes that the existing curtailment rights of Inland with its "firm" Industrial customers provide a substantial peak-shaving benefit to both the company and those Industrial "firm" customers. An additional increase in curtailment for five extra half-days would be advantageous if the base of the "needle peak" discussed by Mr. Powell is greater than five days, after considering platooning of curtailment rights to effectively broaden the base. The Commission has considerable difficulty however, with a mandated change to 10 half-days of curtailment incorporated in a firm gas contract. While the Commission is not prepared to increase the extent of curtailment, it finds favour with Inland's proposal that a short-fall in curtailment in one day can be carried over to another day.

As Inland is considering peak-shaving options the Commission believes it would be most prudent for the utility to avail itself of the offer of additional peak-shaving put forward by Cominco and Prince George Pulp and Timber. Inland should also consider allowing customers like Consumers' Packaging to negotiate a reduction in their existing curtailment responsibilities by entering into contracts with other Industrial customers to provide those curtailment rights or, in the alternative, pay Inland a higher rate to reflect the improved quality of service desired.

3.4 Confidentiality of Prices

The matter of confidentiality of prices occupied more hearing time than any other issue. Inland proposed that there should be confidentiality of burner-tip prices and margins of utility sales to allow the utility to compete with direct sales because its cost of gas is public knowledge at this time. Inland is prepared to have the margin of its sales rates become public when the rate is unbundled to establish a transportation service rate because the cost of gas to transportation service is confidential. In evidence Inland acknowledged that while the existing commodity cost of gas to the utility is known it may become confidential effective November 1, 1987. Even if the rate remains public for

the upcoming contract year, Inland will be able to attain some measure of confidentiality when the Government and existing contracts allow it to purchase gas from suppliers other than BCPC. Inland also proposed that its "negotiated" rates remain confidential to allow the utility to meet competition from competing fuels and to allow it to negotiate on an individual basis.

Other participants at the hearing argued against confidentiality of Inland's margin. Mr. Gathercole noted that revenue shifted as a result of discounted confidential margins by Inland could be automatically transferred to core customers via the Gas Pricing Clause ("GPC"). In argument he submitted that, "the core customers will be being used to subsidize Inland's undercutting its competition, and in order to see whether that is happening we need more information."

The Industrial customers argued in favour of public margins noting that recent disclosure of final offer prices by Inland to its non-captive customers had not led to a "me too" reaction of all customers demanding the lowest rate.

The Producers also argued against confidentiality noting that the consideration of choosing one gas source against another should relate to competition in the field, and not to the monopoly transportation systems. The Independent Petroleum Association of Canada ("IPAC") urged the Commission to cause Inland to separate the regulated transportation function of Inland from the function of buying and selling gas.

The Commission strongly supports the notion that margins for monopoly transportation sales and services should be public. The Commission recognizes that this could put Inland at a competitive disadvantage for the upcoming contract year if the prices of gas negotiated by Inland are made public. The Commission directs Inland to make the margins on all Industrial sales and transportation schedules explicit in those schedules. If however, Inland is ultimately allowed to negotiate discounts in the margin for customers

considering alternative fuels or by-pass the reduced margin for those customers will be filed as a public Tariff Supplement when accepted by the Commission. Any reductions in margin will be offered equally to sales and service options.

With respect to authorized overrun ("AOR") gas Inland wished to have the rate for AOR sales remain confidential. The Commission believes that the margin for AOR sales should be public. However, as stated earlier in this Decision the Commission may consider a differential margin between sales and service of interruptible gas to account for the use of the valley in the core customers nomination with Westcoast. Through such methods the core customers would retain a high load factor from AOR sales or be compensated by interruptible transportation customers for the use of core customer pipeline space.

3.5 Force Majeure

The provisions regarding force majeure found in Inland's Transportation Service Agreements vary depending on, for instance, whether the transportation service in question is firm or interruptible. There would appear to be two general issues in dispute. The first is whether Shippers should receive credit from Inland for Westcoast charges incurred during a declaration of force majeure due to strikes or lockouts. The second issue considers whether Shippers should only be entitled to relief from their contractual obligations during an event which would have given rise to a declaration of force majeure by Westcoast prior to November 1, 1985.

