



LETTER NO. L-34-04

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VIA E-MAIL

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June 30, 2004

Mr. Scott Thomson
Vice President, Finance and Regulatory Affairs
Terasen Gas Inc.
16705 Fraser Highway
Surrey, B.C. V3S 2X7

Dear Mr. Thomson:

Re: Terasen Gas (Vancouver Island) Inc. ("TGVI")
Preliminary Expenditures on Gas Supply to Vancouver Island
Deferral Account – May 2004 Update Report

On May 31, 2004 in response to Commission Letter No. L-21-04, Terasen Gas filed its May 2004 Update Report. Total expenditures to the end of May 2004 were projected to be \$793,000, including \$134,000 for expenditures on matters that were the subject of Commission Letter No. L-27-03.

In the May 31st letter, TGVI requests approval to record project development costs relating to Terasen Gas Inc., an affiliate of TGVI, in the deferral account that was approved by Order No. G-69-03. These costs amounted to \$65,000 in 2003, and TGVI submitted that it is necessary to include these costs in the deferral account in order to comply with the Commission direction respecting affiliate transactions. Although the transfer pricing policy of the two companies may establish the amount of charges between the TGVI and Terasen Gas Inc. in 2003, TGVI is requested to explain the nature of services required, why it was unable to complete this work using its own staff, and how it confirmed that Terasen Gas Inc. was the least expensive source of outside assistance.

TGVI projects that a further \$77,000 of Terasen Gas Inc. costs should be recorded in the deferral account in 2004. TGVI is requested to confirm that the 2004 costs to be recorded are limited to Direct Charges and do not include any Allocations under the Shared Services Management Agreement. TGVI also needs to explain the nature of services obtained and the steps it is taking to compare Terasen Gas Inc. costs to those of other service providers.

To the extent TGVI can demonstrate that Terasen Gas Inc. billings relative to the Vancouver Island Liquefied Natural Gas project represent incremental payments and are cost-effective, the Commission approves recording them in the deferral account.

On page 4 of the May 31st letter, TGVI refers to discussions with Engineering, Procurement and Construction ("EPC") contractors for the LNG facility, and refers to both sole source arrangements and to inviting bids from three or more contractors. TGVI will be expected to justify that its choice of sole sourcing or bidding the

contract is expected to result in the best outcome for its customers, when it files future Update Reports and applies for a Certificate of Public Convenience and Necessity for the project. Also, when the Commission reviews the prudence of the expenditures recorded in the deferral account, TGVI will be expected to show that all expenditures were necessary and that it has made every effort to contain these expenditures.

Yours truly,

Original signed by:

Robert J. Pellatt

JBW/yl