

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

and

IN THE MATTER OF
a Revenue Requirements Application by
Inland Natural Gas Co. Ltd.

DECISION

August 6, 1987

Before:

J.D.V. Newlands, Deputy Chairman and
N. Martin, Commissioner

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I. BACKGROUND

Inland Natural Gas Co. Ltd. ("Inland", "the Applicant") is the second largest natural gas distribution utility in British Columbia. The Company's primary business is the distribution of natural gas to over 100,000 customers in 54 communities in British Columbia. The service area extends from the Peace River area in the north, through the Caribou and Okanagan regions to the West Kootenays.

Wholly-owned subsidiaries of Inland include Columbia Natural Gas Limited, Fort Nelson Gas Ltd., Grande Prairie Transmission Co. Ltd., Peace River Transmission Company Limited, Inland Development Co. Ltd., Inland Gas & Oil Ltd. and Inland Natural Gas Marketing Ltd.

Inland had owned directly 67.1% of the shares of Trans Mountain Pipe Line Company Ltd. ("Trans Mountain") but in September 1985 sold 20% of its holding to Transland Investments Ltd. thereby reducing its direct ownership of Trans Mountain to 47.1%. Its indirect ownership remains at 67.1%.

At the date of the hearing after the issuance of additional shares by Inland, Trans Mountain owned 45.5% of Inland's voting shares. Subsequently, in February 1987 Trans Mountain sold 1.2 million common shares of Inland, thereby reducing its interest in Inland to 36%.

The corporate structure of the Inland group of companies (Exhibit 4, Tab 17) is reproduced as Appendix A in this Decision. Appendix B illustrates Inland's returns and other utility data for the period 1981 - 1987.

Inland last appeared before the Commission for general rate relief in October 1984 with a Decision issued January 1985. For fiscal year 1986, relief was granted by a deferred income adjustment (Hot Gas, see page 22), which remains subject to Commission determination in this Decision.

II THE APPLICATION

Pursuant to Sections 67(2) and 106 of the Utilities Commission Act, Inland applied May 30, 1986 for interim and permanent rate relief to be effective July 1, 1986. Based on a fiscal 1987 forecast the Applicant requested an across the board increase of 2.32%, or \$3,998,000 over existing rates, to achieve a 15% return on common equity (12.77% return on rate base). The previous rate of return on common equity was 15.75%, approved by Decision dated January 11, 1985.

By Order No. G-38-86, dated July 4, 1986, the Commission approved the requested interim increase subject to refund with interest should the rates not be confirmed. Order No. G-47-86, dated July 31, 1986, set down the Application for public hearing to commence in Kelowna, September 22, 1986.

Four significant matters arose after filing of the Application on which the Commission heard testimony at the hearing.

1. Inland applied for and the Commission approved the issue of one million common shares of Inland for \$11 million (Order No. G-53-86, dated August 19, 1986). The capital structure of Inland was directed to be subject to review at the public hearing. The capital structure of Inland is discussed in Section IX of this Decision.
2. Inland also applied for Commission approval to vary Order No. G-63-85 in which the Commission had approved Inland's earlier request to defer approximately \$1 million revenue from fiscal 1985 to be amortized in full in fiscal 1986. The Applicant requested the amortization to be varied and spread evenly over two years, 1986 and 1987. By Order No. G-54-86, dated August 25, 1986, the Commission approved the request subject to review in the public hearing. This matter is addressed in Section VI (2) of this Decision.

3. By letter dated August 27, 1986 (Exhibit 15A) the Mechanical Contractors Association of British Columbia expressed opposition to Inland's proposed activities relating to merchandising of natural gas appliances. The Association contended that Inland would use its monopoly status to provide unfair competition with contractors and entrepreneurs to supply and install gas equipment. This matter is addressed in Section IV (4) of this Decision.
4. On the basis of its Application, and by Orders No. C-3-85 and C-4-85 Inland was granted a Certificate of Public Convenience and Necessity to provide natural gas service to the Village of Chase and the unincorporated areas of Blind Bay and Sorrento. For each project Inland was directed to file monthly progress reports, with a final report showing the facilities installed, the costs thereof and the customers being served.

By letter dated May 8, 1986 the Commission put Inland on notice that significant cost overruns on the projects would be reviewed. This matter is addressed in Section IV (2) of this Decision.

Evidence for the Applicant was presented by Mr. R.E. Kadlec, President and Chief Executive Officer; Mr. C.I. Kleven, Vice President, Finance and Administration; Mr. R.T. O'Callaghan, Vice President, Gas Supply and Engineering; Mr. G.M.O. Solly, Vice President, Operations; Mr. J.L. Randall, Vice President, Marketing and Utility Planning; Mr. J.D. Ferguson, Manager of Gas Supply; Mr. W.R. Manery, Manager of Technical Services; and Mr. J.O. Wessler, Manager, Regulatory Affairs and Dr. R. Evans, Financial Consultant.

Appearances were made by Mr. R.B. Wallace for British Columbia Forest Products Ltd., Caribou Pulp & Paper Company, Husky Oil Limited, Prince George Pulp & Paper Limited, Northwood Pulp & Paper Limited, Westar Timber Limited, Weyerhaeuser Canada Limited, and the Council of Forest Industries; Mr. K.E. Gustafson for Consumers Packaging Inc.; Mr. R.J. Gathercole, Ms. J. Harry and Ms. J. Vance for Consumers' Association of

Canada, Federated Anti-Poverty Group of B.C., B.C. Old-Age Pensioners Organization, and the Council of Senior Citizens Organizations; Mr. J. Pelrine and Mr. R. Milner for British Columbia Petroleum Corporation ("BCPC"); Mr. D.K. Clark for Czar Resources Ltd.; Ms. S.L. Taylor for Westcoast Transmission Company Limited ("Westcoast"); Mr. V.J. Traynor for Mechanical Contractors Association of B.C. and Mr. B. McClure for Janistar Finishing and Heating Ltd.

In addition, Mr. V.J. Traynor, Mr. D.B. Harvey and Mr. H.R. Bach, representing the interest of the mechanical contractors, appeared to give testimony on Inland's merchandising activities. Dr. W.R. Waters also appeared as expert witness on behalf of the forest industrial intervenors with regard to the appropriate capital structure and rate of return on common equity of Inland.

III INTRODUCTION

The three member Commission Panel ("Commission") for this hearing was comprised of Mrs. M. Taylor as Panel Chairman, J.D.V. Newlands and N. Martin. Mrs. Taylor was unfortunately forced to withdraw from the Panel for personal reasons on the third day of hearing. Mr. Newlands, Deputy Chairman of the Commission, took over as Panel Chairman for the balance of the hearing.

Mr. Kadlec, President and Chief Executive Officer of Inland stated that significant decreases in the volumes of gas sold, magnified by an increase in the cost of service were the principal reasons Inland sought a rate increase. His evidence was that cost increases were attributable to increases in insurance premiums, the need for greater marketing effort to retain existing sales, inflation, additions to rate base, and the proposed adoption of more equity in the utility capital structure (Exhibit 2, Tab 1, p. 3).

Mr. C.B. Johnson, Counsel for the Applicant, in an extensive argument addressed the principal issues of the hearings, which included the capital structure, the appropriate equity component, business risks of Inland, rate of return on equity, sales volumes, the strike adjustment provision, sales of gas to Columbia, the revenue deferral on account of high heat content gas ("hot" gas), supply nominations, operating and maintenance expenses, the deferred interest account, intercorporate charges, capitalization of overheads, rate base items, and the marketing department including natural gas for vehicles and merchandising programs.

Mr. R.B. Wallace, Counsel for some major Industrial customers summarized his argument as follows:

" . . . this hearing has been longer than any of us anticipated, and in my experience probably more complex and more difficult. In my submission, however, the issues before you are fairly limited when you take them down to their basic core.

The issues, simply put are the following: First, is Inland going to be permitted to continue to increase its margin, its costs of operations at rates well in excess of inflation during a time when most other sectors of the economy have learned to and continue to apply cost restraint?

Second, is Inland going to be permitted not only to continue to invest in plant which does not recover its costs, as is the case in its mains extension program, and is it going to be permitted to expand into new and equally un lucrative areas such as merchandising and natural gas for vehicles at the expense of the general ratepayers?

Third, is Inland going to be permitted a return on equity well in excess of that awarded by any board in the last year and, more importantly, is Inland going to be allowed to earn a return on equity that is not presented in the capital structure?

In my submission these questions are simple questions, but they will require tough answers and a great deal of serious thought and consideration before they are resolved. Inland has indicated that the increase it seeks is only 2.3% on current rates, a statistic that on its face is true, but a statistic that does not tell the whole story by any means.

The facts, when examined more deeply, show a much more complex and I believe disturbing situation. A comparison of your January, 1985 decision and the current application shows that in the test year Inland forecast decreasing sales and increasing costs. Inland is projecting sales decreases of 1.5% since 1985, yet by way of contrast Inland's own margin is up 12.6% overall, and on a per gigajoule basis Inland's margin is up 14.3%, an increase almost triple the rate of inflation we've experienced over the last two years — or triple the annual rate of inflation, and 50% over the combined rate of inflation.

What is Inland's reaction been to its declining sales, to its increased costs, and to the drop in competitive energy prices generally? My submission is that it has been to urge others to reduce their returns, but at the same time to ask for more for itself."

(Transcript pp. 2912 - 2914)

Ms. J. Vance, Counsel for the Consumers' Association of Canada and Old Age and Anti-Poverty groups argued:

". . . there are several submission we will make respecting the increase Inland has applied for in this rate application. First, despite certain laudible efforts Inland has not held its costs down as

much as it could have when compared to non-regulated private sector corporations that have implemented restraint mechanisms.

Second, there are components of Inland's management operation that lack articulated and effective plans and strategies as well as ongoing monitoring mechanism in order to maximize cost efficiency.

In the result the increase is made necessary because of shortcoming which Inland must be admonished to correct.

Third, there are certain components of Inland's marketing scheme which should not be a part of a regulated utility's program.

Fourth, there are items contained in Inland's budget, the cost of which are too high and the figures in respect thereof must accordingly be decreased.

Fifth, Inland as a regulated utility is subsidizing both regulated and non-regulated companies through a deficient method of calculating intercorporate charges and a consequential failure to recover the full value and range of tangible and intangible benefits it provides.

Sixth, there are certain costs Inland has included in its rate base which relate to expenditures in respect of items which benefit shareholders as well as ratepayers. An item may benefit ratepayers one way, but benefit shareholders in another way. When that item's cost is included in the rate base or treated as an expense the effect is that the shareholders get a free ride. The Commission can correct this by allocating to the shareholders a portion of the cost of certain items.

Seventh, not enough has been done by Inland regarding the move to its service area, and a Commission directive in this regard is required."

(Transcript pp. 3019-21)

The proceedings commenced on September 22, 1986 and concluded on November 26, 1986 after 19 days of hearings including three days of argument.

The Commission has found the issues raised in this hearing to be most difficult to reconcile as the Commission attempts to ensure safe, secure and reasonably priced service for all customers and a stable environment to ensure that a

healthy utility will be maintained to provide a continuing level of highly valued service through not only the next year, but well into the future.

The Commission has deliberated and debated extensively the issue of the appropriate capital structure for Inland. As a result of extensive evidence on this issue the participants at the hearing developed widely differing models of the existing capital structure of Inland utility. Section IX of this Decision deals with the appropriate capital structure for regulatory purposes.

IV RATE BASE

Mid-year fiscal 1987 utility rate base is forecast to be \$142.5 million. Plant additions for 1987 are forecast at \$9.2 million, compared to actual additions of \$13.2 million (1986) and \$12.2 million (1985). Natural Gas for Vehicles ("NGV") fuel stations estimated at \$1.9 million (exclusive of overhead) are forecast as major additions to plant.

A significant component of plant additions in previous years has been extensions to outlying communities funded in part by the Distribution System Expansion Program("D.S.E.P.") and the Gas Extension Assistance Program ("G.E.A.P."). DSEP funding is no longer available.

As reflected in Appendix B, capital investments relating to traditional markets are forecast to decline but activity in related areas of merchandising and NGV are being pursued. However, major future capital investments may be required for peak shaving purposes if warranted by recent restructuring of Westcoast's tariffs or by changes in Inland's load profile.

I. Natural Gas for Vehicles (NGV)

Inland's Application provides for additions to plant in service of \$1.9 million for fleet and public NGV stations. Up to July 1, 1986 cumulative capital expenditures on NGV activities amounted to \$250,000. Forecast expenditures of almost \$2 million for 1987 demonstrates a dramatic increase in management interest in NGV (Exhibit 4, Item 27, p. 4).

Test year 1987 NGV sales are forecast at 133,000 GJ with a contribution at the gross margin level of \$519,000 (Exhibit 4, Item 27, p. 1) or \$3.90/GJ compared to the system average of \$1.22/GJ.

Inland was questioned by several parties regarding its NGV programs for the provision of compressors and dispensers along with a program to assist conversion of vehicles. Mr. Kadlec pointed out that the NGV market was the newest and one of the more profitable market available for expansion by Inland. However, he acknowledged that during the first half of 1986 expansion of NGV sales had been slower than hoped.

The Commission recognizes that NGV is a significant growth prospect for Inland. B.C. Hydro Gas has already demonstrated the inroads that can be made via this new market. Moreover, NGV sales have a desirable provincial impact by displacing imported oil with B.C. natural gas. British Columbia is currently a North American leader in this field.

In response to a request from Commission staff Inland provided a contribution analysis of the costs of NGV, summarized as Exhibit 4, Item 27, page 1. The evidence shows that the calculated rate of return on investment is presented on an incremental cost rather than an average cost basis. The practice of Inland is to only capitalize overheads directly applicable to the NGV projects (at a rate of approximately 5%) and not to apply full utility overheads as applied to other utility capital expenditures. For fiscal 1987 total overhead capitalized as a percentage of total capital additions represents 51.9% (Exhibit 88).

With respect to the incremental costing of overheads for NGV, the Commission believes it appropriate to continue the current practice while NGV development is in its fledgling growth period. However at some future date the NGV market will mature and should then be required to carry full utility overheads. Full allocation of overheads would then afford equal opportunity for other investors entering the market.