Inland's Large Industrial sales customers are relieved from paying Westcoast charges under the existing Schedule 11. However, Inland's evidence is that it no longer receives such credit from Westcoast. It would appear that all of the parties agree that the strike relief provisions should mirror one another under either utility sales or transportation service. Inland argued this should reflect their current situation with Westcoast and the Commission agrees. If Inland must continue to pay Westcoast tolls and tariffs notwithstanding a declaration of force majeure due to strikes or lockouts and could not be reimbursed by the

sales or service customer, Inland would be bearing the risk of its customers' labour situations. This is clearly unacceptable. The force majeure provisions dealing with Westcoast tolls and tariffs during strikes or lockouts shall remain in the form found in the proposed tariffs. The Commission recognizes that Inland may have to adjust the amount it is collecting under its strike adjustment clause to reflect this.

With respect to a Shipper being able to declare force majeure only in situations where Westcoast would have declared force majeure prior to November 1, 1985 the Commission finds this equally unacceptable. A force majeure provision is intended to provide relief from contractual obligations where events occur beyond the control of the contracting party. Inland's concern that Shippers may not offer adequate diversity of gas supply is not a force majeure question but one of whether adequate back-up supply is provided sufficient to reduce the risk of a failure of gas supply in reasonable circumstances. Inland has required this diversity of gas supply under the applicable schedules. Inland is therefore directed to remove Article 12.3 from the Schedule 15 Transportation Agreement, and similar provisions in other agreements.

3.6 Daily Versus Monthly Gas Balancing

Inland provides monthly gas balancing on existing Schedule 11 and the proposed Schedules 15 and 16. Inland has also provided for monthly gas balancing in Document No.5. Daily gas balancing is required for Schedule 17, Documents 1, 2, 3 and 4.

Dealing first with Schedule 17, which is a Schedule that provides for AOR sales, Inland's evidence is that it only wishes to provide daily gas balancing because this Schedule is not curtailable by Inland. Inland argued that the provision of monthly balancing allows those Industrial customers to enter into gas supply contracts at improved effective load factors which will result in lower negotiated wellhead prices. Inland wished to encourage Industrial

customers to make use of Schedule 15, rather than Schedule 17, because of the curtailment rights under Schedule 15.

The Commission notes that Schedule 17 includes additional charges in the Inland margin which exactly equate with 50% of the demand charges from Westcoast. Therefore, to the extent Inland might have to increase its nomination by 50% of a Schedule 17 customer's own nomination, Inland has already compensated itself in the Schedule 17 rate for the additional demand cost with Westcoast. Also, Mr. VanGenderen testified there would be some offset because more valley gas would be available for AOR or Interruptible sales. The Commission concludes that Inland should provide monthly gas balancing for Schedule 17 because Inland has fully compensated itself for the additional demand charges liable from Westcoast.

Turning to Documents 1, 2, 3 and 4 Inland argues that there cannot be monthly gas balancing on those schedules because of the inherent differences between transportation service gas being used for interruptible purposes as opposed to AOR sales. The problem appears to be that an Industrial customer nominating interruptible service will cause Westcoast to deliver the nominated volume of gas that day under interruptible service. Inland argues that it will be liable to Westcoast for those interruptible service charges because of the "shotgunning" technique used to deliver the gas. Inland argued that because of the Westcoast provisions it is unable to offer monthly gas balancing for Documents 1, 2, 3 and 4 without incurring added costs to the core market.

The Commission accepts, at this time, Inland's testimony with respect to the need for daily gas balancing on these Documents. However, the Commission views monthly gas balancing as a desirable feature to be offered to all Industrial customers on the Inland system. The Commission encourages Inland to investigate ways to provide this balancing without added cost to the core market. This could perhaps be accomplished by modifications to the Westcoast contract or adjustment to the Documents so that the interruptible customer will absorb any remaining costs as a result of the provision of monthly balancing to the Documents.

3.7 Producers as Shippers

This issue is whether Producers should be allowed to be Shippers on Inland's system. Inland argued they should not for the reasons set out in the evidence of Mr. Arthur found under Tab 2 of Exhibit 20 and on pages 1 and 2 behind Tab 1 of Exhibit 56. Inland is concerned with the creditworthiness of possible Producer/Shippers; the necessity to deal with end-users in the management of its system (including ensuring that it has access to the end-user's property and the right to curtail the end-user); the possible monopolization of Inland's system by producers tying up capacity; and, the possible breach of franchise agreements including a possible reduction in revenue to the Municipalities.

