SIXTH FLOOR, 900 HOWE STREET, BOX 250
VANCOUVER, B.C. V6Z 2N3 CANADA
web site: http://www.bcuc.com

BRITISH COLUMBIA UTILITIES COMMISSION

ORDER NUMBER G-118-05

TELEPHONE: (604) 660-4700
BC TOLL FREE: 1-800-663-1385
FACSIMILE: (604) 660-1102

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

and

An Application by Stargas Utilities Ltd.
for Approval to Alter Rates, Make Additional Deferrals, Levy Administrative Charges
and Establish a Gas Cost Variance Account

BEFORE: L.F. Kelsey, Commissioner November 7, 2005

O R D E R

WHEREAS:

A. The Commission, by Order No. C-4-00, approved a Certificate of Public Convenience and Necessity for Stargas Utilities Ltd. ("Stargas", "the Company") to operate a natural gas distribution system at the resort community of Silver Star; and

B. On October 22, 2004, Stargas applied for Commission approval to alter rates, make additional deferrals and levy administrative charges; and

C. On January 5, 2004, Stargas agreed to withdraw its application and re-file after its May 31, 2005 fiscal year end; and

D. By Order No. G-2-05, the Commission set the current rates as interim effective January 1, 2005 and directed Stargas to file an Application by July 18, 2005 that contains the actual results from January 1, 2005 to May 31, 2005 and forecast results for June 1, 2005 to December 31, 2005; and

E. On July 13, 2005, Stargas applied for Commission approval to increase residential rates by seven cents per gigajoule ("GJ"), decrease commercial rates by 11 cents per GJ; defer and amortize a Payment for Shortfall penalty of approximately $42,000; levy administrative recoveries of 2.5 percent for customers paying bills by credit or debit cards and charge new customers an additional fee of 10 percent of the cost of installing a new service ("the Application"); and

F. On July 19, 2005 the Company filed an addendum requesting the approval of a Gas Cost Variance Account ("GCVA") effective January 1, 2005 with a starting credit balance of $15,139 as of May 31, 2005; and

G. Commission Order No. G-71-05 established a Regulatory Agenda and written public hearing to review the Application; and

H. The Commission has reviewed the Application by Stargas to Alter Rates, Make Additional Deferrals, Levy

. . . /2

Administrative Charges and Establish a GCVA and the evidence adduced thereon, all as set forth in the Reasons attached as Appendix A.

NOW THEREFORE pursuant to Sections 50(2), 58, 60 and 61of the Utilities Commission Act ("the Act"), the Commission orders as follows:

1. The Commission approves the requested increase of seven cents per GJ for residential customers and a rate decrease of 11 cents per GJ for small and large commercial customers, effective January 1, 2005. The Commission orders that the amount of the 2005 Residential rate increase from January to November be billed as a lump sum charge including interest on the customers' December 2005 bill. The Commission orders that the amount of the 2005 Commercial rate decrease from January to November be refunded as a lump sum credit including interest on the customers' December 2005 bill. The interest rate to be applied to the lump sum charge or credit is at the average prime rate at the principal bank where Stargas conducts its business.

2. The Commission approves the Stargas request to defer and amortize the Payment for Shortfall penalty over five years commencing on January 1, 2005.

3. The Commission approves the Stargas request to establish a non-rate base GCVA effective January 1, 2005 with a credit balance of $15,139 as of May 31, 2005.

4. Until such time that credit card company approval to levy transaction fees is granted, Stargas is to continue to include the costs of credit card transactions as a component of O&M. In the event that the vendor credit card agreement allows for the recovery of transaction fees directly from customers paying by credit/debit card, Stargas may apply for Commission approval to recover these transaction costs as a fee under its tariff.

5. The Commission approves the 10 percent administrative fee on the installation of new services added to the schedule of rates and charges, applying to all applications for new service, effective December 1, 2005.

6. The Commission does not consider that unpaid dividends are appropriate for inclusion in rate base and should be removed. These cumulative dividends will become a cost to Stargas when it has the financial resources to be able to pay dividends. Accordingly, the preferred shares are to be shown as a no-cost item in the capital structure, until such time as the dividends are declared or paid.

7. The Commission approves the 5-year promissory note to Terasen Utility Services Inc. for $57,160 at an interest rate of 8 percent issued on January 15, 2004, pursuant to Section 50(2) of the Act.