2. Pipeline Extensions to Chase/Sorrento

Considerable time at the hearing was spent reviewing the circumstances and costs related to the pipeline extension by Inland to serve the community of Chase. This extension received substantial funding from both the federal and provincial governments under D.S.E.P. and G.E.A.P. The original estimate of cost for the project was \$1,647,943 but the final estimate rose to \$2,225,181 (see Appendix C).

Inland pointed out that the increased cost of the project was a result of poor weather during construction and substantially more rock to be blasted than originally forecast. To assist in offsetting the increased cost of the project, Inland switched funding from the federal and provincial programs to increase the contributions, and the utility increased the expected revenue from customers under its six year mains extension test. Based on Inland's adjustments, the utility argued that it was within the bounds of a 20% overrun on the Chase and Sorrento projects, if the two projects were considered together. The Applicant, however, even though aware of the apparent cost increases did not seek any amendment to its Certificate.

The Commission considers the Chase project to be separate from the extension to Sorrento. Funding from the federal government was made on an individual project basis and the B.C. Utilities Commission issued separate certificates. The Commission will assess the final costs on the Sorrento project when that project is completed.

At the public hearing held by the Commission before awarding the Certificate to construct the extension to Chase, the Applicant advised the Commission that capital costs on project extensions could range up or down by 20%. The Applicant pointed out that more work than normal had been done on the estimates of the Chase extension and the utility had greater confidence in its forecast for that project.

The Commission recognizes that extension projects with significant fixed federal and provincial contributions create a leveraged situation where any cost overruns greatly impact the utility funding. Bearing in mind this leverage effect, the Commission believes the utility has an even greater fiscal responsibility with respect to projects where substantial public funding is provided. The Applicant conceded that the funding from the government bodies had been premised in part on the cost estimates provided by Inland.

With these factors in mind, the Commission is prepared to accept a cost overrun of 20% on the project cost estimate approved when the Certificate of Public Convenience and Necessity was issued for the Chase extension. If the Applicant had brought this matter to the attention of the Commission at the outset, through the appropriate Application, the above problem may have been avoided. The Sorrento project will be considered on its completion. The value to be used for rate base purposes for Chase is accordingly \$1,977,532. The amount disallowed should be depreciated at the approved rate and included in the cost of service.

3. Propane Air Plants

Inland testified that four propane air plants with a net book value of approximately \$400,000 were included in rate base but are currently not operational. The utility had included upgradings of these plants in its capital budget for 1985 for an expenditure of approximately \$100,000 to improve safety so they could remain operational under new safety regulations. However, even though the Commission approved the upgradings these expenditures were not undertaken and, as a result, the provincial gas inspection department no longer approved operation of the plants after December of 1985 (Transcript p. 2655).

Inland testified it was reviewing its overall gas supply and peak shaving requirements and these propane air plants could form a part. This work was not complete at the time of the hearing and so no commitment has been made on the status of the propane air plants.

Mr. R.B. Wallace, counsel for Industrial intervenors argued that the plants are no longer used and useful and do not meet current safety standards. His recommendation was to remove the plants from rate base (Transcript p. 2952).

The Commission, in agreement with Mr. R.B. Wallace, is concerned that Inland continues to carry the depreciated value of the plants on its books when they are no longer operational and so for the moment, has removed the net book value of the plants of approximately \$400,000 from rate base. These costs are to be held in Account No. 102 as a non-rate base category of "Gas Plant Held for Future Use". Depreciation is to continue to be taken as a cost of service in the normal manner and credited to Account No. 105 in a subdivision entitled "Accumulated Depreciation - Gas Plant held for Future Use".

At the same time, the Commission recognizes these plants could be valuable for peak shaving purposes, particularly in light of the escalation in Westcoast demand charges in the past few years. The Commission therefore directs Inland to complete a review of the future requirements of the propane air plants by December 31, 1987 with a report to be provided to the Commission. This report is to include details on the current book value, disposition value, preferred location for emergency and peak shaving purposes, value for peak shaving purposes, and expected upgrade costs for them to be made operational.

The propane air plants should be compared with other peak shaving alternatives including contracts with industrial customers. If the result of the studies indicate that these plants are no longer used and useful then an

accelerated write-off should be considered. At that time the Commission will further determine on the amounts held in Account No. 102. This may result in reinstatement or an accelerated write-off in view of the past service provided by these plants.

4. Merchandising of Natural Gas Appliances

On June 12, 1986 Inland applied for Commission approval permitting a promotional incentive program to allow new and existing customers to upgrade their own heating equipment for a small initial investment. In tandem with its new incentive program Inland had set in motion a dealer marketing program whereby Inland or its agents supplied and installed furnaces and water heaters, as well as a full range of gas appliances.

Authority to sell appliances is contained in Section 23(2) of the filed Tariff, general conditions, approved February 1977, which states, "The Company may sell gas appliances on a cash or finance plan basis and make reasonable charges for these services". Inland does not have authority in the tariff to install appliances.

In June 1986 the Commission received a number of complaints from concerned contractors who derive their income from the sale, installation and repair of furnaces, water heaters and other equipment. By Order No. G-45-86 the Commission approved Inland's promotional incentive program, but because of concern about Inland's merchandising activities, requested submissions to be heard at the revenue requirements hearing. The objective must be a program which is fair to all parties - contractors, customers and Inland.

Inland's program was described in Mr. J.L. Randall's letter of July 15, 1986, filed as Exhibit 4, Item 21(a), pp. 1 - 3 and is reproduced as Appendix D to this Decision. In argument Mr. C.B. Johnson, counsel for the Applicant, stated :

"What I think is at the bottom of this, Mr. Chairman, it is my submission at least, that the contractors wish the utility to spend money on promotion. They are desirous of this occurring. They

weren't aware that part of the Inland program involved going out and actively knocking on doors, but the contractors want Inland to spend the money on promotion and then in essence hand them over customers. They really want the expenses involved with promotion to be utility expenses and the profits associated with the sale of the appliances, the furnaces, to be a profit to the contractors.

And it is my submission that if the expenses for promotion of the sale are to be borne by the utility and I suggest that it is in the interest of the customers of a utility and in the interest of increased gas sales to promote these appliances. If the expenses for promotion are to be borne by the utility, then the benefits, i.e. the profits from the sale of the appliances, should be to the utility."

(Transcript pp. 2831 - 2832)

Mr. V.J. Traynor, Executive Vice President, Mechanical Contractors Association of British Columbia, gave evidence at the hearing (Exhibit 21) opposing Inland's merchandising program. This is reproduced as Appendix E to this Decision. In argument Mr. Traynor stated:

"We wish to express again our contention that the type of competition that Inland Natural Gas is proposing is made possible only by their special status which is granted by the Utilities Commission. The advantages of Inland Natural Gas with this special status are extensive.

They include the areas of capitalization, administration and overhead, name, credit information, billings and direct-from-manufacturer ordering. We believe that the testimony of Inland Natural Gas during these hearings amply justifies our point that in the areas of capitalization, administration and overhead the utility has an advantage over any and all of their competition."

(Transcript pp. 3057 - 3058).

The contractors argued that Inland should restrict its merchandising efforts to advertising and promotion and let the wholesalers and contractors do the actual selling, installing and servicing of gas equipment with the end result being an increase in the volume of gas sold by Inland (Transcript p. 3065).

Inland testified that the principal purpose of its merchandising efforts was to increase gas volumes sold (Transcript p. 607). Its "test" program covered 72 % of its customer base (Transcript p. 923); and the merchandising function costs as shown on Exhibit 4, Item 21(c) were costed on an incremental cost basis, with no general and administrative costs allocated (Transcript p. 920). The Commission notes that with regard to replacement equipment no increase in gas consumption would result and in fact if high efficiency equipment is installed a reduced consumption may well take place.

The Commission learned there had been no contact by Inland with the Mechanical Contractors Association to determine whether a joint program might be undertaken (Transcript p. 811). Before the hearing completed two meetings occurred but the Commission understands these to have been unsuccessful in reaching a consensus between the contractors and Inland.

The Commission has considered the concerns expressed by the Mechanical Contractors Association as well as the approval given by the Commission to Inland to sell appliances in 1977 as set forth in Section 23(2) of the filed tariff. The Commission is particularly concerned with what from the evidence appears to be a pricing advantage accruing to Inland from incremental pricing. From the contractors' perspective incremental pricing will preclude them from competing and since the merchandise sales program is not profitable without an income credit from additional gas sales, a hardship could result to Inland's customers and shareholders while benefiting the new equipment purchasers in the short-run.

In the interest of ensuring fair and equitable competition in the marketplace and not inhibiting the market penetration and availability of appliances, the Commission believes furnaces, fireplaces and water heaters sold by Inland must bear the full cost of sale including full overheads, but all other appliances can continue to be priced incrementally.

The exception to the above would be that if Inland wishes to be involved in special initiatives or incentives with regard to gas furnaces, fireplaces and water heaters the same initiatives and incentives must be made available to dealers and contractors.

While the Commission does not want to remove Inland from the appliance sales market entirely at this time, it does want to remove any artificial advantage Inland might have created through its adoption of an incremental pricing policy. A fully competitive market would be of benefit to all parties. In order to ensure a smooth transition from incremental pricing and permit an orderly reduction in inventory, if this is in fact required, the revised pricing policy will become effective April 1, 1988 for gas furnaces, fireplaces and water heaters.

In the interim, if the inventory reduction is required, Inland must not adopt a merchandising strategy which would further imperil the ability of small business operations to compete and to provide the appropriate support service to Inland after April 1, 1988. Commencing in September 1987, Inland will provide the Commission, on a monthly basis, a revenue and cost report with regard to the sale of furnaces, fireplaces and water heaters.

5. Deferred Interest Account

The Commission in its Decision dated March 18, 1981 approved the establishment of a deferred interest account to absorb volatile fluctuations in its short-term interest rates.

Since the early part of 1986, short-term interest rates appear to have stabilized. In fact, Inland's subsidiary, Columbia, requested and received permission from the Commission in fiscal 1986 to allow the cessation of a similar account in favour of a forecast rate.

The Applicant explained that (Transcript p. 2695) "while the percentage of short-term debt in Columbia is a greater component of the capital structure, the overall debt levels are significantly lower. Any swing would not impact on

the Inland earnings per share as greatly as it would in Inland if those swings existed." The Applicant also stated that (Exhibit 4, Tab 4, p. 2) "Previous evidence of the Company's financial witnesses has noted that the use of the interest deferred account has been one of the steps taken by the Commission to minimize regulatory risks . . . an alternative would be to include a prospective issue of higher cost fixed rate long-term debt in the capital structure."

Dr. Evans testified that (Transcript p. 1209) "I think it would be advantageous to all concerned to keep that account, just as I do the strike adjustment provision. None of these things in and of themselves at this juncture, I would venture to say, would probably cause me to move-off of my recommendation, but they all contribute to the perception on the part of investors that this Commission is doing everything it can to reduce regulatory risks, and provide a reasonable regulatory environment in which this company can operate."

In light of the above evidence, the Commission approves the continuation of the deferred interest account. However, in order to protect utility customers, and in view of Inland's greater diversification and investment in non-utility activities, the Commission directs that only deferred interest pertaining to the utility operation should be apportioned for rate base treatment and amortization. Deferred interest charges must be calculated in accordance with the instruction contained in the January 11, 1985 Decision (p. 9). Furthermore, complete details must be available for audit by Commission staff.

The Commission has incorporated a short-term rate of 8.5% in the capital structure to reflect the current trend in short-term interest rates.

V SALES

Fiscal 1987 total sales of 48,029 TJ were forecast 5% lower than 1986 normalized projected results largely due to reduced forecast sales to large industrial customers and Columbia. Although purchase contracts had not been signed by Northwood Pulp, Prince George Pulp, Westar Timber and Weyerhaeuser to take effect from November 1, 1986, Inland included these loads in its forecast sales volume.

Inland's large industrial sales forecast was derived from the customers' own projections (Transcript p. 838) and the Commission accepts those estimates.

The Applicant forecasts use per residential customer at 106 GJ in forecast 1987. Records for 1985 and 1986 showed normalized use in fiscal 1985 and 1986 of 107.1 GJ and 107.4 GJ respectively (Transcript pp. 541-544). The Commission recognizes forecast use per account is judgmental, and the Applicant's estimate of 106 GJ is reasonable.

Sales to Columbia have normally been subject to particular review in the Inland hearings due to the non arms-length relationship. Constraints on potential sales are Columbia's 60% load factor with Alberta & Southern ("A & S"), the price differential of Inland and A & S gas, and availability of Inland gas. Gas deregulation has introduced added uncertainty from the revenue requirement perspective as gas purchase opportunities may influence the ability of Inland to supply Columbia under certain circumstances.

At the outset of the hearing Inland requested the Commission to approve the establishment of a special deferral account to be operated as follows:

"Inland, in view of the continued uncertainty that exists both for pricing in Alberta and pricing in British Columbia, proposes and seeks Commission approval of the establishment of a deferral account which would be pegged at the amount projected, the sales volumes and the revenue projected, and then deviations from that projected revenue would be recorded in a deferral account.

If Inland were able to make increased sales or sales at a higher margin to Columbia, that extra revenue would be put in a deferral account. Conversely if the sales volume or the margin fell below that forecast the shortfall would be put in a deferral account to be dealt with in future years."

(Transcript p. 43)

Mr. Solly, Vice President, Operations testified (Transcript pp. 2389 - 2413) on a policy issue concerning the shift of forecast sales to Columbia from fiscal 1985 to fiscal 1986. The record shows that actual fiscal 1986 sales were 1,700 TJ more than forecast partly due to a shift of sales of approximately 500 TJ from fiscal 1985 to 1986 (Transcript p. 1460). This shifted revenue between the two fiscal years, although the gas was moved within the same gas contract year, November 1, 1984 to October 31, 1985 (Transcript pp. 1457 - 1460).

Considering the above circumstances and the request of the Applicant, the Commission approves the establishment of the requested deferral account to commence July 1, 1986. It is to operate in the manner proposed on Transcript p. 43, as quoted above. The balance of the account is to be carried in rate base as a deferred charge or credit with the appropriate cost attributed thereto.

VI GAS PURCHASES

Inland purchases all of its natural gas, except for that exchanged with Columbia, from Westcoast. In turn, Westcoast purchases natural gas from the B.C. Petroleum Corporation. Two matters respecting gas purchases arose at the hearing and the Panel's views on these matters are discussed below.