The Municipalities supported Inland's argument although they did not appear to object to the principle of producers being Shippers, but rather to the possible reduction in revenue from franchise fees.

The Producers want to be Shippers so they may offer "one-stop shopping" to direct gas purchasers, including bundled sales service very similar to Inland's current sales tariffs. They rejected Inland's arguments saying those difficulties could be covered by provisions in the Transportation Schedules or in individual operating agreements. Inland's witnesses agreed this could be done but argued this would add undue complexity without any apparent benefit. The Industrials, Consumers Packaging and IPAC basically echoed the Producers' sentiments.

The Commission believes Producers should have access to Transportation Service Schedules as Shippers. However, the Commission acknowledges Inland's concerns with respect to creditworthiness and monopolization of Inland's system. Both of those matters should be covered in the Transportation Schedules along with other requirements like access to the end-user's property.

The Commission is not in a position to attempt to interpret the franchise agreements to determine whether Producers being Shippers would constitute a breach of such agreements. Inland was concerned with the possibility that an injunction may prevent producers from supplying gas within the municipalities and that the end-users would possibly have to go back to Inland to arrange for their transportation requirements. However, the Commission notes that the Producer will have nominated with Inland and this space will be available in a practical sense. It may be that the Transportation Agreement may simply be assigned.

The Commission recognizes that franchise matters will be discussed further in Kelowna. It is also worth noting that the current Schedules provide for the payment of franchise fees above those currently collected if it is determined these fees must be paid.

3.8 Shippers Holding Contracts With Westcoast

Inland strongly opposed Shippers holding their own contracts with Westcoast. Inland has raised various problems related to this issue including its exclusivity clause with Westcoast and the potential for further reductions in franchise fee revenue to municipalities. Apart from several contractual impediments there appear to be two main issues related to Shippers holding contracts with Westcoast. First, Inland holds the view that if an Industrial customer acquires its own contract with Westcoast it will be one step closer to by-passing the Inland system. The Industrial customers have countered this argument by stating that acquiring their own contracts with Westcoast is such an important issue that if it is not provided they are likely to be forced to by-pass the Inland system, should this be available.

The second concern raised by Inland is that Industrial customers obtaining their own contracts with Westcoast will attempt to contract gas behind the McMahon processing plant to minimize their cost of delivering marketable quality gas on the Westcoast system. Inland would also like to maximize its reserves behind the McMahon plant to reduce costs for the core customers.

Inland argued that it may be impeded from competing for plant capacity until 1991 when the Inland/Westcoast contract expires. However, other evidence at the hearing has identified the potential for Inland to contract for gas sooner than 1991.

The issue of allocating space behind the various gas processing plants in British Columbia may be unique in North America. The resolution of this issue is a perplexing problem being discussed not only in this hearing, but before the National Energy Board and between BCPC, the B.C. Government, the distributor companies and producers. Ideally, the allocation of space behind the processing plants could be determined in a way which would allow the British Columbia distributors and Industrial customers fair and equal access to the capacity at the same time.

In this regard Inland gave assurances in its argument that it would deal in some equitable manner with plant capacity with its Industrial customers when Inland itself is able to buy gas directly.

The Commission supports the desirability of Shippers having the right to contract for services from Inland related solely to the Inland transportation system if they can arrange their own transportation with Westcoast. The Commission therefore finds Documents 3, 4 and 5 to be desirable. The Commission believes that these Documents should be filed as Rate Schedules so that Industrial customers can at least avail themselves of currently uncontracted capacity behind the various gas processing plants in British Columbia, if that is their desire. The Commission recognizes that allocation of plant capacity is an important issue to the distributors although it is beyond the Commission jurisdiction. Because the issue has the potential for frustrating government policies concerning competitive marketing the Commission urges Inland, for its part, to seek an early resolution of the plant capacity problems with Westcoast and BCPC. The Commission does not believe this issue can be allowed to persist until 1991, as indicated by Inland.

3.9 Transportation Services for Inland's Schedule 5 Customers

Inland is committed to providing Transportation Service to its Schedule 5 customers commencing November 1, 1988 subject to the prior resolution of a number of issues. The Industrial panel urged the Commission to order Inland to provide Transportation Service to these customers as soon as possible.