8. The Commission considers the market rate for management, regulatory and other executive services to Stargas should be at the rate for a KPMG account manager. Accordingly, the rate for management, regulatory and other executive services that is allowed for recovery in rates is limited to $120 per hour.

9. Stargas is to provide, subject to timely filing, amended Gas Tariff Rate Schedules in accordance with the approvals given by this Order.

DATED at the City of Vancouver, in the Province of British Columbia, this 15th day of November, 2005.

BY ORDER

Original signed by:

L.F. Kelsey
Commissioner

Attachment

STARGAS UTILITIES LTD.
2005 APPLICATION TO ALTER RATES, MAKE ADDITIONAL DEFERRALS AND LEVY ADMINISTRATIVE CHARGES

REASONS FOR DECISION

1.0 INTRODUCTION

1.1 Background

Silver Star Mountain Resorts Ltd. (the "Resort") is the primary developer and ski hill operator in the resort community located north-east of Vernon. The Resort created a subsidiary, now known as Stargas Utilities Ltd. ("Stargas", "the Company"), which acquired the existing propane grid from its parent. By Order No. C-4-00, the Commission approved a Certificate of Public Convenience and Necessity for Stargas to operate a natural gas distribution system at the Resort.

The Stargas rates are based on the price of alternative energy sources (electricity and propane) and in the short-term are not intended to fully recover costs, or provide a return on investment. Over time, the Company hopes to earn a full return.

On August 15, 2002, Stargas filed for Commission approval to re-capitalize the Company, revise the ownership structure, and increase rates and fees to recover cash flow deficiencies. Commission Order No. G-61-02 established a written hearing for the review of the Stargas application and Order No. G-73-02 scheduled a public information town hall meeting. As a result of discussions at the Commission's public information meeting held in Silver Star Village, Stargas agreed to reduce its requirements and amended its application on November 1, 2002. The amended application exempted the installation of a new customer service from a non-discretionary administrative cost recovery fee of 10 percent on the cost invoiced by contractors. The amended application was approved by Order No. G-80-02 effective December 1, 2002 ("2002 Application").

On October 22, 2004, Stargas filed for Commission approval to increase Residential rates by seven cents per GJ (0.43 percent) and reduce Small and Large Commercial rates by 11 cents per GJ (-0.65 percent). Stargas also proposed the deferral and amortization of a gas supply take or pay penalty of approximately $42,000, administrative recoveries of 2.5 percent for customers paying bills by credit or debit card, and an additional administrative fee equal to 10 percent of the Company's cost of installing a new service for new customers. On January 5, 2004, Stargas agreed to withdraw its application and re-file after its May 31, 2005 fiscal year end.

By Order No. G-2-05, the Commission set the current rates as interim effective January 1, 2005 and directed Stargas to file an Application by July 18, 2005 that contains the actual results from January 1, 2005 to May 31, 2005 and forecast results for June 1, 2005 to December 31, 2005.

Currently, both residential and commercial natural gas rates are lower than propane rates. The price of residential electricity is slightly lower than natural gas, while the price of commercial electricity is higher.

1.2 The Application

On July 13, 2005, Stargas applied to the Commission for approval to increase residential rates by seven cents per GJ, decrease commercial rates by 11 cents per GJ; defer and amortize a Payment for Shortfall penalty of approximately $42,000; levy administrative recoveries of 2.5 percent for customers paying bills by credit or debit cards and charge an additional fee of 10 percent of the cost of installing a new service. On July 19, 2005 the Company filed an addendum requesting the approval of a Gas Cost Variance Account ("GCVA") effective January1, 2005 with a credit balance of $15,139 as of May 31, 2005 ("the Application").

Based on the average annual use of 120 GJ for residential and 700 GJ for commercial customers shown on page 12 of the Application, the average annual increase for residential customers would be $8.40 and the decrease for commercial customers would be $77.00.

1.3 The Written Hearing Process

Commission Order No. G-71-05 established a written public hearing for review of the Application. Interventions were received from the Silver Star Property Owners Association and Mr. David Bissett.

Stargas responded to information requests from the Commission and Mr. David Bissett. The Intervenors did not provide written submissions to the Commission commenting on the Application.

2.0 FINANCING

2.1 Promissory note

On January 15, 2004, Terasen Utility Services Inc. ("TUS") provided Stargas with financing through an 8 percent 5-year promissory note for $57,160. Commission approval of this financing is required pursuant to Section 50(2) of the Utilities Commission Act ("the Act"):

> "Except in the case of a security evidencing indebtedness payable less than one year from its date, a public utility must not issue a security without first obtaining approval of the commission under this section and, if Section 54 applies, under that section."

