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**BRITISH COLUMBIA
UTILITIES COMMISSION**

**ORDER
NUMBER** G-39-05

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

and

**An Application by Terasen Gas Inc.
regarding Rate Schedules 7, 10, 14 and 14A
for Market-Based Commodity Rates for the 2005/06 Gas Contract Year**

BEFORE: L.F. Kelsey, Commissioner April 21, 2005

O R D E R

WHEREAS:

- A. Pursuant to Order No. G-37-04, the Commission reviewed in a written public hearing the application by Terasen Gas Inc. ("Terasen Gas") for approval of market-based commodity rates for the 2004/05 gas contract year for Rate Schedule 7 – General Interruptible Service, Rate Schedule 10 – Large Volume Interruptible Sales, and Rate Schedules 14 and 14A – Term and Spot Gas Sales; and
- B. By Order No. G-64-04 and attached Reasons for Decision, the Commission approved Rate Schedules 7, 10, 14 and 14A tariffs for 2004/05 and directed Terasen Gas to file several reports related to these rate schedules; and
- C. In a report dated December 14, 2004, Terasen Gas provided a fully allocated cost of service study for the provision of Rates Schedule 14 and 14A service in relation to Gas Management Fee revenue from these rate schedules, and a statement regarding the analysis from Terasen Gas' Internal Audit Services; and
- D. On January 10, 2005, Terasen Gas filed a report regarding the development and cost of a single combined billing option for customers buying their commodity through marketers, and the response from marketers which led Terasen Gas to conclude that the demand for a combined bill is insufficient to warrant further action. A confidential report by Accenture Business Services for Utilities on the cost of providing a single billing option was appended to the Terasen Gas report; and
- E. In a report dated February 9, 2005, Terasen Gas provided an analysis of the cost of core market supply resources that are used to provide gas balancing for transportation customers, and recommendations on a Swing Premium methodology for the Annual Fixed Rate option for the 2005/06 gas contract year; and
- F. On February 23, 2005, Terasen Gas filed its application (the "Application") regarding Rate Schedules 7, 10, 14 and 14A for approval of market-based gas commodity rates for the gas contract year commencing November 1, 2005 and ending October 31, 2006 (the "2005/06 gas contract year"); and

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- G. The Application proposed the current terms of service be maintained for the most part, but also requested approval that Rate Schedule 14 be eliminated for 2005/06, and that the Swing Premium for the Annual Fixed Rate option under Rate Schedule 14A be reduced from \$0.93/GJ to \$0.69/GJ; and
- H. Commission Letter No. L-15-05 invited written comments from interested parties on the Application and on the reports that Terasen Gas had filed, and requested that Terasen Gas provide a copy of the Commission Letter to all current and recent customers under these rate schedules and to all active marketers in the Terasen Gas service area. Commission Letter No. L-21-05 subsequently extended the time period for filing comments; and
- I. On March 28, 2005, Premstar Pacific filed comments on the Application; and
- J. On March 29, 2005, Absolute Energy Inc. filed comments on the Application, and attached letters of comment from three customers to its submission; and
- K. On March 29, 2005, Direct Energy Marketing Limited filed comments on the Application; and
- L. On March 29, 2005, Avista Energy Canada, Ltd. filed comments on the Application; and
- M. On April 6, 2005, Terasen Gas submitted its reply to the comments that were filed regarding the Application; and
- N. The Commission has considered the Application and the written submissions that it has received, and is satisfied that market-based rate arrangements should be approved for the 2005/06 gas contract year, for the reasons that are set out in the Reasons for Decision that are attached as Appendix A to this Order.

NOW THEREFORE the Commission orders as follows for Terasen Gas for the 2005/06 gas contract year:

- 1. The Commission approves the termination of Rate Schedule 14 effective October 31, 2005.
- 2. The Commission approves the Rate Schedule 14A tariff, as set out in the Application except that the Swing Premium under the Annual Fixed Rate option shall continue to be \$0.93 per gigajoule.
- 3. The Commission approves the extension of the Rate Schedule 10 tariff without material changes, as set out in the Application.
- 4. The Commission approves the extension of the Rate Schedule 7 tariff without material changes, as set out in the Application.
- 5. Terasen Gas will file a report for Rate Schedule 14A within 30 days of the end of each month that summarizes gas purchase and sales quantities, and costs and revenue for each rate option for the month.