I. Westcoast Costs

Inland's Application includes a Westcoast demand charge of $4,900 \text{ } 10^3 \text{ m}^3$ per day at a rate of \$229.457 per 10^3 m^3 per month, meaning that the Westcoast capacity charge is forecast to be \$13,492,000 (Exhibit I-08-01).

The basis for the contract demand volume is Mr. R.T. O'Callaghan's letter of October 31, 1985 to Westcoast setting out proposed terms for supply November 1, 1986 to October 31, 1987 (Exhibit I-08-03). Inland's nomination for firm gas sales was for $4,500 \text{ } 10^3 \text{ m}^3$ per day, but with a right of first refusal to acquire a further $400 \text{ } 10^3 \text{ m}^3$ per day.

With the dramatic shift in pricing from commodity to demand in recent years (\$75 per 10^3 m^3 per month, May 1985 compared to \$486 10^3 m^3 /mo., January 1, 1987) it is clear that Inland must optimize its gas supply/demand profile. Questions were raised in the hearing on reduced nominations, increased peaking service, increased curtailment, concessions from industrials, use of storage and other methods potentially usable by Inland (Transcript pp. 369 - 371). No savings reflecting optimization of the supply/demand profile have been reflected in this Application or appear as firm alternatives for the immediate future.

The Commission finds that Inland's actual contractual commitment to Westcoast of $4,500 \text{ } 10^3 \text{ m}^3$ commencing November 1, 1986 has been maintained throughout the winter season due to warmer than normal weather conditions in

its service area. While Inland may have required additional gas if unusually cold weather had occurred, the fact is that Inland did not incur the added expense and should not recover extra revenue from customers for the 1987 fiscal year. The Commission has also reviewed Inland's expenses for peaking and overrun gas requirements, and finds that the actual expenses do not exceed those budgetted for. Therefore, the budgetted expenses are accepted.

At the hearing Inland gave an undertaking to provide further information with respect to certain gas supply matters. By letter dated May 29, 1987 Inland adjusted its cost of A & S gas to 51¢/GJ, from 74¢/GJ, and calculated a total saving of \$1.1 million for the 400 10^3 m^3 contract demand reduction between November 1, 1986 and June 30, 1987. This account as set up by Order No. G-32-87 dated June 2, 1987 is now refundable to Rates 1 to 10 customers together with interest, and is exclusive of any other refund calculated in this Decision.

At the request of Commission staff the Applicant submitted a pro forma automatic fuel adjustment clause [Exhibit 4, Item 8(e)]. Such a mechanism is intended to deal with a mix of gas costs purchased from a number of different suppliers. The Commission considers it premature at this time to set down a formal mechanism and so future unit demand and unit commodity changes are to be passed through to customers as they have been in the past with formal Application and acceptance by the Commission.

2. Deferral on Account of "Hot Gas"

In the Spring of 1985, Inland's gas purchases from Westcoast contained a higher energy content than forecast, causing an abnormal variance with unanticipated revenues being earned. This resulted from Inland purchasing a lower volume of gas from Westcoast (due to the higher btu content of the gas) while selling that gas to its customers based on the energy content of the gas.

In May 1985, Inland proposed to the Commission that the gas cost savings identified at approximately \$1 million, be accrued and recognized in fiscal 1986. Inland's 1986 forecast at that time targeted the allowed return on equity at 15.75% after including the full \$1 million fortuitous revenue in 1986 income.

On that understanding, Inland's request was approved by Order No. G-63-85. In the covering letter to the Order the Commission put Inland on notice that a review of fiscal 1985 and 1986 revenue requirements were to be undertaken for the Commission to determine whether a public hearing would be necessary (Exhibit 105).

By letter dated August 21, 1986, Inland further requested that income recognition as approved by Order No. G-63-85 be amended to allow for the amortization of the deferred credit to be spread evenly over a two-year fiscal period, 1986 and 1987 (Exhibit 106). This request was approved by Order No. G-54-86 subject to review at the time of the hearing.

Mr. R.B. Wallace, Counsel for the industrial intervenors, argued that heat content is a cost of gas item which naturally should be passed through to customers (Transcript p. 2924). The Commission is satisfied that although the full amount has not been passed through directly in rates as Mr. R.B. Wallace suggested, the full amount of revenue has gone to the customers. Half of the gain was recognized in fiscal 1986 without which a general rate increase may have been necessary. The remaining 50% is to be recognized in fiscal 1987, a test year for rate-making purposes.

VII OPERATION AND MAINTENANCE EXPENSE ("O & M")

The Commission has used the approved level of fiscal 1985 O & M expenses as the benchmark in the review of appropriate expenses for fiscal 1986 and 1987 (see Appendix F). Even though actual 1985 expenses exceeded the approved level, the Commission in these circumstances considers the approved levels to be a more objective base level for the following reasons:

- (a) Fiscal 1985 was the last test year for revenue requirement purposes.
- (b) Today Inland's organization has greater involvement in non-utility activities, therefore fiscal 1985 presents a clearer picture of baseline costs to the Commission.
- (c) Depending on the time frame and circumstances which may arise, the Commission accepts Decision-approved levels of expenditure for comparative purposes. Actual levels of expenditures are vulnerable to abnormalities.

Comparing the 1985 Decision with forecast 1987, the Applicant forecast total 1987 O & M expenses at a level of \$2,440,000 greater than the 1985 Decision, or approximately 14% higher. Approximately 30% of the increase represents increased insurance expense. The overall increase represents a 14% increase over two years while inflation has been about 7% over the same period. Growth in customers served is forecast at about 7%.

The evidence shows \$2,440,000 is represented by increases in the following major cost components:

Gross Payroll, net of transfers	\$734,000	7%
Other Employee Benefits, net of transfers	(203,000)	(12%)
Insurance	808,000	358%
Materials and Services, net of transfers	1,101,000	25%
	<u>\$2,440,000</u>	<u>14%</u>

(Ref: Exhibit 4, Item 23, pages 1-3;
Exhibit 14A, page 2, and Revisions)

1. Shift of Costs from the Field to the Head Office

The total labour force is forecast to reduce by 26 people from the 1985 Decision level. This is represented by a decline of 39 people in Operations and Construction but with increases of seven in Sales and Service and six in Vancouver Office (Exhibit Vol. 4, Item 23, p. 4).

Aggregate remuneration of Vancouver office employees charged to utility operations increased to \$5,520,000 (1987) from \$5,020,000 (1985), an increase of 10%. On the other hand aggregate remuneration in operations and construction has declined to \$4,336,000 (1987) from \$5,672,000 (1985), a decrease of 23% (Exhibit 14, page 10).

This trend is caused in part by a decrease in mains and service activity in the traditional market. At the same time however, it seems deregulation and NGV market development has increased the management cost of utility operations in the short-term with the prospect of benefits flowing through to all classes of customer in the future. A third reason is the increased activity in non-utility operations.

2. Allocation of Costs to Subsidiary Companies, Regulated and Unregulated

Since 1985, Inland has increased its diversification into non-regulated operations, the principal activities being oil and gas exploration, and gas marketing. Indications of the increase in activity and allocation of intercorporate charges for the years 1985-1987 are shown on Exhibit 40A attached to this Decision as Appendix G.

(a) Charges to regulated subsidiaries

Inland's regulated subsidiaries include Columbia Natural Gas Limited, Fort Nelson Gas Ltd., Grande Prairie Transmission Co. Ltd. and Peace River Transmission Company Limited. Since 1969, the appropriate charges to

Inland's subsidiaries have been redetermined every three years, by a review of the time spent by Head Office personnel on subsidiary matters (Exhibit 4A, Tab I, p. I) In 1981 a management audit by Touche Ross & Co. concluded that "the inter-company charges to the subsidiaries are calculated in accordance with sound cost allocating principles . . . and have been accounted for on a consistent basis since 1969." (Exhibit 89).

Prior to 1985, Inland's investment was predominantly in regulated operations. The method of allocating intercorporate charges was less contentious then since charges to each subsidiary were scrutinized by the respective regulatory agency. The Commission concluded in 1987, at least with Inland's charges to Columbia Natural Gas Limited, that "although the Commission accepts that the existing method of allocation may be reasonable, it should be reviewed periodically to account for changes in operation and circumstances." (Columbia Decision dated January 21, 1987, p. 19).

(b) Charges to non-regulated subsidiaries

Companies in this category include Inland Gas & Oil Ltd., Inland Natural Gas Marketing Ltd. and Inland Development Co. Ltd., and other joint venture activities.

Evidence presented in this hearing indicated activities as follows:

"In the 1986 fiscal year Inland Gas & Oil Ltd. (formerly St. John Gas & Oil Co. Ltd. ("IGO") became more active in oil and gas exploration, initially through a joint venture arrangement with Esso Resources of Canada Ltd. with respect to one well in the Deep Basin area of B.C.

In December 1985, IGO together with Trans Mountain Petroleum Ltd. ("TMP"), a wholly-owned subsidiary of Trans Mountain entered into a joint venture ("the Canadian Joint Venture") with Canadian Hunter Exploration Ltd. ("Canadian Hunter").

Under the Canadian Joint Venture IGO and TMP each agreed to contribute \$12.5 million to fund a \$40 million exploration and development program. Canadian Hunter agreed to contribute the remaining \$15 million."

(Exhibit 4A, Tab I, p. 15)

"In August, 1986, Inland Gas & Oil Corp. ("IGO Corp") and Trans Mountain Oil Pipe Line Corporation ("TM Corp.") executed a joint venture agreement with American Hunter Inc. whereby IGO Corp. and TM Corp. each committed \$3.5 million to fund a \$7 million exploration and development program, primarily in North Dakota. American Hunter Inc. is a wholly owned subsidiary of Canadian Hunter.

Upon the earlier of the expenditure of these funds on June 30, 1987 IGO Corp. and TM Corp. will each earn a 25% working interest in all joint venture lands and a 42-1/2% working interest in the first well spacing unit to be drilled in each project area containing the joint venture lands."

(Exhibit 4A, Tab I, p. 16)

"On April 30, 1986, Inland Natural Gas Co. Ltd. formed a natural gas marketing company called ING Marketing Ltd. which provides industrials with those gas acquisition services which they are least able to provide themselves.

The services provided through Inland Gas Marketing Ltd. are as follows:

- Maintain supply/producer data base,
- Log of all consummated and proposed transactions,
- Prompt notification of all sales and purchase tenders,
- Negotiation assistance between producers and subscribers,
- Arrange Westcoast transportation for delivery to Inland,
- Arrange Inland transportation through Inland's system
- Verify billing.

These services will encourage industrials to contract for a variety of supplies to hedge against price changes. Moreover, these responsibilities will help provide gas supply diversity which will maintain a steady and reliable energy supply.

ING Marketing Ltd. hired a full time Vice-President and General Manager on September 1, 1986, to manage its affairs."

(Exhibit 4A, Tab I, p. 17)

Inland's unconsolidated financial statements for the year ending June 30, 1986 states in Note 6 to the Accounts:

"6. GUARANTEE

The Company has guaranteed the performance of all the obligations of Inland Gas & Oil Ltd. which is committed to spend \$8.5 million on petroleum and natural gas exploration in 1987 under a joint venture agreement."

(Exhibit 55)

The Commission views the guaranteeing by Inland of obligations of its non-utility subsidiaries as a potential imposition of a burden on the customers. The Commission directs the company to investigate this problem and propose solutions in its next revenue requirement hearing.

The methodology employed by Inland to account for non-utility charges is to maintain a formal time-keeping system whereby each employee who dedicates time to a subsidiary company completes monthly timesheets. By these timesheets the company can monitor the type of activity and number of hours devoted to each subsidiary company, regulated and non-regulated (Exhibit 4A, Tab 1, pp. 2-3).

Mr. Kadlec stated in evidence:

"Inland Natural Gas isn't going to give a privileged arrangement to Inland Marketing, or Inland brokerage, let's call it, so we don't get confused here, that they would give to any other, and it's as simple as that . . . And if there's any confusion on that, I'd like to assure that won't happen." (Transcript pp. 138-139)

". . . I can assure you that there's no advantage to, in it to us to burden the utility with the costs that rightfully belong to another company." (Transcript p. 403)

"If you're saying that if we improperly charge our time to the utility rather than charge it to the company that we're spending our time, it puts a burden on the utility and I guess you're suggesting it's an easy way to do it and provide lower-cost service to the other company that's involved." (Transcript p. 405)

The issue of intercorporate charges and potential for cross-subsidization was of major concern to all intervenors in the hearing. Evidence shows that non-utility subsidiaries (both regulated and non-regulated) have not been charged for Board of Directors meetings (Transcript pp. 2242-2249), and Annual Report costs (Exhibit 97). Questions were also raised with regard to allocation of leasehold costs to subsidiaries (Exhibit 99), and intangible benefits conferred by Inland to its non-regulated operations such as privileged information (Transcript pp. 129, 567), affiliation and name recognition (Transcript pp. 138, 2646-2651).

The Commission is very concerned that it is becoming increasingly difficult to determine the extent of utility resources used for non-utility purposes. Inland's method of recording non-utility charges depends heavily on the initiative of the employees recording their time and therefore may result in inadequate allocations to non-utility functions. The record already shows that some costs have not been charged to non-utility activities.

As well as the direct costs to be allocated to non-utility ventures the non-utility companies benefit from a pool of skilled labour maintained at utility customer expense. It may be appropriate for the utility to charge a retainer for the availability of staff and facilities. The utility may also consider charges for the provision of intangible benefits such as the association with the utility name and guarantees provided by the utility.

The Commission considers that it must ensure the utility customers bear their fair share of costs but to the extent practical do not bear unrelated costs. To date the attitude of Inland is to allocate costs to the utility except where the costs can be identified as non-utility costs. This results in a bias in cost allocation to the benefit of non-utility ventures. The Commission holds the view that any bias (if unavoidable) should flow to the benefit of the utility customers since the non-regulated ventures have been initiated from the resources of the utility.

In recognition of the foregoing the Commission increases the charges to non-utility ventures by \$50,000 and will review this matter again in the next proceeding.

VIII OTHER MATTERS

I. Normalization

Several questions were raised during the proceedings on the methodology used by Inland to "normalize" actual results. Principal normalizing adjustments permitted by the Commission are adjustments for weather, strikes, curtailments and for variations in the rate of short-term interest. The Commission holds the view that the process of normalization is important to all participants in the regulatory process as regulatory returns are based on forecast test years assuming normal conditions. However, numbers produced are notional and the basis of calculation is not an exact science.