Commission approval was not obtained before this financing was completed. Stargas states that the principal and terms offered in the financing were the most favourable that the Company could obtain at that time.

The Commission approves the 5-year promissory note to TUS for $57,160 at an interest rate of 8 percent issued on January 15, 2004, pursuant to Section 50(2) of the Act.

3.0 RATE BASE

3.1 Deferred Payment for Shortfall Penalty

On February 11, 2000, BC Gas Utility Ltd. ("BC Gas") filed with the Commission an application to serve the Resort under a Rate Schedule 3 Tariff Supplement for a 5-year term commencing October 1, 1999. Under the terms of the agreement, Stargas was required to pay a main extension contribution in aid of construction ("CIAC") of $444,329 plus $31,103.03 GST and take, or pay for a minimum quantity of gas. The CIAC amount is based on the estimated cost of construction and natural gas consumption. The higher the forecast consumption, the lower the CIAC required.

Under Section 2.4 of the Rate Schedule 3 Tariff Supplement:

> "Payment for Shortfall – If on the 5th Anniversary of the Commencement Date there remains a Gas consumption shortfall, the Customer will pay to BC Gas on the shortfall all of the charges under Rate Schedule 3, Table Charges other than the Gas Cost Recovery Charge and Riders set out therein."

Due to lower than forecast customer additions and usage, Stargas was required to pay a "Payment for Shortfall" penalty. The Company has requested approval to defer the "Payment for Shortfall" penalty of $42,160 and amortize the penalty over five years commencing January 1, 2005.

The Commission approves the Stargas request to defer and amortize the Payment for Shortfall penalty over five years commencing on January 1, 2005.

3.2 Unpaid Cumulative Preferred Dividends

Stargas had incurred cumulative tax losses in excess of $615,000 at May 31, 2002 and filed an application to re-capitalize the Company on August 15, 2002. The Company proposed to issue cumulative preferred shares in order to absorb the cumulative losses and recognize the "time value" of the shareholders' investment. Stargas shareholders recognized that a return on shareholder equity would be deferred until the Company became profitable. Commission Order No. G-80-02 approved the issuance of $400,000 of cumulative preferred shares on November 7, 2002. The deferred dividend rate on the preferred shares is based on the Commission's annual benchmark return on equity plus 75 basis points.

Stargas has recorded cumulative unpaid dividends of $122,693 that are included in the 2005 Test Year rate base. In response to BCUC IR 1.3.1, Stargas confirmed that the dividends have not been declared or paid, and that Stargas does not expect to be in a position pay dividends in the next several years. The unpaid dividends included in the 2005 Test Year rate base represent a "notional" return on equity and are not an "actual" cost of capital.

The Commission does not consider that unpaid dividends are appropriate for inclusion in rate base and should be removed. These cumulative dividends will become a cost to Stargas when it has the financial resources to be able to pay dividends. Accordingly, the preferred shares are to be shown as a no-cost item in the capital structure, until such time as the dividends are declared or paid.

4.0 REVENUES

4.1 Administrative Recovery for Customers Paying by Credit/Debit Card

Stargas offers its customers direct bill payment by credit card and is investigating debit card bill payment. Due to the small number and dollar value of its transactions, Stargas incurs a 2.56 percent charge on credit card payments and additional fixed charges for the equipment and line rental. To recover these costs, Stargas seeks to levy an administrative recovery of 2.5 percent of the bill amount for customers paying by credit card. If payment by debit card is introduced, the 2.5 percent charge will also apply to debit card payments.

The current Stargas vendor credit card agreement does not permit Stargas to charge transaction fees to customers that pay by credit card. As stated in a separate Refinancing application, the Company is in the process of replacing its bank debt and has a verbal agreement from TD Canada Trust, its prospective bank, to levy transaction fees on credit and debit card payments.

Until such time that credit card company approval to levy transaction fees is granted, Stargas is to continue to include the costs of credit card transactions as a component of O&M. In the event that the vendor credit card agreement allows for the recovery of transaction fees directly from customers paying by credit/debit card, Stargas may apply for Commission approval to recover these transaction costs as a fee under its tariff.

4.2 Administrative Fee of 10 percent of the Cost of Installing a New Service

For all customer initiated work, except for the installation of new services, Stargas charges a 10 percent administrative fee on the cost invoiced by contractors. In order to reach consensus during the negotiation of its 2002 Application to re-capitalize the Company, revise the ownership structure, and increase rates and fees to recover cash flow deficiencies, the Company agreed to exempt new customers from the 10 percent administrative fee. Stargas is now requesting that the 10 percent administrative fee also be applied to the cost of installing new services.