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6. The Commission will accept, subject to timely filing, Gas Tariff Rate Schedules in accordance with this Order and Reasons for Decision attached as Appendix A.
7. Terasen Gas will provide a copy of this Order and Reasons for Decision to all current customers of Rate Schedules 7, 10, 14 and 14A.

DATED at the City of Vancouver, in the Province of British Columbia, this 22nd day of April 2005.

BY ORDER

Original signed by:

L.F. Kelsey
Commissioner

Attachment

TERASEN GAS INC.
APPLICATION FOR RATE SCHEDULES 7, 10, 14 AND 14A
MARKET-BASED COMMODITY RATES FOR THE 2005/06 GAS CONTRACT YEAR

REASONS FOR DECISION

1.0 INTRODUCTION

Terasen Gas Inc. (“Terasen Gas”, formerly BC Gas Utility Ltd. “BC Gas”) has sold natural gas at market-based commodity rates to its transportation service customers since the early 1990’s. The February 21, 1992 BC Gas Inc. Phase A Rate Design Decision anticipated the sale of surplus or “valley” gas that is available under baseload contracts to interruptible customers. The October 25, 1993 BC Gas Phase B Rate Design Decision approved Rate Schedule 14 as a separate rate schedule for interruptible backstopping sales. The Phase B Decision also approved several bundled or burner-tip schedules, including Rate Schedule 7 for small volume interruptible sales. Thereafter, BC Gas applied annually for approval of market-based commodity rates under Rate Schedules 7 and 10 and more recently 14. The rate options offered have evolved as the natural gas market in the area developed.

In the mid 1990’s, the gas markets in the area became more liquid, with more marketers present and more supply options available. The increased market liquidity meant industrial customers had more supply alternatives available to them, including fixed price contracts. To preserve the market for its surplus Core Market supply, in its 1996 Rate Design Application BC Gas proposed the reconstruction of Rate Schedule 14 as an on-system commodity sales option whereby the Utility could negotiate supply and price terms that would meet the needs of a particular industrial customer. The Commission concluded that the revisions to Rate Schedule 14 were unlikely to result in anti-competitive behaviour or rates that were in any way discriminatory towards customers, and approved the revisions.

By 2000 the ongoing shaping of its gas supply portfolio materially reduced the amount of surplus baseload gas that BC Gas had available for interruptible sales. For 2000/01 the Commission approved significant changes to Rate Schedule 10 to recognize the lower reliability of the supply. The Order also permitted BC Gas to offer firm gas supply under Rate Schedules 7 and 14, with rates designed to recover the cost of the gas that BC Gas purchased to make these sales.

The Commission approved Rate Schedule 14A for the 2002/03 gas year. This rate schedule applies when BC Gas performs the nominating and balancing functions that Shipper Agents typically perform for customers or groups of customers.

When Terasen Gas filed its application for Rate Schedules 7, 10, 14 and 14A for the 2004/05 gas contract year, several gas marketers raised concerns that the proposed Rate Schedule 14 and 14A terms may be an impediment to the development of a competitive gas commodity market in British Columbia, that Core Market customers may be subsidizing the rate offering and that Terasen Gas may be inappropriately using customer information. By Order No. G-37-04 the Commission established a written hearing process to review the application. After the hearing, the Commission issued Order No. G-64-04 and attached Reasons for Decision which stated:

“The Commission is of the view that there may not be a long term future for the continuation of Rate Schedules 14 and 14A, as other participants offer similar supply options to customers. However, discontinuance of these rate schedules would require sufficient notice for customers to make alternative supply arrangements in an orderly manner. The Commission is persuaded that the Application has merit notwithstanding considerable argument by competitors opposing Rate Schedules 14 and 14A. There is also strong support for their continuation.”