The financial markets rely on actual results as a general rule and, all things being equal, the regulatory process is well served if normalized numbers are close to actual numbers. However, deletion of certain normalizing adjustments may expose the utility to unnecessary risk and this is not an option considered by the Commission at this time.

In the Commission's view it is an opportune time to examine the methodology used to calculate the normalizing adjustments as approved by the Commission. The Commission has reference particularly to the mechanics of the strike adjustment and generally, use of a normalized retained earnings to match the income statement adjustments.

The Commission has therefore directed Commission staff to review normalization methodology with the Applicant as soon as possible. Depending on the outcome of this review the Commission may request a written submission from Inland.

2. Separation of Utility and Non-Utility Activities

The subject matter of separation between utility and non-utility activities was discussed at Transcript pages 388-390 :

Mr. B.J. Wallace: The Pipeline Review Panel had a recommendation, which this note is found at 5.2.(ii), which I think I'm quoting correctly as being a recommendation that there be a separate Board of Directors with complete separation of policy-making, management and accounting?

Mr. Kadlec: I don't know if it says separate Board of Directors, but they don't feel it should be part of the utility, is my understanding.

The Chairman: Mr. Johnson?

Mr. Johnson: Mr. Wallace is quoting, I think accurately, but referring to pipeline companies. The Pipeline Review Panel distinguished between pipeline companies, and distribution companies, and has a separate section which deals with distribution companies.

The Chairman: All right, thank you, Mr. Johnson

Commissioner Newlands: To save the anticipation, Mr. Johnson, does the distribution company say the same thing?

Mr. Johnson: No, they, I think it's fair to say that they realize that it's a much more complex situation, and they're not quite so certain as to what could happen with distribution companies.

Mr. B.J. Wallace: Well, then, let me just read what it says about that at 5.2 (iii) under the heading, "Degree of Separation - Distribution Companies", and I'm reading the second paragraph, "The degree of separation needed in the activities of a distribution company is the same in principle as for transmission companies, although the Panel recognizes the greater complexity of the activities of the typical distribution company, and therefore the need for a difference in practice."

I think that puts it all there. Mr. Kadlec, you made the observation before that these are only recommendations, and my question is, do you agree with that recommendation?

Mr. Kadlec: I think there has to be separation. The Board of Directors, if we're the major shareholder, we can appoint, if that's a concern, we can appoint a Board of Directors as shareholders of that company that are not on the Board of Inland.

I don't think the important question is the Board of Directors, so much as whether it's utility or non-utility.

Mr. B.J. Wallace: Is it Inland's policy to work towards the degree of separation which has been recommended by that report?

Mr. Kadlec: Well, we'll, I guess I'm not even convinced at this point in time there is going to be a role for Inland Gas Marketing. But, as the whole area develops we'll be re-examining that constantly, as we are today. It's, I don't find the Board of Directors particularly—if they say Board of Directors for the transmission companies, I don't know why they would, but if that further degree of separation is necessary, I'd be quite happy to do it.

I'm more concerned over whether or not Inland Gas Marketing can provide a service to the customer, and if it can't, then it will be disbanded. If it can, and if it appears that as we get through the contractual constraints that are out there, we will definitely look at separating it as much as we can from the utility, even further than what it already is.

Based on the above exchange, the Commission directs the Applicant to fully examine the subject of separation, with a report to be provided to the Commission by March 4, 1988 as further discussed in Section IX.

3. Strike Adjustment

The Commission has used a strike adjustment in the setting of utility rates for some years. In the recent Columbia hearing the subject was discussed and in its January 21, 1987 Decision the Commission commented (page 16) :

"The Commission will not require the Applicant to change its method of strike adjustment allowance at this time. However, the purpose of the strike adjustment allowance is not to guarantee the Applicant recovery of all previous losses due to strike but is a vehicle to avoid requiring the Applicant to make forecasts for a test year. The Commission will continue to consider other methods which could yield more equitable results to both the Applicant and its customers."

The issue was also raised in this hearing, the main argument being that Inland is awarded a risk premium as reflected in the rate of return on common equity which takes into account financial and business risk. If the risk premium covers the risk of strikes it follows that further protection should not be afforded through the strike adjustment.

The Commission as a result of concerns raised by others at the hearing directs its staff to review the matter with Inland and report by December 31, 1987.

4. Head Office Location

The Commission believes that to the extent possible and efficient, a utility's staff should be located within the service area. In the most recent Inland Decision of January 11, 1985 the Commission stated:

"(the Commission) will expect the Applicant to keep this matter under active consideration to determine whether or not departments or portions thereof can be advantageously relocated in the future."
(page 20)

Although the Applicant has engaged an outside consulting firm to review relocation there have been continuing significant leasehold improvements at the Head Office (Transcript pp. 1933 and 2080). While the lease on the Head Office premises expires in 1988 with option for renewal, the shift of costs has been in the direction of greater spending at Head Office and lower spending in the field.

In consideration of recent activities the Commission directs Inland to file a report with the Commission by December 31, 1987 citing advantages and disadvantages of relocating all or part of the utility head office into the service area. The analysis is to include a statement of (a) financial and (b) economic costs and benefits of such a relocation. All leasehold improvement expenditures should be minimized until the study is completed and a review thereof made by the Commission.

5. Hearing Costs

In argument Ms. Vance raised concerns with regard to the hearing costs in general and the need for the incurrence of specific cost at all such as the rental of a "work room" at the Hotel Vancouver, when the Applicant's head office is also in downtown Vancouver. The Commission is concerned with regard to hearing costs and believes all reasonable steps must be taken to minimize them. In addition, the Commission is concerned that an inequity may exist inasmuch as the Applicant can be allowed the full recovery of its costs while other participants must bear the entire costs regardless of the contribution made in the proceeding. One method to overcome this potential inequity would be to permit the Applicant to recover, through its rates, only the percentage of its costs upon which it has been successful. In other words, if the Applicant were granted the full revenue requirements sought, then the full amount expended would be recovered. Similarly, if it received less than that applied for, a lesser portion would be recovered through the rates, with the balance absorbed by shareholders. This will be given further consideration in the next proceeding.

Total hearing costs exclusive of intervenors costs which are not recoverable pursuant to the Utilities Commission Act are to be recovered over two years commencing in fiscal 1987. These costs total approximately \$290,000.

IX CAPITAL STRUCTURE

The determination of an appropriate capital structure for rate-making purposes for the utility operation of Inland Natural Gas Co. Ltd. became the focus of this 1986 Revenue Requirement hearing. The Applicant and the intervenors agreed that the interlocking relationship between Inland and Trans Mountain is a unique one, and no other Board or Commission in the Canadian regulatory environment has had to deal with this contentious area (Transcript pp. 2749 - 2751).

The Applicant utilized a capital structure for rate-making purposes that included a common equity component of 35.49%. Intervenors disagreed and maintained that the proper common equity component for rate-making purposes should be 20%. In its simplest form, the difference arises because the Applicant applied a "corporate capitalization" approach while the Intervenors applied a "consolidation" approach.

The above divergence of views resulted from the takeover of Trans Mountain. Dominion Bond Rating services (D.B.R.) in Exhibits 79 and 80 reported as follows:

"THE TAKEOVER

Inland Natural Gas Co. Ltd. was involved in a lengthy takeover battle, where it ultimately bought 67% of Trans Mountain Pipe Line Co. Inland issued treasury common shares and acquired 67% of Trans Mountain including \$5.4 million of shares that it owned previously. The effects of this takeover was:

- (a) The creation of \$19.2 million in goodwill, which was allocated to land and land rights - items which are not depreciated.
- (b) Trans Mountain had acquired 93.5% of the shares of Inland. Thus, with the takeover, one of the main assets that Inland was taking over was itself. It had cost Trans Mountain close to \$60 million to purchase Inland shares.

- (c) Had Inland taken over Trans Mountain for cash, it would virtually have wiped out all of Inland's equity since, in effect, it would be taking over itself. Thus, the equity that Inland has largely emanates from the Treasury stock that it issued for Trans Mountain shares.
- (d) The net effect of this transaction on Inland's balance sheet was negative, because equity declined after all adjustments, and DBRS treats minority interest as neutral in the calculation of asset base liquidity ratios."

One year later the December 14, 1984 report maintained the reduced ratings and stated, "Additional equity (was) needed to bring the balance sheet on side and help interest coverage ratios."

DBRS' analysis of liquidity contained the following:

"Debt levels were unchanged on a consolidated basis in 1984 and still remain too high for the size of the equity base."

"The balance sheet, excluding Trans Mountain, is more reasonable but with Trans Mountain, the Company still requires about \$30 - 40 million additional equity to bring its balance sheet into line. Conversion of \$45 million in floating rate bank borrowings to fixed rate instruments has helped lock in some fixed rate debt, but the level of debt is still too high for the equity base. This was all caused by the addition of Trans Mountain which was debt financed."

The February 28, 1985 report contains the following passages:

"Inland, however, has a very weak balance sheet, stemming from the fact that it controls Trans Mountain, and Trans Mountain in turn has a considerable interest in Inland Common shares. This hurts Inland's balance sheet in two ways: (1) Trans Mountain debt is consolidated with Inland; (2) Inland's equity base is reduced by the proportional ownership of Trans Mountain in Inland shares. As a result, Inland has too much debt for the equity base, and must either have Trans Mountain sell its Inland shares or issue new common shares to bring its balance sheet into line. Unless additional equity is added, the rating is in doubt."

"Consolidated balance sheet ratios are weak, and without further injection of equity, interest coverage is expected to decline further in 1985. The latter is being restricted by the large amount of interest paid for borrowings related to Trans Mountain, and the loss of deferred taxation since early 1984. What is needed is sale of Inland shares by Trans Mountain to restore the balance sheet, or a common share issue by Inland directly. The way things stand now, there is simply too much debt for the equity base."

On November 15, 1985, DBRS had this to say:

"The consolidated balance sheet remains weak, and the sale of 20% of its Trans Mountain Pipe Line (TMPL) investment to a subsidiary only corrects the problem artificially."

"The balance sheet of Inland, excluding TMPL, is reasonable, compared to other gas utilities, and debt levels are just under 50% of total capitalization."

"Interest coverage for Inland on a stand-alone basis declined to 2.3 times in 1985, but remains comparable to other utilities."

"The balance sheet, excluding TMPL, should remain at reasonable levels in 1986 and will include additional investment of \$15 million in its utility system."

The Applicant's auditors, Thorne Ernst and Whinney, expressed their opinion on the issue of balance sheet presentation of reciprocal shareholdings (Exhibit 103):

"Inland Natural Gas Co. Ltd. ("Inland") currently owns 47.1% directly and owns 50% of the common shares and 100% of the participating preferred shares of Transland Investments Ltd. ("Transland"), which in turn owns 20% of the outstanding common shares of Trans Mountain Pipe Line Company Ltd. ("Trans Mountain"). Trans Mountain owns 45.6% of the issued common shares of Inland. Prior to the sale of a 20% interest in Trans Mountain to Transland, Inland was required by generally accepted accounting principles to consolidate its investment in Trans Mountain. After the sale of the Trans Mountain shares to Transland, Inland has the option of accounting for its investment in Trans Mountain on either a consolidated basis or by the equity method.

Under these circumstances, there exists two accepted methods of accounting for the reciprocal shareholding: the liquidation method and the treasury stock method.

Inland has chosen to continue to consolidate Trans Mountain in its consolidated financial statements because of its significant continuing interest in the company, the fact that this presentation is consistent with that of previous years and because continuation of consolidation was felt to be less confusing to Inland shareholders."

Inland's 1986 Annual Report at page 22 states the following:

"The Company sold 20% of the outstanding shares of Trans Mountain to Transland Investments Ltd. in September 1985. The Company owns 50% of the common shares and 100% of the participating preferred shares of Transland. As a result of the Company's interest in Transland together with its direct ownership of Trans Mountain, the consolidated financial statements continue to include 67.1% of Trans Mountain."

I. Application

Inland submitted in its original Application a utility capitalization comprised of:

Long-term debt	40.15%
Unfunded debt	14.07%
Preferred shares	10.29%
Common equity	35.49%

The derivation of the Applicant's capital structure can be traced through Exhibit 4, Tab 17(b); 66 and 67 (attached as Appendix H).

It can be seen that Exhibit 4, Tab 17(b) commences with the consolidated capital structure. The Applicant then reversed all consolidation entries to arrive at Inland "legal" (Exhibit 55 of this hearing).

"Legal", in this context, means the unconsolidated financial statements of Inland Natural Gas Co. Ltd. in which Inland's investments in subsidiary companies are shown at cost. These financial statements are prepared solely for presentation to income tax and regulatory authorities and are not for issuance to shareholders (Exhibit 55, Note 1 to the financial statements - basis of accounting).

The Applicant further disaggregated Inland legal into (a) Inland "utility", (b) "other utility", and (c) "non-utility" in Exhibit 4, Tab 17(b). The sum of Inland utility and other utility, excluding Trans Mountain, is the amount put forward by the Applicant for regulatory purposes. This amount has been referred to as Inland's "corporate capitalization", a procedure Inland has followed since 1982. For regulatory purposes the above-mentioned jurisdictional utilities are individually regulated on the basis of their own capitalization.

Mr. Kleven, Inland's witness, testified that valuable assets were expended by Trans Mountain in obtaining shares of Inland; these shares represent value, can be sold and have the right to dividends. Therefore, he argued the cost of Inland shares held by Trans Mountain, for the purposes of determining the equity of Inland utility, should not be deducted from the parent's equity.

On page 2338 of the transcripts, Mr. Kleven stated:

" . . . that Trans Mountain on its own, on a stand-alone basis, had adequate equity to support its rate base, and its other investments, and . . . Inland is in the same position, that Inland non-consolidated has equity to support its investment in rate base, in Trans Mountain, and its other utility investments."

2. Intervenors Position

Dr. Waters, appearing on behalf of the Industrial intervenors, argued that Inland's utility activities are supported by a common equity component of only 20% (Exhibit 47, Table 9b). Dr. Waters' methodology is summarized in Exhibit 47.

In his analysis, Dr. Waters used as his starting point the consolidated capital structure of Inland. Dr. Waters argued that use of a balance sheet prior to consolidation would not reflect the downward adjustment that materializes at the consolidated level for Inland in the form of a deduction of the purchase cost of the shares in Inland held by Trans Mountain. This deduction effectively eliminates, as an asset, the excess of Trans Mountain's purchase price for these shares over their book value (Exhibit 47, p. 43; Transcript pp. 1303 - 1314).