The costs related to coordinating the installation of new services are currently included in general expenses. Charging a 10 percent administrative fee on the installation of new services would recover the additional costs from the customers' responsible.

The Commission approves the 10 percent administrative fee on the installation of new services added to the schedule of rates and charges, applying to all applications for new service, effective December 1, 2005.

5.0 EXPENSES

5.1 Application for GCVA

Stargas received gas supply from Terasen Gas Inc. ("TGI") through Tariff Supplement No. A-2 (Rate Schedule 3 – Large Commercial Service) that was approved by Commission Order No. G-19-00, and expired on October 1, 2004. Direct Energy Marketing Limited ("DEML") replaced TGI as the Company's gas supplier on November 1, 2004 and Order No. E-2-05 approved the natural gas supply and management agreement between Stargas and DEML. Commission Order No. G-6-05 approved the Terasen Gas Rate Schedule 25 Agreement, Tariff Supplement 13, for firm transportation service to Stargas effective November 1, 2004.

On July 19, 2005 the Company filed an addendum to the Application requesting the approval of a GCVA effective January 1, 2005. A GCVA accumulates the difference between the gas cost recovered in rates and the actual cost incurred in purchasing the commodity. TGI provides a GCVA as part of its Rate 3 service, but not its Rate 25 service. As a result of the change from TGI to DEML, Stargas has requested approval of a non-rate base deferral GCVA. From January 1, 2005 to May 31, 2005, Stargas reported that the revenue from the cost of gas recovered in rates exceeded the cost of purchasing the commodity by $15,139. The Company proposes to file annual requests for amendment to its gas cost recovery amount including any balance in the GCVA.

The Commission approves the Stargas request to establish a non-rate base GCVA effective January 1, 2005 with a credit balance of $15,139 as of May 31, 2005. Other gas utilities report their GCVA balances on a quarterly basis and Stargas should consider if quarterly reporting of its GCVA balance to the Commission is necessary in its circumstances.

5.2 Okanagan Funding Ltd. Management Service Fees

Stargas has a non-arms length relationship with Okanagan Funding Ltd., the company that provides management services to Stargas. In the Application, Stargas states:

> "Okanagan Funding Ltd., a company owned by Mr. & Mrs. Blumes, supplies management services to the utility at the following rates (designed to recover the embedded cost of the respective service providers and unchanged from 2002):
>
> Administrative services: $40 per hour
> Accounting services $60 per hour
> Management, regulatory and other executive services $250 per hour"

Management services are also provided by Mr. Larry Youell, the President of Stargas. In its response to BCUC IR 5.1.4, Stargas provided the following market rates for management services in the Vernon area:

Administrative services: $45 to $75 per hour
Accounting services: $75 per to 145 per hour
KPMG account manager - Senior accounting services: $120 per hour

A regulated utility, such as Stargas, should not be paying fees that are in excess of comparable market rates. **The Commission considers the market rate for management, regulatory and other executive services to Stargas should be at the rate for a KPMG account manager. Accordingly, the rate for management, regulatory and other executive services that is allowed for recovery in rates is limited to $120 per hour.**

5.3 Interim and Permanent Rates

Commission Order No. G-2-05 directed Stargas to refund the difference between the 2005 permanent rates and interim rates, if the permanent 2005 rates were lower than the interim rates.

The Application showed that at the proposed rates, residential and commercial customers are expected to receive annual savings compared to the cost of competitive fuels-propane and electricity. These Reasons for Decision contain adjustments to the Stargas cost of service for the 2005 calendar year. However, even with these adjustments, the Company is not expected to earn its allowed return during the calendar 2005 period; therefore no adjustment to the proposed rates is required.

The Commission approves the requested increase of seven cents per GJ for residential customers and the rate decrease of 11 cents per GJ for small and large commercial customers, effective January 1, 2005. The Commission orders that the amount of the 2005 Residential rate increase from January to November be billed as a lump sum charge including interest on the customers' December 2005 bill. The Commission orders that the amount of the 2005 Commercial rate decrease from January to November be refunded as a lump sum credit including interest on the customers' December 2005 bill. The interest rate to be applied to the lump sum charge or credit is at the average prime rate at the principal bank where Stargas conducts its business.