The Commission is encouraged that Transportation Service will be made available to Inland's Small Industrial customers. This will enable them to engage in the direct purchase of natural gas. In addition, it may relieve some of the competitive pressures from alternative fuels Inland is experiencing with respect to these customers and which we expect to hear more about in the second phase of this hearing.

Inland stated that certain issues must be resolved before they can provide this service. For the most part, these are the same issues which are being resolved for Large Industrial Transportation Service to take place. The differences, if any, relate to the size of the load and the service that the Small Industrials are presently receiving. The Commission accepts Inland's argument that they must learn to walk before they can run. However, Transportation Service should be available to Inland's Small Industrial customers commencing November 1, 1988. To ensure that this service is in fact available at that time, Inland is directed to provide the Commission, by October 1, 1987, with draft schedules it feels are necessary to provide this service. Inland should at that time clearly identify what notice requirements it will require from Schedule 5 customers moving to Transportation Service.

3.10 First Call Priority

Inland requires that Shippers choosing Transportation Service provide a diverse gas supply to ensure that adequate gas will be available on days when Inland is curtailing the transportation customer. As part of the diversity of gas supply Inland requires that the Shipper have at least 75% of his maximum day transportation volume ("MDTV") as first call priority gas. The first call priority means that the gas is not under contract for delivery to other parties at an equal priority to the delivery to the Shipper.

Inland stated in argument that the 75% level of first call priority was a good starting point. Counsel for Inland further stated, "But I suppose if at some future date it was demonstrated that there was a good reason to change from that, we'd be prepared to listen at that time."

The Industrial customers did not take issue with Inland's 75% requirement for first call priority gas volumes, since the Industrials felt that, in most cases, they would require equivalent or better security of supply for their own operations.

The Producer groups argued that the level of first call priority, and the diversity of supply behind any transportation contract should be determined by the independent gas supply consultant.

The Commission recognizes that there can be many sources of gas supply, with varying levels of priority, which may be contracted as primary and back-up supply for a particular contract. The Producers demonstrated at the hearing how they had provided for interlocking arrangements of gas supply amongst themselves which made available many wells behind at least two of the gas processing plants in British Columbia to supply gas to their Industrial customers. In addition, these Producers were prepared to make Alberta gas available in the event all B.C. gas was being utilized for other contracts. Such a situation would enhance the security of gas supply to all British Columbians during emergency periods.

The Commission is satisfied that the 75 % first call priority volume is a good starting point for the transportation contracts. However, the Commission can visualize situations where the amount of first priority gas should be increased in percentage, and cases where the diversity is so complete that the percentage could be reduced as low as 57.5 %. The level of 57.5 % simply reflects the diversity of gas supply available from BCPC which is considered to be the most diverse gas supply historically available.

The Commission therefore directs Inland to modify its first call priority clause to allow the Company to either increase or decrease the percentage of first call priority gas depending upon the diversity of gas supply offered for a particular contract.

With respect to the use of Alberta gas, Inland's position is that this gas should be provided as back-up in emergency situations only. The Producers take the position that Alberta gas should be allowed when they have exhausted the B.C. sources of natural gas. The differences of opinion with respect to the use of Alberta gas were based on implications for increased costs to the core market of Westcoast gathering and processing facilities if Alberta gas substantially displaced gas production which otherwise would have come from British Columbia.

With respect to the use of Alberta gas the Commission does not take issue with the positions raised by any of the parties. The Commission believes that the provision of Alberta gas as part of the back-up supply arrangements to a transportation contract is desirable when the Alberta gas is to be used after B.C. sources of supply have been exhausted. This provision will ensure that the Westcoast processing facilities are not by-passed by transportation customers seeking lower cost processing. The Commission would not like to see a situation develop where Inland's core customers faced escalating processing costs due to transportation customers choosing gas processed outside B.C.

3.11 Nomination Lead Times

Under the current Inland/Westcoast contract, Inland is required to nominate its contract demand twelve months in advance of the contract year for which the contract demand will apply. Inland therefore requires that its Industrial customers give the utility thirteen months advance notice of the Industrial's nomination. During the past year Inland and Westcoast have allowed the Industrial customers latitude in choosing between utility sales and transportation service for some period after the nomination deadline. At this time the date for choosing between utility sales and transportation service for the contract year commencing November 1, 1987 is September 1, 1987.