The consolidated balance sheet of Inland was adjusted by Dr. Waters by deducting an item for "Land and Land Rights" valued at \$19.2 million. The reason for this was that as the acquisition of Trans Mountain was accounted for by the purchase method, on consolidation \$19.2 million, being the excess of the total investment over the book value of net assets acquired, was allocated to Land and Land Rights (Exhibit 73 Inland Natural Gas Co. Ltd. 1983 Annual Report, Notes to Consolidated Financial Statements, Note 1).

Dr. Waters maintained that Land and Land Rights in the amount of \$19.2 million cannot be included in the rate base of either Inland or Trans Mountain. Furthermore as both companies are regulated on the basis of historical cost, a return cannot be earned on goodwill increments arising on acquisition. Although there may be a substantial economic value in these Land and Land Rights, Dr. Waters argued it can only be realized if Land and Land Rights are no longer required for the pipeline service. For these reasons, Dr. Waters reduced the consolidated equity by \$19.2 million.

The intervenors believed the consolidated common equity supporting Inland's activities is therefore comprised of the common equity per the Annual Report, after including the recent equity issue, the minority interest in Trans Mountain less the Land and Land Rights deduction referred to above.

Dr. Waters conducted two tests of the adequacy of the Applicant's equity component:

1. He applied the requested capitalization (35.5% equity) to the utility operations, represented by a rate base of \$142,805,000, and found that a residual common equity component of 5.7% applied to the non-utility operations [Exhibit 47, Table 9(a)].
2. Assuming that Inland's non-utility activities require an equity capitalization of 40% the residual equity component supporting utility rate base would be 20% [Exhibit 47, Table 9(b)].

Dr. Waters concluded "that the requested ratio (of 35.49%) is quite unreasonable inasmuch as the actual ratio is less than 20% even under very generous assumptions" (Exhibit 47, p. 45).

3. Accounting Issues

Much discussion focussed on the concept of consolidated financial statements and the accounting recommendations of the Canadian Institute of Chartered Accountants or CICA (Exhibit 65).

Section 1600.03 of the CICA Handbook states that:

"Consolidated financial statements are those produced by aggregating the financial statements of one or more subsidiary companies on a line-by-line basis (i.e., adding together corresponding items of assets, liabilities, revenues and expenses) with the financial statements of the parent company (related by common share ownership) eliminating intercompany balances and transactions, and providing for any minority interest in a subsidiary company. Consolidated financial statements recognize that the separate legal entities are components of one economic unit and are distinguishable from the separate parent and subsidiary company statements and from combined statements of affiliated companies. The distinction is based both on the nature of such statements and on the difference in circumstances justifying their use."

The accounting treatment for equity when consolidating companies with reciprocal shareholdings is presented in the following sections:

1600.70

- (a) Where a subsidiary company holds shares in the parent company, **such shares should be presented on consolidation as if the parent company had purchased its own shares.**

1600.71

- (a) Where a subsidiary company holds shares of the parent company, the issued share capital of the parent should be set out in full, with **the cost of the shares held by the subsidiary shown as a deduction from shareholders' equity.** (See Share Capital, Section 3240, April 1975)

Applicant's Position

Mr. Kleven described his methodology to capital structure as a "historic and unconsolidated approach for the purposes of rate-making" (Transcript p. 2337). He stated that, "on an unconsolidated basis there is plenty of equity for the utility operation" (Transcript p. 2338). It is his view that the Commission should be looking to Inland legal (Exhibit 55) financial statements to assess the amount of equity available to the utility. He agreed with Mr. Wallace that the CICA rules for reporting to shareholders on a consolidated basis should be followed and Inland indeed does so.

Intervenors' Position

Mr. R.B. Wallace, acting for the Industrial intervenors, argued that, "Inland must only be permitted to earn a return on equity actually invested and available for the benefit of the users. Equity is the most expensive form of capital, from a rate payers point of view and should only be used in the capital structure when it is properly required to provide financial flexibility and a reasonable level of protection to shareholders and debtholders by way of appropriate levels of leverage and coverage." (Transcript p. 2954).

By way of measuring the equity available to customers, the Industrial intervenors advanced the position that the equity in Inland was that amount shown in the Annual Report to shareholders of Inland Natural Gas. These are the consolidated financial statements of the company and properly deduct the cost of Inland shares held by Trans Mountain. In support of his position, Mr. R.B. Wallace referred to various sections of the CICA Handbook.

Mr. Wallace argued that the whole purpose of the foregoing discussion is the determination of a measure of a fair return to shareholders on the shareholders' investment. To do this the most important statements to look at are the consolidated statements (Transcript p. 2967).

Pursuant to the above, the consolidation process requires that some \$52 million (the cost of Inland shares held by Trans Mountain) be deducted from the consolidated equity.

Mr. Wallace argued that the accounting rules are not in existence simply as a mere accounting convention, but are put in place primarily to ensure that the financial statements that are consolidated present fairly the financial position of the company and are the statements whereby the shareholder judges his investment in the company (Transcript p. 2968).

4. Commission Conclusions

The consolidated balance sheet of the company presents the book value of all its assets on the left-hand side and various sources of funds financing those assets on the right-hand side. In other words, Inland's consolidated capital structure is a weighted average of the various capital structures supporting the assets employed in its several business activities.

The consolidated balance sheet as at June 30, 1986 shows the sources of capital to be:

	<u>(\$000)</u>	
- unfunded debt	23,503	9.6 %
- long-term debt	121,615	49.7
- deferred income taxes	20,089	8.2
- preferred shares	15,918	6.5
- common equity	<u>63,745</u>	<u>26.0</u>
(including minority interest)	<u>244,870</u>	<u>100.0 %</u>

On February 13, 1987, Trans Mountain sold 1,200,000 common shares of Inland at \$12.90 per share. According to the Applicant, Inland's common equity (as reflected in the consolidated financial statements) has increased by approximately \$14 million. With this addition the consolidated common equity component is approximately 30%.

Of the various business activities pursued by Inland, the Commission views its gas distribution utility operation as the least risky.

The Commission agrees that the application of generally accepted accounting principles on a consolidated basis shows Inland to be financed with a common equity component (including minority interest) of approximately 30%. The issue, however, in this proceeding is the appropriate capital structure for the determination of just and reasonable rates and the Commission in these circumstances believes that the principle inherent in the Applicant's proposal provides the appropriate basis. In essence what has resulted from these inter-company holdings is "double leverage" within Inland and this leverage effect results in a higher rate of return on consolidation than that which is allowed for regulatory purposes. Similar impacts are produced when a utility is held by a holding company or for that matter another utility. An example of this is the relationship between Inland and its wholly-owned subsidiary Columbia Natural Gas Limited. The application of the principles put forward by the Applicant results in an equity capitalization of 35.49%.

The Commission, although adopting the principles in general, then considered whether or not the end result provided an efficient capital structure. In considering the approved capital structure for regulatory purposes the Commission, amongst other matters, has considered the Applicant's historic structure, the capitalization of other utilities and the level of perceived risk for the utility operation at this time. The Commission has concluded that the proposed capital structure by the Applicant contains approximately \$4 million more equity than is reasonably required and accordingly the Commission believes that the equity "injection" approved subject to review pursuant to Commission Order No. G-53-86 is not required for Inland's interim utility operations. Accordingly this amount, on a weighted average basis, has been deducted from the Applicant's proposal, hence establishing an equity component of approximately 32.5% which is approximately 2.5% higher than the 30.09% adopted in the 1985 Decision.

This particular hearing was greatly extended and its costs considerably increased by the discussion of the question of the utility's capital structure. Unfortunately this may not be the last time this question is raised in the hearing process as long as Inland, the Company, continues to include utility operations regulated by this Commission and other operations not regulated by this Commission in the immediate Inland corporate structure. A simple solution to the problem would be for Inland to isolate the Inland utility assets regulated by BCUC in a company separate from Trans Mountain, Columbia, Fort Nelson Gas and all of the related or non-related companies. With these assets and expenses separated, the company would be a utility unto itself and therefore would be much easier to regulate — a distinct benefit to customers, shareholders and intervenors alike.

Another approach to a simplified corporate structure, rather than separation, could be consolidation. If Inland's utility operations in British Columbia were consolidated and then separated from Trans Mountain and the non-utility subsidiaries, this too would simplify the determination of the overall revenue

requirements. However, this may be more than offset by having to keep or develop separate costs to support different regional rates. That is to say, rates for Fort Nelson and Columbia.

These are not the only solutions and accordingly the Commission orders Inland to address either of these approaches or others in the immediate future and advise the Commission of the Applicant's recommended solution. This report should be provided to the Commission no later than March 4, 1988.

X RATE OF RETURN

Dr. Evans, the Applicant's expert witness on rate of return, testified that, in his view, Inland's overall business risk has increased (Exhibit 3, Tab 1). He attributed this to greater competitive risks together with the adverse possibilities flowing from the proposed Westcoast toll design. With regard to the decline in natural gas prices, he submitted that some reduction in long-run capital recovery risks has occurred because of the competitive position of natural gas vis-a-vis alternate fuels.

Dr. Waters, expert witness for the industrial intervenors, identified three broad categories of business risk (Exhibit 47, p. 31) :

1. The risk that the rates will not be set at a level sufficient to provide a fair rate of return on total capital invested.
2. The risk that a particular period's operating and/or financing costs will exceed those utilized in setting the rates, or that the revenues will fall short of those projections.
3. The risk that the system will become uneconomic and will be shut down completely or will be unable to recover fully its fixed costs, including those relating to financing.

It was his opinion that none of these risks was such as to cause concern for investors. To support his position, Dr. Waters pointed to the very positive tone of Inland's Annual Report and to the continued strength of Inland's share price.

The Commission is aware of recent changes in the energy sector and of Inland's particular circumstances. The effects have been both positive and negative, offering opportunities and challenges. To date, however, the utility's business risks have not changed in any material way such as to result in a bond rating change or an altered perception by investors.

The question of financial risk flowing from the utility's capital structure has been addressed at length in this Decision.

The fear of rekindled inflation in 1986/87 has subsided and the long-term Government of Canada bond yield was in the region of 9.75%. Considering that the real rate of interest is still at a historical high and Canadian rates are well above those in the United States, any sudden increase in the test year interest rates would appear to be unlikely. The Applicant used 9.5% as the yield for 1987 whereas the intervenors suggested 9%. The Commission is satisfied that the range of 9 to 10% is a reasonable forecast for long-term Government of Canada bond yields in the immediate term.

Dr. Evans used three tests in arriving at his recommendation:

1. comparable earnings;
2. discounted cash flow (DCF); and
3. equity risk premium.

He gave primary weight to the results obtained from the comparable earnings test and expressed reservations about the use of the DCF method because of the difficulty in inferring investor growth expectations.

To permit Inland the opportunity to undertake new common equity financing without dilution of nominal book value, Dr. Evans assumed a 110% to 120% market-to-book ratio and a 60% payout ratio. He derived the following returns:

- | | |
|------------------------|----------------|
| 1. comparable earnings | 15.0% - 15.25% |
| 2. DCF | 14.0% - 14.7% |
| 3. equity risk premium | 14.3% - 15.3% |

Evaluating the results of his studies and applying professional judgment to his findings, Dr. Evans recommended a 15% rate of return on book common equity.

Dr. Waters estimated the required rate of return for the utility-related common equity of Inland. He relied on the Discounted Cash Flow and Equity Risk Premium tests applied to samples of low risk non-utility corporations. As a test of his results, he also used beta values for a sample of utilities. As a result Dr. Waters was of the opinion that the efficient capital structure for Inland utility should have a book common equity component of 30-32.5% (Transcript p. 1952). For that amount of common equity, he concluded that the investors' required rate of return would be no more than 12 3/8% and that the associated fair rate of return on common equity would be in the range of 12 7/8% to 13 1/8%.

The Commission believes that a rate of return on common equity in the range of 13.25% to 13.75% on a 32.5% common equity component is fair and reasonable. For revenue requirement purposes the Commission has used a rate of return of 13.50%.

XI DECISION

Exclusive of any savings on account of lower contract demand, identified at \$1.1 million, as discussed on page 22 of this Decision and dealt with separately by Order No. G-32-87 and which is subject to further consideration, the Commission confirms an average rate increase of 0.34% for the 1987 fiscal year, to take effect from July 1, 1986.


The Commission confirms an average level of rates of 0.63% over permanent rates existing on June 30, 1986, as at July 1, 1987. This small revision is to reflect the full amortization of the "hot gas" credit as discussed on page 23, which was completed as of June 30, 1987.

The interim increase of 2.32% in effect since July 1, 1986 will required partial refunding with interest in accordance with the terms of Commission Order No. G-38-86.

The Commission concludes that this Decision provides Inland with an opportunity to earn a rate of return on common equity of 13.5%, within a range of 13.25% to 13.75%, based on a 32.5% common equity component.

The Commission will accept revised rate schedules in accordance with this Decision supported by a reconciliation of rates, volumes and revenues, showing also a calculation of amounts refundable.

DATED at the City of Vancouver, in the Province of British Columbia,
this 6th day of August, 1987.


J.D.V. NEWLANDS, Deputy Chairman
N. MARTIN, Commissioner



BRITISH COLUMBIA
UTILITIES COMMISSION

ORDER
NUMBER G-52-87

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 a Revenue Requirements
Application by Inland Natural Gas Co. Ltd.

BEFORE: J.D.V. Newlands,)
Deputy Chairman; and) August 5, 1987
N. Martin,)
Commissioner)

O R D E R

WHEREAS Inland applied May 30, 1986, pursuant to Sections 67(2) and 106 of the Utilities Commission Act ("the Act") requesting interim and permanent rate relief to be effective July 1, 1986; and

WHEREAS the Commission Issued Order No. G-38-86 granting to Inland an interim refundable rate increase of 2.32% effective July 1, 1986; and

WHEREAS the Commission by Order No. G-47-86 set down the Application for public hearing to commence in Kelowna on Monday, September 22, 1986; and

WHEREAS the Commission has considered the Application and the evidence adduced thereon, during 19 days of public hearing, all as set forth in a Decision issued concurrently with this Order.

NOW THEREFORE the Commission hereby orders Inland Natural Gas Co. Ltd. as follows:

- I. The Rate Base and Revenue Requirement for the Fiscal Year ended June 30, 1987 are as set out in Schedule I contained in the Decision.

