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CANADA



BRITISH COLUMBIA  
UTILITIES COMMISSION

ORDER  
NUMBER G-98-95

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

and

An Application by BC Gas Utility Ltd.  
for Approval of an Off-System Incentive Program

**BEFORE:** M.K. Jaccard, Chairperson, )  
L.R. Barr, Deputy Chairperson; and ) November 27, 1995

## O R D E R

### WHEREAS:

- A. On July 4, 1995 BC Gas Utility Ltd. ("BC Gas") filed with the Commission a revenue requirements application ("the Application") which requested approval pursuant to Sections 64 and 101 of the Utilities Commission Act of an incentive mechanism for off-system gas sales and other off-system activities ("the original proposal"); and
- B. In reviewing the Application, further information requests, educational workshops and pre-hearing conferences occurred prior to negotiation dates which were held between October 11 and 19, 1995; and
- C. During those negotiations, the parties agreed that while the original proposal was not acceptable, interested parties would attempt to develop a mutually acceptable alternative through a separate set of negotiations; and
- E. On November 15, 1995, a tentative negotiated settlement for an Off-System Incentive Program was circulated to all Registered Intervenors and the Commission ("the OSIP"); and
- F. The Commission has reviewed the OSIP together with comments received from Registered Intervenors and has determined that approval is in the public interest.

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2

**NOW THEREFORE** the Commission orders as follows:

1. The OSIP attached as Appendix 1 to this order is approved subject to BC Gas complying with the terms set out therein.
2. For the benefit of interested parties, the Commission hereby clarifies that the required reports referred to in Appendix 1 to this order are considered to be public documents, and as such will be available for review at the Commission offices.

**DATED** at the City of Vancouver, in the Province of British Columbia, this 28th day of November, 1995.

BY ORDER



Dr. Mark K. Jaccard  
Chairperson

Attachment

**BC GAS UTILITY LTD.  
OFF-SYSTEM INCENTIVE PROGRAM**

**BACKGROUND**

BC Gas Utility Ltd. ("BC Gas" or "Company") first initiated its off-system business activities in March 1992. Starting with month to month commodity sales of surplus core market gas supplies; i.e. valley gas, the Company's off-system business has since evolved to include daily spot sales, capacity release, swaps/exchanges, as well as other types of transactions. Off system business does not include volume incentive adjustments, cost of service, or other credits or rebates received under the terms of baseload or other gas supply contracts.

At present, this area of the Company's business represents approximately \$25.0 million in gross annual revenues and provides about \$5.8 million in annual net revenues. The most expensive discretionary purchases of gas are preferentially sold off-system. Net revenues are calculated by subtracting the variable cost of gas from the off-system revenue and used to offset fixed costs paid for by the Company's core market customers.

The Company's Revenue Requirement Application dated June 30, 1995 included several references to gas supply and off-system incentives. BC Gas submitted that a well developed Off-System Incentive Program ("OSIP") would serve to align the interests of customers, shareholders and employees.

In response to an information request from Commission Staff, BC Gas submitted a preliminary incentive proposal that was subsequently reviewed at a technical workshop held on September 14.

Following feedback received at the workshop from intervenors and Commission Staff, a revised OSIP was developed addressing four key objectives:

1. avoid paying incentives for activities and results already achieved, but reward new, substantial exertions by the Company
2. discourage activity that might adversely affect the security of supply or total net gas costs
3. minimize administrative effort
4. maximize net revenues.

At meetings held on October 16th and 20th, two alternative proposals were discussed. Final agreement on a methodology, terms and conditions was reached on October 27, 1995. Participating at these meetings were counsel representing the Consumers Association of Canada (B.C.), B.C. Old Age Pensioners' Organization, Council of Senior Citizen's Organization of B.C., Federated Anti-Poverty Groups of B.C., Senior Citizens' Association of B.C., West End Senior's Network Society, and representatives of Westcoast Energy Inc., BC Gas Utility Ltd. and British Columbia Utilities Commission Staff.

This document sets out the terms of the OSIP which those participating in the meetings, other than Westcoast Energy Inc., consider to be appropriate for implementation by BC Gas. Agreement on the terms and conditions of this OSIP involved compromise and represents a balance of interests and a consensus among the parties who consider it to be appropriate.

## **TERMS**

### **1. Test Period**

The term of this OSIP will extend over two years, namely calendar years 1996 and 1997. In order to determine the incentive to be received, or the shortfall contribution to be paid, in 1996 by BC Gas under the OSIP, the Company's performance during the gas contract year November 1, 1995 to October 31, 1996 will be examined. In order to determine the incentive to be received, or the shortfall contribution to be paid, in 1997 by BC Gas under the OSIP, the Company's performance during the gas contract year November 1, 1996 to October 31, 1997 will be examined. BC Gas will withdraw from the Gas Cost Reconciliation Account ("GCRA") the incentive to be received by the Company, or deposit to GCRA the shortfall contribution to be paid by the Company, for each of 1996 and 1997 on December 31 of those years.

### **2. Benchmark**

The annual net revenue benchmark level established for BC Gas has been set at \$5.8 million (Cdn) in each gas contract year. This benchmark is representative of the average level achieved over the past three years. Much discussion occurred regarding the appropriate benchmark on a forecast basis. For this initial OSIP, the parties have agreed to use the historic level of net revenue as the benchmark and to include an adjustment to the sharing mechanism in 1997 (see item 5.).