The Commission determined that the interests of customers, marketers and Terasen Gas were best served by making Rate Schedules 14 and 14A supply available for the 2004/05 gas year. The Commission approved the continuation of Rate Schedules 7, 10, 14 and 14A with certain relatively small changes to the tariffs. In response to suggestions and concerns that were raised by marketers, the Commission also directed Terasen Gas to file reports on several matters related to Rate Schedules 14 and 14A. These directions resulted in the following filings:

- A report dated December 14, 2004 which provided a fully allocated cost of services study for the provision of Rate Schedule 14 and 14A service in relation to Gas Management Fee revenue from these rate schedules, and a statement regarding the analysis from Terasen Gas' Internal Audit Services;
- A report dated January 10, 2005 regarding the development and cost of a single combined billing option for customers buying their commodity through marketers, and the response from marketers which led Terasen Gas to conclude that the demand for a combined bill is insufficient to warrant further action. A confidential report by Accenture Business Services for Utilities on the cost of providing a single billing option was appended to the letter; and
- A report dated February 9, 2005, which provided an analysis of the cost of core market supply resources that are used to provide gas balancing for transportation customers, and recommendations on a Swing Premium methodology for the 2005/06 gas contract year.

2.0 APPLICATION AND REVIEW PROCESS

On February 23, 2005, Terasen Gas submitted its application for Rate Schedules 7, 10, 14 and 14A for the November 1, 2005 to October 31, 2006 gas contract year (the “Application”). Terasen Gas proposed to maintain the current terms of service for the most part, but sought approval for two significant changes:

- The Application requested that Rate Schedule 14 for service to marketers and customers who do not require gas nominating and balancing service be eliminated for 2005/06; and
- The Application also requested the Swing Premium for the Annual Fixed Rate option under Rate Schedule 14A be reduced from \$0.93/GJ to \$0.69/GJ.

Commission Letter No. L-15-05 invited written comments on the Application and the reports that Terasen Gas had filed, and requested Terasen Gas to provide copies of the Commission Letter to current and former customers under the rate schedules, and to all marketers who are active in the Terasen Gas service area. Letter No. L-21-05 subsequently extended the dates for submitting comments.

The Commission received written comments from PremStar Pacific (“PremStar”), Absolute Energy Inc. (“Absolute”), Direct Energy Marketing Limited (“Direct”) and Avista Energy Canada, Ltd. (“Avista”). On April 6, 2005 Terasen Gas replied to the written comments.

3.0 RATE SCHEDULES 14 AND 14A – TERM AND SPOT GAS SALES

Rate Schedules 14 and 14A provide for the sale of gas to on-system customers and marketers on a firm basis at the interconnection with the Duke Energy Gas Transmission system. A customer may choose from among Annual Fixed Rate, Term Fixed Rate, Monthly Index Rate and Daily Index Rate options. The Daily Index Rate option can be used to supply spot gas to customers who have experienced gas supply failure for some reason, including customers who have been released from their marketer. Each customer must meet Terasen Gas’ credit requirements.

Rate Schedule 14

Terasen Gas continues to believe that Rate Schedule 14 holds value for the marketplace, but considers that changing conditions have diminished the value of the rate schedule. The number of Rate Schedule 14 customers has declined from 200 in 2003/04 to 100 in 2004/05, primarily as a result of one purchasing agent choosing an alternative supply service for the current gas year. After discussing the matter with marketers, Terasen Gas concluded that it is now in the best interest of all concerned to eliminate Rate Schedule 14. Avista, PremStar and Direct supported the elimination of Rate Schedule 14 for 2005/06.

Absolute submitted that Rate Schedule 14 and the other market-based commodity rate schedules should be continued as they provide benefits of price transparency, the comfort of dealing with a well-known utility entity and the option for customers to attain a fixed price. Absolute argued that the rate schedules allow the customers to take better control of their purchasing decisions, and provide clear benchmarking to alternatives in the market. Absolute attached letters from Rate Schedule 14 customers RG Properties Ltd., ALS Canada Ltd. and RPB Hotels and Resorts to its submission. The customers stated that Rate Schedule 14 offers value to customers by providing price transparency, a secure and credit-worthy supplier and the ability to obtain a desired mix of fixed and market index prices.