.../2

BRITISH COLUMBIA
UTILITIES COMMISSION

2

ORDER
NUMBER G-52-87

2. Inland is to proceed with refunds to its customers of record in the period July 1, 1986 through August 31, 1987 as specified in the Decision of the Commission issued concurrently with this Order. Such refunds are to include interest calculated as specified in Order No. G-38-86. A reconciliation schedule is required to be filed with the Commission concurrently.
3. The Commission will accept for filing, subject to timely filing thereof, amended Tariff Rate Schedules confirming as firm effective September 1, 1987, rates which conform to the terms of the Commission's August 6, 1987 Decision.
4. Inland will comply with the several directions incorporated in the Commission Decision.

DATED at the City of Vancouver, in the Province of British Columbia, this 6th day of August, 1987.

BY ORDER



Deputy Chairman

INLAND NATURAL GAS CO. LTD.

Schedule J
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UTILITY INCOME AND EARNED RETURN

For the Fiscal Year Ended June 30, 1987

(\$000)

	Fiscal 1985 Decision (JAN 11/85)	1987 Rate Application (May 30/86)	1987 AMENDED APPLICATION	Adjusted Adjustments	Adjusted Balances
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SALES VOLUME (1)	48,651	47,923	48,029		48,029
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UTILITY REVENUE

Gas sales - present rates	\$162,399	\$171,979	\$172,346		\$172,346
Gas sales - interim rates	3,360	3,998	3,998		3,998
Deferred 1985 COB			502		502
Refundable portion	(862)		(881)	(2,527)	(3,409)

Total	164,897	175,977	175,965		173,437
Cost of Gas	112,870	117,392	117,615		117,615

Gross Margin	52,027	58,585	58,350		55,822
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OPERATING EXPENSES

Operating and maintenance	17,222	19,449	19,662	(5011)	19,612
Property, franchise taxes	9,967	10,726	10,712	(6612)	10,646
Depreciation & amortization	4,424	4,856	4,856	145 (3)	5,001
Other operating revenue	(620)	(673)	(697)		(697)

	30,993	34,588	34,533		34,562
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Utility Income before Taxes	21,034	24,227	23,817		21,260
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Income Tax - current	3,814	5,991	5,859		4,283
- deferred					

EARNED RETURN	\$17,220	\$18,236	\$17,958		\$16,977
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UTILITY RATE BASE	\$131,239	\$142,805	\$142,524		\$141,949
-------------------	-----------	-----------	-----------	--	-----------

RETURN ON RATE BASE %	13.12	12.77	12.60		11.96
-----------------------	-------	-------	-------	--	-------

(1) O and M expenses adjusted,

(2) Change in franchise fee due to change in sales.

(3) Hearing cost amortization.

Schedule II
=====

INLAND NATURAL GAS CO, LTD.

Utility Rate Base for the Fiscal Year Ended June 30, 1987

(1000)	Decision for Fiscal 1985 (JAN 11/85)	Fiscal 1987 Application (May 30/86)	Fiscal 1987 Amended App'n (Nov 26/86)	Adjustments	Adjusted Balance
=====					
Gross plant in service					
Beginning of Year	\$180,788	\$206,047	\$206,047	(\$281,111)	\$205,399
Additions to gas plant				14001121	
Mid-year	5,265	4,371	4,371		4,371
Intangible plant	984	987	987		987
Construction in progress	671	380	370		370
Less- customer advances on construction	(275)	(320)	(320)		(320)

Gross Plant	187,433	211,465	211,455		210,807
Less - CIAC	(10,781)	(15,046)	(15,046)		(15,046)

	176,652	196,419	196,409		195,761
Accumulated depreciation	(34,977)	(42,895)	(42,895)		(42,895)
Adj. to accu. depreciation	(1,940)	(2,293)	(2,293)		(2,293)

Net Plant	139,715	151,231	151,221		150,573

Deferred income tax	(11,107)	(11,031)	(11,031)		(11,031)
Deferred charges	928	592	330	73,631	403

Working capital allowance	1,703	2,013	2,004		2,004

Utility Rate Base	\$131,239	\$142,805	\$142,524	(\$575)	\$141,949
=====					

- (1) Chase project cost disallowed,
 - (2) Propane plant removed from rate base,
 - (3) Heating cost:
- | | | |
|--------------|----|---------|
| Beginning | \$ | 0 |
| Additions | | 290,000 |
| Amortization | | 145,000 |
| Mid-year | | 73,000 |

INLAND NATURAL GAS CO. LTD.

Schedule 111
=====CALCULATION OF INCOME TAXES ON UTILITY INCOME
FOR THE FISCAL YEAR ENDED JUNE 30, 1987

(\$000)	DECISION (JAN 11/85)	1987 Rate Application	1987 AMENDED APPLICATION	Adjustments	Adjusted Balances
Earned return	\$17,219	\$18,236	\$17,958		\$16,977
Deduct: interest on debt	(9,790)	(9,411)	(9,250)	(275)(11)	(9,525)
Add: non tax deductible exp.	106	102	102		102
Accounting income aft. tax	7,535	8,927	8,810		7,554
Deduct: timing differences adj. hearing costs	(4,014)	(3,603)	(3,603)	(145)(12)	(3,603) (145)
Taxable income after tax	\$3,521	\$5,324	\$5,207		\$3,806
Income tax rate %(current)	52.000	52.947	52.947		52.947
1-current income tax rate	48.000	47.053	47.053		47.053
Deferred income tax rate	0.000	0.000	0.000		0.000
Taxable income before income tax	\$7,335	\$11,315	\$11,066		\$8,089
Add: amount required to provide for deferred tax	0	0	0		0
TAXABLE INCOME	\$7,335	\$11,315	\$11,066		\$8,089
Income tax - current	\$3,814	\$5,991	\$5,859		\$4,283
- deferred	0	0	0		0
TOTAL INCOME TAX	\$3,814	\$5,991	\$5,859		\$4,283

(1) Interest expense = rate base * debt cost component of average cost of capital.
(2) Additional hearing cost expensed for tax purposes.

INLAND NATURAL GAS CO, LTD.

Schedule IV
=====

COMMON EQUITY FOR THE FISCAL YEAR ENDED JUNE 30, 1987

	1985 DECISION	1987 APPLICATION	1987 AMENDED APPLICATION	ADJUSTMENTS	ADJUSTED BALANCES
Common share capital					
Beginning of Year	\$3,098	\$3,333	\$3,133		\$3,133
Contributed Surplus	9,843	13,176	9,376		9,376
Retained Earnings					
Balance-- beginning of year	29,610	36,889	36,889		36,889
Forecast net income for the year (1)	7,207	8,706	8,383	(1)	7,452
DEDUCT:					
Dividends	4,607	5,757	5,462	(177)(12)	5,285
TOTAL - End of Year	\$44,151	\$56,347	\$57,319		\$51,565
Common equity as at Beginning of Year	\$41,551	\$53,398	\$49,398		\$49,398
Add: ave share issued 8/20/86			\$3,452	(3,452)(33)	\$0
MID-YEAR COMMON EQUITY	\$42,851	\$54,873	\$54,311		\$50,482

- (1) Mid-year Rate Base multiplied by % return on equity.
 (2) Reduced dividend to reflect (3).
 (3) Forecast equity issue not included for utility purposes.

INLAND NATURAL GAS CO. LTD.

Schedule V
=====

RETURN ON CAPITAL FOR THE FISCAL YEAR ENDED JUNE 30, 1987

(\$000)

1985 DECISION	Capitalization Per Decision (JAN 11/85)	Adjustments	Capitalization Amount	Percentage %	% Average Embedded Cost	Cost Component %
=====						

Long Term Debt	\$67,517		\$67,517	47.41	12.914	6.12
Unfunded Short-term Debt	16,290		16,290	11.44	11.700	1.34
Preference Shares	15,740		15,740	11.05	8.286	0.92
Common Equity	42,851		42,851	30.09	15.750	4.74
	\$142,398		\$142,398	100.00		13.12
=====						

1987 RATE APPLICATION	Capitalization	Adjustments	Capitalization Amount	Percentage %	% Average Embedded Cost	Cost Component %
=====						
Long Term Debt	\$62,092		\$62,092	40.15	12.899	5.18
Unfunded Short-term Debt	21,754	(0)	21,754	14.07	10.000	1.41
Preference Shares	15,918		15,918	10.29	8.312	0.86
Common Equity	54,873	0	54,873	35.49	15.005	5.32
	\$154,637		\$154,637	100.00		12.77
=====						

1987 AMENDED APPLICATION	Capitalization	Adjustments	Capitalization Amount	Percentage %	% Average Embedded Cost	Cost Component %
=====						
Long Term Debt	\$62,092		\$62,092	40.06	12.899	5.17
Unfunded Short-term Debt	22,676	(0)	22,676	14.63	9.000	1.32
Preference Shares	15,918		15,918	10.27	8.312	0.85
Common Equity	54,311	0	54,311	35.04	15.001	5.26
	\$154,997		\$154,997	100.00		12.60
=====						

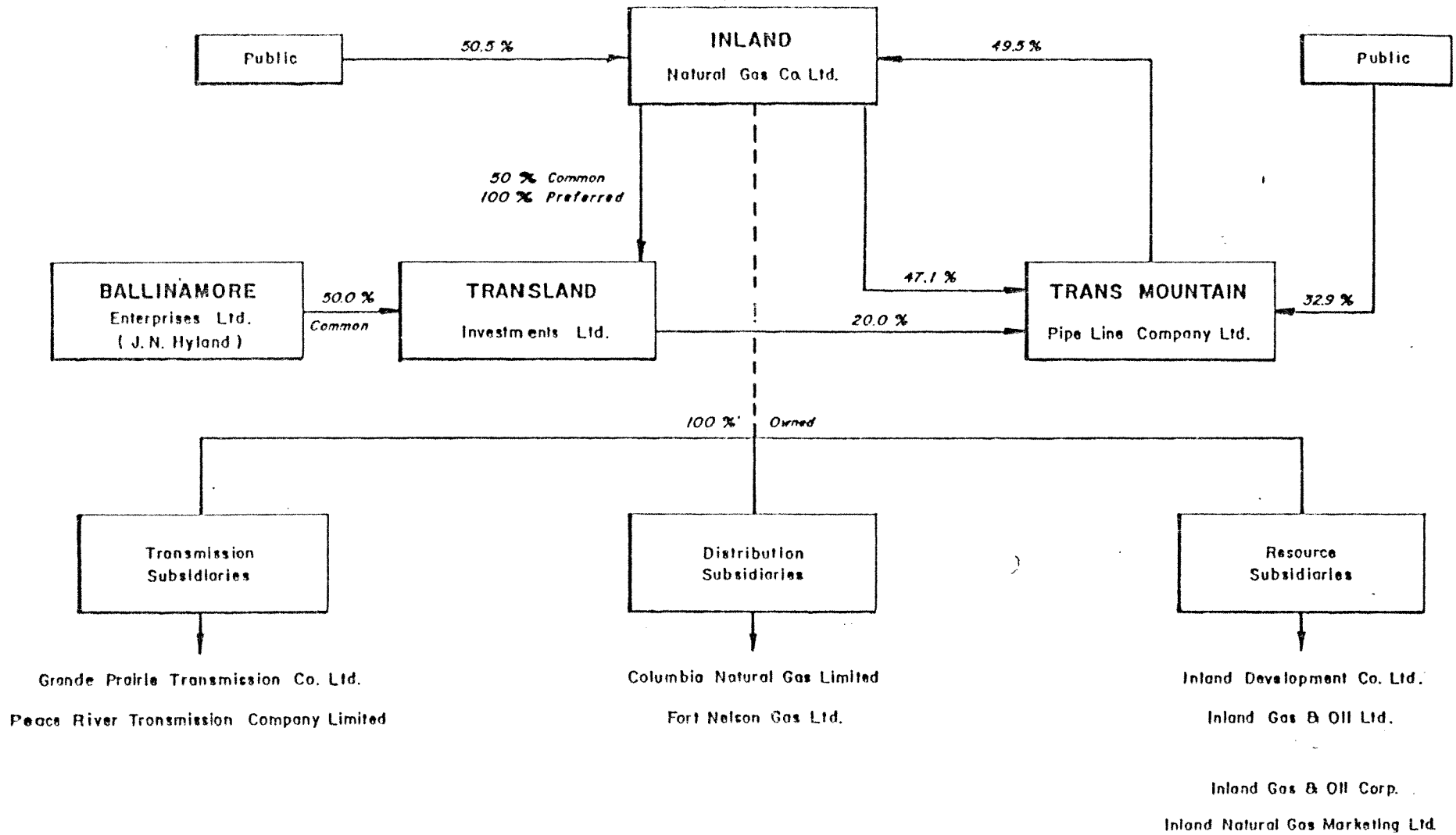
1987 ADJUSTED BALANCES	Capitalization	Adjustments	Capitalization Amount	Percentage %	% Average Embedded Cost	Cost Component %
=====						
Long Term Debt	\$62,092	\$9,082	\$71,174	45.92	12.512	5.75
Unfunded Short-term Debt	22,676	(5,253)	17,423	11.24	8.500	0.96
Preference Shares	15,918		15,918	10.27	8.312	0.85
Common Equity	54,311	(3,629)	50,682	32.57	15.500	4.40
	\$154,997		\$154,997	100.00		11.96
=====						

(1) Adjusted for new long term debt issue.

(2) Revised short-term interest rate.

(3) Approved rate of return on common equity.

CORPORATE STRUCTURE



INLAND NATURAL GAS CO. LTD. FOR THE YEARS ENDING JUNE 30.