The long lead-time in making nominations has been a sore point between Industrial customers and Inland, and, in turn, Inland and Westcoast for some time. More flexibility and shortened lead-times would seem to be required in the current competitive marketing era.

Mr. DeBiasio raised interesting points during his examination by Inland's Counsel. At page 2535 of the transcript, Mr. DeBiasio suggested the Commission order Inland to have the nomination period shortened. Mr. DeBiasio pointed out that he was very impressed when the Commission ordered Inland to extend the date for choosing between sales and service this year and "lo and behold it happened". The Commission believes that the nomination lead-times included in the Inland/Westcoast contract are excessive and are not responsive to government policies fostering a competitive marketplace. In the spirit of the government agreements, and as discussed in the Pipeline Review Panel Report, this type of issue should be renegotiated by the parties. The Commission is aware that this matter is being raised at the current N.E.B. review of Westcoast rates, but the Commission also directs Inland to pursue this matter privately with Westcoast and report back to the Commission by October 1, 1987.

While the Commission believes that shorter lead-times and greater flexibility in nominations are required, the Commission does recognize the need of the utility companies to plan for capacity additions and gas supply. The amount of prior notification of demand changes would logically depend on the magnitude of the change in demand. For example, a small change in demand can, in most instances, be accommodated without long lead-times.

3.12 Affiliate Transactions

IPAC raised the matter of affiliate transactions in paragraphs 59 and 68 of its evidence and in argument. IPAC urged the Commission to impose limitations on non-arm's-length purchasing by Inland from Inland Producer affiliates.

The matter of Inland's gas purchasing and competition with other Producers and Brokers was also discussed by Inland's Counsel with the Industrial panel. The potential for utilizing brokerage companies like United Gas Brokers was canvassed.

The Commission recognizes that inadequate evidence has been raised in the hearing so far to fully address the matter of affiliate transactions. However, the Commission is very concerned that it must come to grips with the appropriate structure of distribution utilities with respect to gas purchases and sales.

In the Pipeline Review Panel Report, that Panel came to the conclusion that, "for the development of an effective competitive marketing system, the panel considered it absolutely necessary that separate policy making, management, and accounting exist between the transportation services and any marketing functions of a pipeline company." With respect to distribution companies the Panel recommended "that distribution companies also review their corporate alternatives and move to the appropriate degree of separation between any unregulated gas purchase and marketing activities, on the one hand, and their regulated transportation activities and their full service to Residential, Commercial and non-direct sale Industrial customers, on the other hand."

If Inland proposes in future to charge different commodity prices for natural gas to different customers within a similar class, or if Inland proposes to purchase natural gas from any non-arm's-length brokerage or production company, Inland is instructed to lead evidence in Phase two of this hearing on the appropriate corporate structure to ensure equitable treatment for all core customers.

3.13 Prior Termination of Contracts

Article XI in the Schedule 15 Transportation Agreement, and similar articles in other Transportation Schedules, deals with the prior termination of a Transportation Agreement if one party fails to perform any of the obligations imposed within the Agreement. The Commission is satisfied with the Article as far as it goes. However, the Commission is concerned that a utility could be left with substantial undepreciated pipeline assets through the prior termination of a contract.

Dealing first with a new customer, the Commission envisages situations where Inland would extend a separate lateral to a new Industrial customer. In so doing it would be prudent for the utility to enter into a long-term agreement with the Industrial customer, or to ensure that should the Industrial customer leave the Inland system prematurely the assets put in place for the customer would be paid for by that customer. As an example, Inland might consider an initial five-year agreement with a new customer with a proviso that should the customer not extend the contract beyond five years he would be liable for the then depreciated assets that were put in place to accommodate that load and which have no residual value if the customer terminates service.

In the case of Inland's existing customers, particularly those customers who have been with Inland for ten years or more, the Commission believes that it is appropriate to continue contract extensions on a yearly basis or longer depending on the wishes of the Industrial customer. These customers have now been with Inland for some period of time and can be considered to have contributed greatly to the assets of the utility put in place for their use.

