



IN THE MATTER OF
the Utilities Commission Act, R.S.B.C. 1996, Chapter 473

and

An Application by BC Gas Utility Ltd.
for Approval of Lease Arrangements with the City of Kelowna

BEFORE: P. Ostergaard, Chair)
R.D. Deane, Commissioner) October 17, 2001

O R D E R

WHEREAS:

- A. On May 18, 2001, BC Gas Utility Ltd. ("BC Gas", "the Utility") applied to the British Columbia Utilities Commission ("the Commission") for approval to enter into Lease-In-Lease-Out ("LILO") arrangements with the City of Kelowna ("the City"), and to establish the mode of regulation under which the BC Gas rates will be set to take these arrangements into account; and
- B. The LILO Application arises out of the existing BC Gas Franchise Agreement, which has been in place since 1957 and provides an option for the City to "buy-out" the existing natural gas distribution system within the municipality's boundary in the event that the parties cannot agree on the terms of franchise renewal; and
- C. The City would enter into a 35-year capital lease with BC Gas for the natural gas distribution system within the municipality's boundary. Title to the assets remains with BC Gas but the value of the City's rights in the lease would be set at \$50 million. The City would pre-pay 95% of this value to BC Gas as rent due under the lease; the remaining 5% would be paid to BC Gas over the life of the lease. After establishing the capital lease, the City would lease back the operation of the distribution system to BC Gas through a 17-year operating lease. The terms of the operating lease require BC Gas to make annual payments to the City over the 17-year term; and
- D. BC Gas has franchise agreements with several other municipalities that contain purchase options and the Utility plans to offer this type of arrangement to them; and

- E. The Commission held a Workshop and Pre-hearing Conference on the LILO Application on Thursday, July 5, 2001, and participants expressed their preference for a written hearing process; and
- F. Commission Order No. G-78-01 established a Regulatory Agenda for a written public hearing and no submissions from the public were received; and
- G. On August 13, 2001, BC Gas filed minor amendments to some of the agreements attached to, and forming part of, the LILO Application; and
- H. The arrangements have been approved by the Inspector of Municipalities; and
- I. The Commission has reviewed the LILO Application and finds that the arrangements should be approved.

NOW THEREFORE the Commission orders as follows:

- 1. The Commission approves for BC Gas the LILO Application (including the minor amendments to the agreements dated August 13, 2001) to enter into the proposed lease arrangements with the City of Kelowna, specifically:
 - a. pursuant to Section 52 of the Utilities Commission Act (“the Act”), the encumbrance of property under the Capital Lease between BC Gas and the City (Appendix C of the Application), and the terms of that lease;
 - b. pursuant to Section 52 of the Act, the encumbrance of property under the Additions Option Agreement between BC Gas and the City (Appendix E of the Application), and the terms of that agreement;
 - c. the terms of the Operating Lease between BC Gas and the City (Appendix D of the Application);
 - d. the determination of the rates of BC Gas on the basis that the revenue requirement of BC Gas be established with the property that is the subject of the Operating Lease with the City and the Additions Option Agreement with the City being in rate base at its depreciated value, being subject to normal depreciation, and earning a normal return on rate base;

- e. the annual Operating Lease payments from BC Gas to the City and the payments from the City to BC Gas pursuant to the Capital Lease are to be accounted for as non-utility transactions;
- f. the interest rate for the deemed debt required for regulatory reconciliation purposes in the City of Kelowna LILO arrangements be set for future Revenue Requirement Applications at a rate equal to the BC Gas cost of long term borrowing (including issue costs) at the time of closing of the City of Kelowna LILO transactions;
- g. the principle implicit in the LILO arrangements that future material changes in accounting standards, taxes or financing terms that affect the LILO transactions, or the accounting for them, will not result in a change to the rates paid by customers, nor will such events adversely affect BC Gas and its shareholders; and
- h. recovery of the costs incurred related to these transactions, including Development Costs and Closing Costs and the costs of this Application, in the manner described in Section 3.6 of the LILO Application, inclusive of crediting any reimbursed Development Costs to BC Gas' cost of service in the year in which they are received.

DATED at the City of Vancouver, in the Province of British Columbia, this 18th day of October 2001.

BY ORDER

Original signed by:

Peter Ostergaard
Chair