YEARS	ROE			YIELD L-T CANADA'S	COMMON EQUITY	RATE BASE \$ 000's	TJ'S SOLD	NORMAL TEMP	LABOUR FORCE	CUSTOMER (average)
	ALLOWED	ACHIEVED	NORMAL							
1981	16.50% (no range)	16.68%	N/A	15.22%	28.20%	\$108,097	51,770	N/A	315	85,488
1982	N/C	13.58%	13.80%	14.26%	29.50%	\$116,149	48,671	-9.00%	356	92,177
1983	15.75% (15.25% - 16%)	13.49%	13.69%	11.79%	28.50%	\$132,024	49,429	9.00%	372	97,721
1984	N/C	16.67%	17.20%	12.75%	28.50%	\$137,680	48,426	8.50%	380	103,320
1985	15.75% (15% - 16%)	17.90%	15.00%	11.04%	28.80%	\$143,678	51,439	-6.00%	394	109,393
1986 EST.	N/C	18.50%	15.60%	9.83%	29.80%	\$149,443	51,924	-4.50%	387	113,939
1987 Test Yr.	15.00% (Application)				33.10%	\$153,803	47,923	normal	368	117,863 117,596

NOTES

- 1 1982 Normalized ROE is from the BCUC Decision, May 1983.
- 2 1983 Normalized ROE is from hearing exhibit #3, September 1983.
- 3 1984 Normalized ROE is from hearing exhibit #24 of the 1984 hearing.
- 4 1985 Normalized ROE is from a November 21, 1985 letter to the BCUC.
- 5 Deferred tax balances are included in the Capital Structure.

BRITISH COLUMBIA UTILITIES COMMISSION		
EXHIBIT 10		
HEARING No. 2	ENTERED BY BCUC	DATE Sep 23/86

	CHASE				SORRENTO				TOTAL	
	ORIGINAL	FINAL PROJECTION	DIFFERENCE		ORIGINAL	FINAL PROJECTION	DIFFERENCE		DIFFERENCE	
FOOTAGE	(m)	(m)	(m)		(m)	(m)	(m)			
Transmission 4"					26,500	25,133	-1367			
Transmission 3"	31,700	31,228	- 472							
Transmission 2"	31,700	31,228	- 472		6,400	6,761	+ 361			
					32,900	31,894	-1006		-1478	
Distribution 4"					4,110	5,446	+1336			
Distribution 3"	2,100	3,535	+1435		14,915	17,245	+2330			
Distribution 2"	3,610	4,231	+ 621		39,270	38,608	- 662			
Distribution 1 1/4"	10,898	11,003	+ 105		43,309	39,433	-3876			
TOTAL	16,608	18,769	+2161		101,604	100,732	- 872		+1289	
CUSTOMERS	(#)	(#)	(#)		(#)	(#)	(#)			
Residential	250	254	+ 4		462	561	+ 99			
Commercial	25	66	+ 41		27	42	+ 15			
TOTAL	275	320	+ 45		489	603	+ 114		+ 159	
COSTS	(\$)	(\$)	(\$)	(%)	(\$)	(\$)	(\$)	(%)		
Transmission	1,293,661	1,664,638	+370,977	129	1,270,900	1,418,508	+147,609	112		
Land	57,000	187,434	+130,434	329	317,900	338,705	+ 20,805	106		
	1,350,661	1,852,072	+501,411	137	1,588,800	1,757,214	+168,414	111		
Distribution	266,022	325,615	+ 59,593	122	1,440,472	1,671,867	+231,395	116		
Stations	31,260	47,495	+ 16,235	152	82,350	93,632	+ 11,282	114		
TOTAL	1,647,943	2,225,181	+577,238	135	3,111,622	3,522,713	+411,091	113	\$ 988,329 121%	
CONTRIBUTIONS	(\$)	(\$)	Revised		(\$)	(\$)	Revised			
5 Year Net Revenue	531,939	563,636	656,734	+ 124,795	1,167,290	1,218,791	1,307,976	+ 140,686		
Provincial	615,000	736,000	736,000	+ 121,000	685,000	564,000	564,000	- 121,000		
Federal	500,000	529,100	494,811	- 5,189	1,250,000	1,355,100	1,325,443	+ 75,443		
TOTAL	1,646,939	1,828,736	1,887,545	+\$240,606	3,102,290	3,137,891	3,197,419	+ 95,129	\$ 335,735	
PROJECT COST	1,647,943	2,225,181	+ 577,238	135	3,111,622	3,522,713	+ 411,091	113	988,329 121%	
LESS INCREASED REV.	-----	- 240,606	- 240,606	---	-----	- 95,129	- 95,129	---	-335,735 ---	
	1,647,943	1,984,575	+ 336,632	120	3,111,622	3,427,584	315,962	110	652,594 114%	
LESS INCR. FIXED OH	-----	- 135,225	- 135,225	---	-----	- 80,748	- 80,748	---	215,973 ---	
	1,647,943	1,849,350	201,407	112	3,111,622	3,346,836	235,214	8	436,621 109%	

INLAND NATURAL GAS CO. LTD.

BOX 12503, 1066 WEST HASTINGS STREET,
VANCOUVER, BRITISH COLUMBIA V6E 3G3
TELEPHONE(604) 684-0484

J. L. RANDALL
VICE-PRESIDENT, MARKETING AND
UTILITY PLANNING
DIRECT: (604) 661-9603
FAX: 661-9614

July 15th, 1986.

Mr. A. C. Michelson,
British Columbia Utilities Commission,
4th Floor,
800 Smythe Street,
Vancouver, B.C.
V6Z 2E1

Dear Mr. Michelson:

RE: BRITISH COLUMBIA UTILITIES COMMISSION REQUEST FOR
ADDITIONAL INFORMATION ON INLAND'S PROPOSED PROMOTIONAL
INCENTIVE PROGRAM FOR FURNACES AND INLAND'S
MERCHANDISING ACTIVITIES.

Inland Natural Gas Co. Ltd. ("Inland") has proposed a promotional incentive program to assist new and existing customers to install natural gas heating equipment.

The purpose of the program is to encourage homeowners using other fuels to convert to natural gas; to replace the Federal Government Canada Oil Substitution Program grant; and to assist existing customers in replacing or upgrading their existing heating equipment, some of which is twenty-five years old.

The promotional incentive would be available to these new and existing customers when they purchase a furnace from any retail outlet. Customers are free to purchase their heating equipment from the dealer of their choice and have it installed by any qualified dealer and be eligible for the promotional incentive. There is no stipulation that they must purchase their equipment from Inland or any specific dealer.

The program will be promoted, upon approval, in such a way that all furnace retailers and dealers in our service area will understand that customers will be eligible for the promotional incentive.



Wholly-Owned Subsidiary Companies

COLUMBIA NATURAL GAS LIMITED • FORT NELSON GAS LTD. • INLAND GAS & OIL CO. LTD. • INLAND DEVELOPMENT CO. LTD.
GRANDE PRAIRIE TRANSMISSION CO. LTD. • PEACE RIVER TRANSMISSION COMPANY LIMITED

A CORPORATE PARTNER IN



-2-

In a separate marketing program, Inland is planning an expansion of its merchandising activities. This program will be tested in two of Inland's regions, the north including Prince George, Quesnel and Williams Lake and in the Okanagan including Kelowna, Vernon, Penticton, Salmon Arm, Osoyoos and Princeton.

This program is designed to assist our residential customers in increasing the value they receive for their energy dollar. It responds to the Commission's comments in our rate application decision dated January 11th, 1985 that Inland look into ways of assisting our customers in managing their energy bills.

Specifically, the objectives for the program are:

- * to offer consumers their best energy investment.
- * to increase consumer awareness of our expertise for gas products.
- * to increase penetration of gas appliances beyond heating equipment installations.

We will achieve these objectives by offering the consumer a package of reliable energy information, quality products, arranged installation and warranty.

This program will create considerable installation and service work for our local heating dealers to whom we will be subcontracting. Attached is an article that appeared in a trade magazine that states the benefits one heating contractor has received by working with Union Gas in a similar program. Currently we have fifteen signed contracts from local heating dealers and are expecting approximately another fifteen signed dealers in the near future.

A recent Customer Attitude Survey conducted by an independent firm showed that many of our customers are unaware of such items as new higher efficiency gas heating equipment. The survey also found that of the 1,000 customers contacted, 50% would prefer to purchase major gas appliances from Inland rather than from a major retail outlet or local heating dealer and 85% agreed that Inland is the place to go for reliable information and advice about conservation and equipment. These statistics reveal our customers want to do business with us.

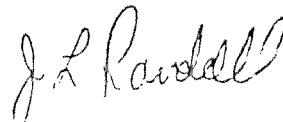
-3-

Through this merchandising program, Inland is providing leadership to stimulate demand for natural gas equipment in the marketplace.

Our aggressive promotion will not only benefit the heating dealers directly, but in addition will respond to our customers' needs.

If you have any questions, please do not hesitate to contact me.

Yours very truly,



J. L. Randall.

JLR:dmc
Attached.

**MECHANICAL CONTRACTORS
ASSOCIATION OF BRITISH COLUMBIA**

#230 - 4259 CANADA WAY
BURNABY, B.C. V5G 1H1
PHONE (604) 430-2454



September, 1986

Mr. A.C. Michelson, Commission Secretary
British Columbia Utilities Commission
4th floor, 800 Smythe Street
Vancouver, B.C.
V6Z 2E1

Dear Sirs:

Re: Public hearing re Inland Natural Gas
Capri Hotel, Kelowna, B.C.
Commencing September 22nd 1986

The Mechanical Contractors Association of British Columbia is an Association of mechanical contractors and suppliers who supply and install natural gas equipment throughout the marketing area of Inland Natural Gas. Although most members of the Mechanical Contractors Association of the Okanagan Valley are not members of the provincial Association, in this instance we speak on their behalf also. The same is true of the Mechanical Contractors Associations of Prince George and Quesnel.

As an Association, we do not wish to take a position on Inland Natural Gas Limited's application for interim and permanent rate relief of approximately 2.3%. Our sole purpose in making this presentation is to express opposition to Inland Natural Gas' proposed activities related to merchandising natural gas appliances. We would remind you that many of the mechanical contractors and suppliers on whose behalf I am speaking use and pay for the services of Inland Natural Gas. None of these members takes issue with the monopoly status of Inland Natural Gas in supplying natural gas. They do, however, express serious opposition to Inland Natural Gas using their monopoly status and entering into competition with their ratepayers and with other companies who do not have a monopolistic status that is approved by the Utilities Commission.

Public Hearing re Inland Natural Gas

Page 2

In their proposal to merchandise natural gas equipment, Inland Natural Gas intends to use their monopolistic status to provide unfair competition with contractors and entrepreneurs whose business it is to supply and install the gas equipment. We say this is unfair competition, because their marketing program will benefit from a captive audience of their customers or would-be customers, and secondly because ratepayers, who include the contractors and entrepreneurs against whom Inland proposes now to compete, ^{ARE} ~~is~~ underwriting this competition.

More specifically, the advantages of a Utility that has monopolistic status are in the areas of capitalization, administration and overhead, name, credit information, billing, and direct from manufacturer ordering.

Our Association and the people on behalf of whom I speak do not oppose marketing activities of Inland Natural Gas that promote the sale and installation of energy consuming equipment. This promotion, however, should be designed to assist the contractor who sells, installs and services this equipment and also the wholesalers from whom the contractor purchases his equipment. Both of these types of businessmen, contractor and wholesaler, ensure our citizens of competitive prices and continued services, based on performance and not on a monopolistic status.

We would refer you to the letter of J.L. Randall, Vice President Marketing and Utility Planning, to Mr. Michelson and the British Columbia Utilities Commission on July 15, 1986. On the first page of this letter Mr. Randall outlines a promotional incentive program to assist new and existing customers to install natural gas heating equipment. On this page he indicates that "customers are free to purchase their heating equipment from the dealer of their choice and have it installed by any qualified dealer and be eligible for the promotional incentive. There is no stipulation that they must purchase their equipment from Inland or any specific dealer. He adds the program will be promoted, upon approval, in such a way that all furnace retailers and dealers in our service area will understand that customers will be eligible for the promotional incentive."

Public Hearing re Inland Natural Gas

Page 3

The Mechanical Contractors Association of British Columbia and the local associations of mechanical contractors in the marketing area of Inland Natural Gas do not take exception to this incentive program if it is carried out the way Mr. Randall has indicated. We endorse Inland's promotional program to have people convert from alternative energies to natural gas. What we object to, however, is described in page 2 and subsequent pages of Mr. Randall's letter to Mr. Michelson.

Mr. Randall writes that Inland will offer "the consumer a package of reliable energy information, quality products, arranged installation and warranty". This, Mr. Chairman and Commissioners, is what mechanical contractors and those for whom we are speaking today are totally opposed to. That is unfair competition.

We do not oppose marketing activities of Inland Natural Gas that promote the sale and the installation of energy consuming equipment. In fact, we applaud such activities. This promotion, however, should be designed to assist the contractor who sells, installs and services this equipment. It should also assist the wholesaler from whom the contractor purchases his equipment.

We are informed by Inland Natural Gas that they intend to employ contractors to install the equipment they sell. It is a fact that "labour only contracts" are undesirable for contractors because of their increased risk factor. You are informed by Inland Natural Gas that manufacturers have agreed to warrant their equipment and Inland is asking dealers or installers to warrant only their own labour on the installation for a one year period. Regardless of what price the contractor puts on such a responsibility, he remains at considerable risk since he has no contractual relationship with the manufacturer and/or wholesaler. We would again remind you that the proposal of Inland Natural Gas if approved by the Commission would eliminate the competition of wholesalers.

You have been informed that there has been considerable enthusiasm on the part of dealers or installers for Inland's proposed merchandising program. The petitions that have been signed by contractors and wholesalers in the Prince George, Quesnel and Kelowna areas contradict this statement. In fact, if these lists are examined

Public Hearing re Inland Natural Gas

Page 4

you will undoubtedly find that a considerable number of the dealers or contractors who have agreed to install Inland equipment have signed the petition against their proposed merchandising program. Why? Because as contractors they know the difficulty of labour only contracts. They simply do not work. Also, they know that Inland as a competitor will soon put them out of business. Why have they, therefore, signed this deal with Inland? Contractors have signed this deal with Inland because it is a matter of survival. You have only to look at your yellow pages to see how many contractors and wholesalers there are in this part of the province and then look at the permits that have been taken out in your various municipalities to understand why most of our contractors and wholesalers today grasp at any straw of hope of income.

One of the arguments that Inland Natural Gas cites for this proposed merchandising program is the recent change in provincial policy and federal changes in the regulation of natural gas. As the chief executive officer of Inland Natural Gas stated in a letter to the Mechanical Contractors Association, "Inland is being faced with what has been termed 'gas - on - gas' competition". In the annual report for the year 1985 Inland Natural Gas "regards this as a historic opportunity for growth and has been planning and restructuring to take advantage of the many avenues for expansion and diversification opened up by these changes in energy policy". We would suggest that if competing with their ratepayers and customers, rather than competing with other marketers of natural gas is one of these avenues for expansion, Inland Natural Gas is contradicting their exciting Adventure Inland British Columbia program which received such wonderful press not too many months ago.