Finally, one must consider any customers who might leave the Inland system to use alternative fuels, or to construct a by-pass pipeline. Depending on the circumstances it might be appropriate to charge such customers a re-entry fee should they wish to rejoin the Inland system at a future date. Such a re-entry fee would be appropriate if the opting in and out of customers created gyrations in rates to other customers and difficulties in gas supply arrangements. Inland may wish to address this matter further in the second phase of the hearing, or at a future date. The Commission does not consider that a re-entry fee is appropriate for customers choosing to obtain their natural gas via Transportation Service as the transportation customers are still utilizing the Inland pipeline system and contributing to it. However, Transportation Service customers wishing to return to sales service may be exposed to gas commodity prices available at that time.

3.14 Producer's Declaration

The Producer's Declaration is provided for in those Transportation Schedules where Inland has the right to curtail the Shipper. The necessity of Inland ensuring that this gas is available has already been discussed. The Commission is aware that the form and content of the Producer's Declaration has gone through a number of changes including the removal of the requirement that the Declaration be sworn. The only remaining issue is with respect to paragraph 6 which reads as follows:

- "6. The Producer acknowledges and understands that the matters declared herein will be relied on by Inland in assessing and arranging its natural gas supply requirements."

Inland argues that this provision is necessary to ensure that the person signing the Declaration recognizes the importance of the accuracy of the information contained in the Declaration. The Producers took exception to the provision, arguing that it goes beyond the scope of what needs to be covered in the Declaration and is not necessary or appropriate. As an alternative, they urged Inland to allow the provision to be covered in a preamble or a covering letter.

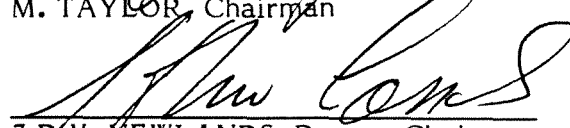
The Commission concurs with Inland's position on this matter. The very reason there is a need for a Declaration is for Inland to ensure, to the maximum extent possible, that the Shipper's gas will be available for the core market on the coldest winter days. Inland should and will be relying on the information supplied by the Producer in assessing and arranging its natural gas supply requirements. Paragraph 6 should be retained in the Producer's Declaration.


4.0 DECISION

The Commission directs Inland to make the necessary changes to its proposed Schedules to reflect the Commission's views contained in this Decision. The revised Schedules and Documents 1 through 5 are to be filed on or before June 26, 1987 as specified in attached Order No. G-37-87.

DATED at the City of Vancouver, in the Province of British Columbia,
this 17th day of June, 1987.



M. TAYLOR, Chairman

J.D.V. NEWLANDS, Deputy Chairman

N. MARTIN, Commissioner



UTILITIES COMMISSION	
ORDER	
NUMBER	G-37-87

PROVINCE OF BRITISH COLUMBIA
BRITISH COLUMBIA UTILITIES COMMISSION

IN THE MATTER OF the Utilities Commission
Act, S.B.C. 1980, c. 60, as amended

and

IN THE MATTER OF an Application by
Inland Natural Gas Co. Ltd.

BEFORE :	M. Taylor,)	
	Chairman;)	
	J.D.V. Newlands,)	June 17, 1987
	Deputy Chairman; and)	
	N. Martin,)	
	Commissioner)	

O R D E R

WHEREAS the intent of the Agreement dated October 31, 1985
between the Governments of Canada, British Columbia, Alberta, and
Saskatchewan was to foster a competitive market for natural gas; and

WHEREAS the provision of Transportation Service by Inland
Natural Gas Co. Ltd. ("Inland") is a necessary step in the movement towards a
competitive market for natural gas; and

WHEREAS certain Industrial customers and Producers of
natural gas have complained to the Commission regarding the Terms and
Conditions of Inland's provision for such Transportation Service; and

WHEREAS Inland has applied to the Commission for approval of
the Terms and Conditions under which it sells natural gas to certain of its
customers and under which it provides Transportation Service to certain of its
customers; and

WHEREAS the Commission has held a hearing inquiring into the
appropriate Terms and Conditions for which approval was sought and other
matters incidental to the provision of Transportation Service; and

.../2

ORDER
NUMBER G-37-87

WHEREAS the Commission considering it desirable to issue in a timely manner a Decision on these matters, including the complaints of certain Industrial customers and certain Producers, has issued its Decision concurrently with the date of this Order.

NOW THEREFORE the Commission orders that Inland comply with the directions contained in its Decision dated June 17, 1987, on or before the dates prescribed for compliance in the Decision.

DATED at the City of Vancouver, in the Province of British Columbia, this 17th day of June, 1987.

BY ORDER


Chairman