### **3. Sharing Mechanism**

The mechanism provides for a symmetrical sharing of annual net revenue variances above and below the benchmark. The BC Gas share of any such variance will be:

- 0 % for the first \$.5 million; plus
- 50 % for the portion between \$.5 million and \$2.5 million; plus
- 20 % for the portion in excess of \$2.5 million.

Where the net revenue falls below the benchmark, the BC Gas share becomes a payment to the core market GCRA. The 0% band reflects a degree of uncertainty about the appropriate benchmark, and is subject to further adjustment for 1997 (see item 5.). The 20% band at the upper end limits the risk for the core market of large windfall profit-taking by the Company and at the lower end limits the risk for the Company of large unavoidable losses. The following examples represent the probable high and low limits. A broader range of outcomes is illustrated in Appendix A.

#### **Examples:**

- 1) Net Revenue = \$7.3 million = variance of \$1.5 million above benchmark

<u>Net Revenues (\$MM)</u>	<u>Core</u>	<u>BC Gas</u>
benchmark	5.8	0.0
first .5 variance	0.5	0.0
next 1.0 variance	0.5	0.5
Total Share(s)	\$6.8	\$0.5

- 2) Net Revenue = \$4.3 million = variance of \$1.5 million below benchmark

<u>Net Revenue (\$ MM)</u>	<u>Core</u>	<u>BC Gas</u>
benchmark	5.8	0.0
first .5 variance	(0.5)	0.0
next 1.0 variance	<u>(0.5)</u>	<u>(0.5)</u>
Total Share(s)	\$4.8*	(\$0.5)

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\*net revenue of \$4.3 plus BC Gas payment of \$0.5

4. Employee Incentive

Within the context of other incentive plans for employees, BC Gas will implement for those Gas Supply employees directly responsible for generating net revenues under this OSIP, a specific incentive arrangement related to the incentive revenue earned by BC Gas. Upon its completion, BC Gas will forward a copy of its employee incentive program to the Commission.

5. Other Terms

Interest on GCRA balances - Variances between the actual balance and forecast balance in the GCRA, whether positive or negative, will attract interest at the Company's short term borrowing rate. Interest will be calculated monthly and added to or deducted from the GCRA balances which accrue after January 1, 1996.

Adjustment Provisions - Two independent adjustments are provided for:

- To partially address concerns about the difficulty of setting an appropriate benchmark, the historic average annual net revenue used to set the benchmark will be recalculated at the end of the 1995/1996 gas year to include the actual net revenue for that year. The variance from the benchmark of \$5.8 million will be used to adjust the 0% sharing bandwidth for 1997. Positive variances will only affect the upper limit and negative variances will only affect the lower limit.

Positive example:      -1996 net revenue = \$7.8 million  
                                      -updated average =  $(3 \times 5.8 + 7.8) / 4 = \$6.3$  million  
                                      -bandwidth adjustment factor =  $6.3 - 5.8 = \$0.5$  million  
                                      -new 0% bandwidth upper limit =  $6.3 + .5 = \$6.8$  million

In this example, BC Gas would earn an incentive for 1997 if net revenues exceed \$6.8 million, and 50/50 sharing would apply up to \$8.8 million. (The 50/50 sharing bandwidths of \$2 million are unaffected by this adjustment.)

- It is also recognized that in a dynamic and evolving regulatory environment, certain fundamental assumptions about gas cost structure and operating circumstances are subject to change. It is acknowledged this OSIP may require a Commission review and adjustment following any significant regulatory decisions that markedly alter these fundamental assumptions upon which this plan has been developed; e.g. BC Gas rate design, NEB, FERC or other regulatory rulings affecting BC Gas' interconnecting pipelines, etc.

Settlement Expiration & Incentive Review - Recognizing the limited experience gained to date with respect to off-system sales and the evolving nature of gas commodity markets in general, this OSIP is recognized as interim in nature, applying only to the two year test period. At the end of the test period it will be reviewed and its future disposition (continuation, adjustment, consolidation with other incentives, abandonment) will be subject to Commission approval.

Regulatory & Management Reporting - In order for the Commission to adequately monitor and evaluate the Company's performance, the already well developed record keeping and reporting procedures will be supplemented. BC Gas will continue with its current practice of regular month by month filings with the Commission of a summary report that details all off-system activity and associated financial impacts.

BC Gas will also keep distinct and separate records, for audit purposes, of its daily "Priority Schedule", which determines the available supply and its marginal costs, a daily "Load Forecast Sheet", which details all on-system supply requirements and a "Deal Sheet" for each and every transaction that will feature all information related to the economics of each transaction.

BC Gas will confer with Commission staff to ensure that these reports provide an appropriate level of disclosure and audit capability with a minimum administrative burden. Commission staff will examine the calculation of any incentive payments received under the OSIP and the Commission will make any appropriate adjustments. For the benefit of interested parties, an overview report by Commission staff will be issued annually which provides an analysis of the effectiveness of the OSIP.

OFF-SYSTEM INCENTIVE SETTLEMENT  
SHARING MECHANISM