To summarize, the Mechanical Contractors Association on behalf of members and of many other small businessmen and taxpayers in British Columbia oppose the "unregulated" utility activities and their impact on traditional marketing and contracting businessmen as proposed by Inland Natural Gas. We do not fear or oppose free competition in our industry; in fact, we want competition. We do, however, oppose and, to be honest, fear the unfair competition of utilities because of their monopolistic advantages and subsidized operations.

Public Hearing re Inland Natural Gas

Page 5

We would request that Inland Natural Gas call off their proposed new merchandising program and replace it with a program that recognizes the traditional wholesalers and contractors as their partners. This implies the recognition of contractors as suppliers as well as installers of the total product line of gas burning equipment. We would sincerely request that the British Columbia Utilities Commission use this public hearing and their influence to have Inland Natural Gas accept our request.

Thank you for your consideration

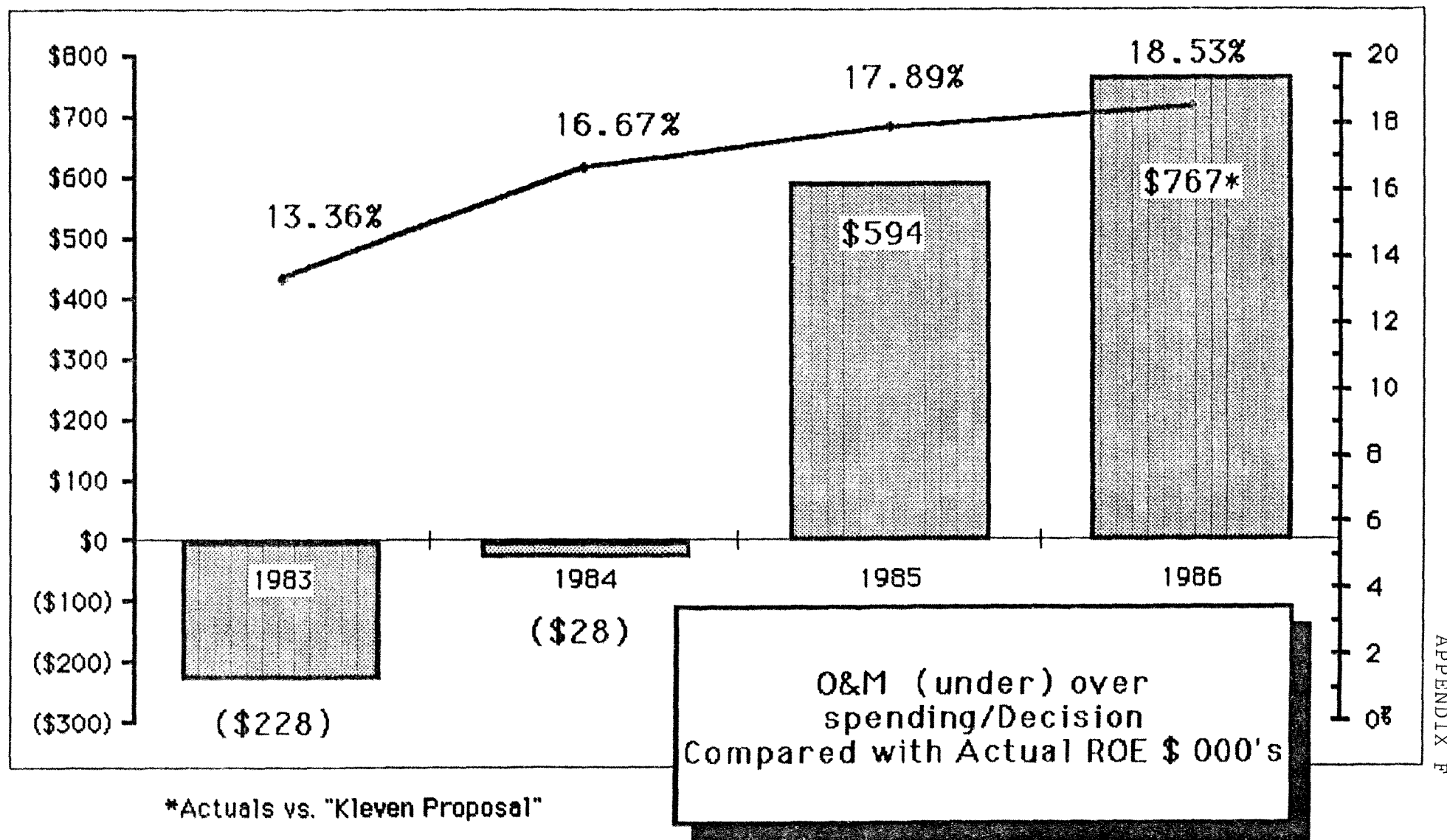
Respectfully submitted,

A handwritten signature in cursive script, appearing to read "V. J. Traynor".

V.J. Traynor

Executive Vice President

VJT:jg



INLAND NATURAL GAS CO. LTD.
ALLOCATION OF VANCOUVER OFFICE CHARGES
TO SUBS AND NON-UTILITY
YEARS ENDED JUNE 30

	1985 Test Year	Forecast	1 9 8 6 Charged	Actual Costs	1987 Forecast
EXHIBIT 40					
Utility Subsidiaries					
Columbia	\$148,800	\$148,800	\$148,800	\$159,881	\$152,625
- NGV	N/A	-	-	33,353	
Fort Nelson	-	-	11,500	26,996	15,000
Peace River	17,400	17,400	17,400	14,614	17,400
Grande Prairie	58,200	58,200	58,200	27,740	58,200
	<u>224,400</u>	<u>224,400</u>	<u>235,900</u>	<u>262,584</u>	<u>243,225</u>
Non-Utility					
Inland Development	4,900	4,900	4,900	899 }	4,900
Inland Gas & Oil	5,700	5,700	5,700	61,394 }	5,700
Trans Mountain	-	-	-	5,207 }	269,224
Inland Gas Marketing	-	-	-	18,778 }	
Other	-	-	-	5,664 }	
	<u>10,600</u>	<u>10,600</u>	<u>10,600</u>	<u>91,942</u>	<u>279,824</u>
Total	<u>\$235,000</u>	<u>\$235,000</u>	<u>\$246,500</u>	<u>\$354,526</u>	<u>\$523,049</u>

Per Vol. 4A, Tab 1, Page 22

Non-utility charges	\$359,224
Deduct - Outside consultants	90,000
	<u>269,224</u>
Charges to subsidiaries	<u>253,821</u>
As above	<u>\$523,049</u>

INLAND NATURAL GAS CO. LTD.
CAPITALIZATION OF UTILITY AND NON-UTILITY ASSETS
As at June 30, 1986

		(\$000)								
Line No.	Particulars (1)	Consolidated Capital Structure (2)	Deduct-Non Recourse			Consolida- tion and Elimination Entries (6)	Balance Inland Legal (7)	Inland Utility (8)	Other Utility (9)	Non- Utility (10)
			Trans Mtn. (3)	Columbia (4)	Fort Nelson (5)					
1	Debt									
2	Short-term debt	\$ 23,503	\$ 1,424	\$ 2,526	\$ (174)	(5)	\$ 19,732			
3	Current maturities	5,604	3,000	133	25	—	2,446			
4		<u>29,107</u>					<u>22,178</u>	\$ 11,399	\$ 721	\$10,058
5	Long-term debt									
6	Inland first mortgage bonds	22,314	—	—	—	—	22,314)		
7	Debentures - Series A	9,840	—	—	—	—	9,840) 44,209	2,795	—
8	- Series B	14,850	—	—	—	—	14,850)		
9	- Series C	25,000	—	—	—	—	25,000	15,519	4,981	4,500
10	Columbia									
11	First mortgage bonds	1,292	—	1,292	—	—	—	—	—	—
12	Fort Nelson									
13	First mortgage bonds	320	—	—	320	—	—	—	—	—
14	Trans Mountain									
15	Term notes	20,000	20,000	—	—	—	—	—	—	—
16	Promissory notes	28,000	28,000	—	—	—	—	—	—	—
17		<u>121,616</u>					<u>72,004</u>	<u>59,728</u>	<u>7,776</u>	<u>4,500</u>
18	Equity									
19	Preference Shares	15,918	—	—	—	—	15,918	14,972	946	—
20	Common Equity									
21	Common Shares	5,845	—	—	—	—	5,845	2,955	187	2,703
22	Contributed surplus	47,382	—	—	—	—	47,382	8,977	567	37,838
23	Retained earnings	40,412	—	—	—	7,412 ⁽¹⁾	33,000	34,800	2,200	(4,000)
24		<u>93,639</u>					<u>86,227</u>	<u>46,732</u>	<u>2,954</u>	<u>36,541</u>
25		260,280	52,424	3,951	171	7,407	196,327			
26	Cost of shares held by Trans Mountain	(52,036)	(52,036)	—	—	—	—			
27		<u>\$208,244</u>	<u>\$ 388</u>	<u>3,951</u>	<u>\$ 171</u>	<u>\$ 7,407</u>	<u>196,327</u>	<u>\$132,831</u>	<u>\$ 12,397</u>	<u>\$51,099</u>
28	(1) Columbia	\$ 4,302								
	Fort Nelson	527								
	All Others	2,583								
		<u>\$ 7,412</u>								

BRITISH COLUMBIA UTILITIES COMMISSION

EXHIBIT

66

INLAND NATURAL GAS CO. LTD.

COMMON EQUITY
AS AT JUNE 30, 1986
(\$000)VOLI
REV

(Rev.)

Line No.	HEARING No.	ENTERED BY	DATE	Share Capital (3)	Contributed Surplus (4)	Sub Total	Retained Earnings (5)	Total (5)
1	11	11/2/86	Oct 6/86	5,845	47,382	53,227	33,000	\$ 86,227
1				5,036	51,014		32,992	89,042
2				200	3,800	4,000	-	4,000
2				<u>6,045</u>	<u>51,182</u>	<u>57,227</u>	<u>33,000</u>	<u>90,227</u>
3								
4								
5								
6				(2,703)	(37,838)	(40,541)	2,518	(38,023)
7								
8								
9								
10								
11								
12								
13							3,568	3,568
14							(2,664)	(2,664)
15							(2,671)	(2,671)
16							1,042	1,042
17							<u>1,046</u>	<u>1,046</u>
18							(561)	(561)
19							(564)	(564)
20							<u>1,385</u>	<u>1,385</u>
							1,379	1,379
				(2,703)	(37,838)	(40,541)	3,903	(36,638)
							98	98
				(2,703)	(37,838)	(40,541)	4,001	(36,540)
				\$ 3,342	\$ 13,344	\$ 16,686	\$ 37,001	\$ 53,687
21				3,333	13,176		36,889	53,398
22				(200)	(3,800)	(4,000)	-	(4,000)
23				<u>\$ 3,142</u>	<u>\$ 9,544</u>	<u>\$ 12,686</u>	<u>\$ 37,001</u>	<u>\$ 49,687</u>

1) Balances agree with volume 4 A Tab 3 Schedule IV

INLAND NATURAL GAS CO LTD.
CALCULATION OF UTILITY COMMON EQUITY
(000)

June 30, 1982 to June 30, 1986

LINE No.	Years Ended June 30	PARTICULARS	Balance per Financial Statement	Deductions re: Trans. Mountain	Deductions re: Inland Gas & Oil	Utility Common Equity	Utility Mean Common Equity
		(1)	(2)	(3)	(4)	(5)	(6)
1	1982						
2		Number of shares outstanding	3,096	--	--	3,096	
3		Share Capital	3,096	--	--	3,096	
4		Contributed Surplus	8,770	--	--	8,770	
5		Retained Earnings	25,360	--	--	25,360	
6		Total	37,226	--	--	37,226	
7		Non-Utility transactions during 1983 (Page 3)					
8		Share Capital		(2,703)			
9		Contributed Surplus		(37,838)			
10		Retained Earnings		64			
11				(40,477)			
12	1983						
13		Number of shares outstanding	5,799	(2,703)	--	3,096	
14		Share Capital	5,799	(2,703)	--	3,096	
15		Contributed Surplus	46,648	(37,838)	--	8,810	
16		Retained Earnings	26,567	64	--	26,631	
17		Total	79,014	(40,477)	--	38,537	37.8
18		Non-Utility transactions during 1984 (Page 4)					
19		Share Capital		--			
20		Contributed Surplus		--			
21		Retained Earnings		1,227			
22				1,227			
23	1984						
24		Number of shares outstanding	5,801	(2,703)	--	3,098	
25		Share Capital	5,801	(2,703)	--	3,098	
26		Contributed Surplus	46,678	(37,838)	--	8,840	
27		Retained Earnings	28,377	1,291	--	29,668	
28		Total	80,856	(39,250)	--	41,606	40.07
29		Non-Utility transactions during 1985 (Page 5)					
30		Share Capital		--			
31		Contributed Surplus		--			
32		Retained Earnings		1,227			
33				1,227			

INLAND NATURAL GAS CO. LTD.
CALCULATION OF UTILITY COMMON EQUITY
<000>

LINE No.	PARTICULARS	BALANCE per Financial Statement	Deductions re: Trans. Mountain	Deductions re: Inland Gas & Oil	Utility Common Equity	Utility Mean Common Equity
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1	1985					
2	Number of shares outstanding	5,806	(2,703)	--	3,103	
3	Share Capital	5,806	(2,703)	--	3,103	
4	Contributed Surplus	46,743	(37,838)	--	8,905	
5	Retained Earnings	30,928	2,518	--	33,446	
6	Total	83,477	(38,023)	--	45,454	43,530 (A)
7	Non-Utility transactions during 1986 (Page 6)					
8	Share Capital		--	--		
9	Contributed Surplus		--	--		
10	Retained Earnings		1,385	98		
11			1,385	98		
12	1986					
13	Number of shares outstanding	11,691	(5,406)	--	6,285	
14	Share Capital	5,845	(2,703)	--	3,142	
15	Contributed Surplus	47,382	(37,838)	--	9,544	
16	Retained Earnings	33,000	3,903	98	37,001	
17	Total	86,227	(36,638)	98	49,687	47,570 (A)

A - Per Exhibit 4A Tab 3 Schedule Y