



LETTER No. L-5-00

ROBERT J. PELLATT
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VIA FACSIMILE

January 14, 2000

Mr. David M. Masuhara
Vice President
Legal, Regulatory & Logistics
BC Gas Utility Ltd.
24th Floor, 1111 West Georgia Street
Vancouver, B.C. V6E 4M4

Dear Mr. Masuhara:

Re: BC Gas Utility Ltd.
Reinforcement of the Salmon Arm Lateral
Deferral Account for the Satellite Liquefied Natural Gas ("LNG") Project

This letter is in response to BC Gas' request, dated June 25, 1999, for approval to amortize the balance in the Salmon Arm Satellite LNG deferral account over three years commencing June 1, 2000. The account balance as of August 31, 1999 was estimated to be \$563,378 plus \$54,625 of allowance for funds used during construction ("AFUDC").

Commission Order No. G-103-97, dated October 2, 1997 permitted a deferral account to be set up for expenditures that related to the satellite LNG facility. It stated the following:

"A deferral account for the recording of up to \$1.7 million (plus overhead and AFUDC) of reasonable and prudent Phase 1 expenditures that relate to a satellite LNG peak shaving facility to reinforce its Salmon Arm natural gas lateral is approved for BC Gas."

The cover letter to the Order stated:

"The Commission has concerns about the level of expenditures that the Company proposes for detailed engineering work and site options prior to confirming, in a broad sense, that an LNG alternative will be acceptable to the public and local authorities. The Company will be expected to demonstrate that costs recorded in the deferral account were prudently incurred in order to recover them from customers in rates."

The Commission has considered BC Gas' request for amortization of the deferral account balance, and has reviewed the information identified in the attached Chronology of Correspondence and reports from staff regarding several meetings with BC Gas.

The Commission considers that \$135,189 of study costs related to alternatives other than satellite LNG should be removed from the deferral account, as the approval of the account was specific to the satellite LNG alternative. The Commission recognizes that some or all of these removed costs may be a prudent component of a project to reinforce the Salmon Arm lateral by compression or other alternative.

BC Gas has recorded \$228,436 of CDS Research Ltd. ("CDS") costs in the account. The Commission has the following concerns about the costs paid to CDS:

1. The scope of the work appears poorly planned.

The scope provided for comprehensive development of four configurations of the LNG facility. The level of design detail appears excessive for this preliminary stage of the design process. The assessment of planning alternatives was still under review with no specific site identified and public acceptance of LNG was still required.

2. The arrangement with CDS Research was not documented.

The project was initiated without a written contract and terms of reference. It appears that CDS received all of its instructions verbally, contrary to proper project management procedures and this presented significant difficulty when the suspension of the project was attempted.

3. The consultant's activities appear poorly managed.

BC Gas did not document its directions to CDS and there is no evidence that BC Gas required regular, written progress reports or provided ongoing scrutiny of, and feedback on, the work generated. Notwithstanding the apparent urgency to reinforce the Salmon Arm lateral, BC Gas accepted a delay in the start of work until early 1998.

4. The consultant's work was not terminated when the results were no longer needed.

There was no decisive action to stop the project when circumstances warranted it. As data about likely delivery pressures from Westcoast Energy Inc. became available, including testimony at the Southern Crossing Pipeline proceeding, BC Gas should have acted to limit work on the project. BC Gas attempted to limit the expenditure at one critical point (the February 12, 1998 letter from CDS refers to "... your directive to freeze the project ..."). However, it was eventually decided to continue and "... preserve the maximum amount of value, ..." (BC Gas letter dated December 17, 1999). The value is questionable at this juncture. It is apparent that the LNG option was no longer the optimum alternative for Salmon Arm and further study had dubious benefit. Nevertheless, the CDS study continued into February and March 1999 with the final report available in August 1999.

For the foregoing reasons, the Commission considers that the CDS study was ill conceived and poorly administered and, based on the current information, that its cost should not be recovered from ratepayers. Project management is a serious issue especially with the number and extent of the projects in which BC Gas is currently engaged.

Therefore, the Commission accepts that the remaining expenditures of \$199,753 plus related AFUDC are consistent with the terms of the deferral account and the reinforcement requirements at Salmon Arm. The Commission is prepared to approve the amortization of this amount over three years commencing January 1, 2001.

However, before the Commission makes a final determination with respect to the CDS expenditure, BC Gas is offered a final opportunity to justify its request to amortize the full amount. It is requested to provide, in written form, any further information to support the position that the CDS costs meet the test for prudence and, therefore, the expenses should be recovered from ratepayers. BC Gas should file any further submissions on this matter by February 15, 2000.

Yours truly,

Original signed by:

Robert J. Pellatt

RB/cms
Attachment

Chronology of Correspondence

- BC Gas letter of August 5, 1997, requesting approval to establish a deferral account for \$1.4 to \$2.5 million of Phase 1 expenditures to reinforce the Salmon Arm lateral.
- Commission Order No. G-103-97 dated October 3, 1997 and cover letter dated October 6, 1997, approving a deferral account for the recording of up to \$1.7 million (plus overhead and AFUDC).
- Progress Report #1, dated December 17, 1997.
- Paper copy of slides from January 21, 1998 meeting of BC Gas (Messrs. Kanzaki and Grey) and Commission staff (Messrs. Grant and Williston).
- Letter from BC Gas, dated April 1, 1998.
- Progress Report #2, dated April 30, 1998.
- Letter from the Commission, L-29-98 dated May 29, 1998.
- Progress Report #3, dated July 31, 1998.
- Progress Report #4, dated March 31, 1999.
- Progress Report #5, dated June 25, 1999, requesting amortization of the deferral account balance.
- BC Gas response to Staff Information Request, dated September 20, 1999, including CDS Research Ltd., Report Project Summary.
- Written Information provided at a meeting of November 8, 1998 between representatives of BC Gas (Messrs. Samuels, Grey) and Commission staff (Messrs. Williston and Brownell) -
 - Paper copy of slide collection for Salmon Arm Lateral project justification
 - Letter from Summit Environmental Consultants, dated November 10, 1997
 - Letter from CDS Research Ltd., dated February 12, 1998
 - Facsimile from PTL Associates
 - Excerpts from March 24, 1998 BC Gas Report.
- Letter from BC Gas, dated November 25, 1999.
- Letter from BC Gas, dated December 17, 1999, responding to Commission Staff Information Request.