Terasen Gas replied that the value of Rate Schedule 14 in the marketplace is diminishing, in the face of opposition from some marketers and the growing costs and uncertainty that have resulted. Terasen Gas concluded that the majority of the customer and market benefits could be obtained through maintaining Rate Schedule 14A, and that the additional benefits from retaining Rate Schedule 14 would be marginal.

The Commission notes that identical service options are offered under Rate Schedules 14 and 14A, although the Gas Management Fees under the latter are slightly higher to cover the cost of gas nominating and balancing service. The Commission is persuaded by the submission of Terasen Gas, and considers that customers will lose little in the way of benefits or options, providing Rate Schedule 14A continues to be available. **The Commission approves Terasen Gas' request to eliminate Rate Schedule 14 for 2005/06.**

Rate Schedule 14A Continuation

The Application requested approval for Rate Schedule 14A to continue for 2005/06 in substantially its current form. PremStar supported this request.

Avista and Direct did not support the continuation of the rate schedule on the basis that Terasen Gas competes with marketers to supply gas to transportation customers, and that this utility option is no longer necessary and compromises the development of a competitive market. These marketers felt that Terasen Gas' Key Account Managers have access to information about customers that is not available to other market participants, and are in a preferential position to solicit business. Direct stated that this activity is, in effect, a "Non-Regulated Business" and argued that the Terasen Gas Code of Conduct for Provision of Utility Resources and Services, or a more suitable Code of Conduct, should apply. Direct and Avista submitted that the activity is cross-subsidized, and that Terasen Gas' December 14, 2004 report did not properly identify the fully allocated cost of a service of the activity, as it did not evaluate a stand-alone entity.

Terasen Gas replied that the comments from marketers were similar to those from previous hearings. It believes that customers view the information provided by Rate Schedule 14A as constructive, and not detrimental to the building of competitive markets. Terasen Gas stated that it has no incentive to capture markets for Rate Schedule 14A, and does not consider the activity a Non-Regulated Business. The December 14, 2004 cost of service analysis was consistent with the Commission's directions, and Terasen Gas does not see value in undertaking an analysis based on a stand-alone entity.

The Commission recognizes the concerns raised by Avista and Direct, but is also cognizant of the submissions in favour of these utility supply options that were considered in some depth in 2004 and repeated in the letters from Absolute and its customers. In striving to reach a balance that will foster a competitive market that will provide the best overall results for customers, the Commission is not prepared to eliminate both Rate Schedules 14 and 14A at this time. **The Commission approves the continuation of Rate Schedule 14A for 2005/06.**

Swing Premium

Commission Order No. G-76-04 approved an increase in the Swing Premium for the Annual Fixed Rate option from \$0.84/GJ to \$0.93/GJ for 2004/05. For 2005/06, Terasen Gas proposes to use the same basic methodology that it used to calculate the 2004/05 Swing Premium, except that the maximum annual volatility would be used rather than the maximum winter volatility. Terasen Gas believes that using the maximum annual volatility is appropriate because the Swing Premium is charged for deliveries over the entire year. In addition, no customers elected the Annual Fixed Rate option for the current year, and customers who used the option in previous years indicated that the premium was too high for the option to provide value. Based on the maximum annual volatility and a current gas price forecast, Terasen Gas proposed a Swing Premium of \$0.69/GJ for 2005/06.

Direct expressed the view that Terasen Gas' proposed reduction in the Swing Premium may be an attempt to increase its commercial competitiveness relative to competing offerings, and reacquire customers who were lost to marketers. Terasen Gas responded that only three of the Rate Schedule 14A customers who were on the Annual Fixed Rate option in 2003/04 moved to marketers, and that the proposed change in methodology was a matter of fairness and not motivated by competitive considerations.

Avista raised several concerns about the proposed calculation of the Swing Premium. Terasen Gas responded to the questions about the calculation and estimated that using the current methodology and forecast winter 2005/06 prices would result in a Swing Premium of \$1.05/GJ. Avista also noted that, when access to imbalance inventory is curtailed, monthly balanced groups must nominate correctly or be subject to Unauthorized Overrun ("UOR") charges. As Annual Fixed Rate customers are not subject to UOR and other high end charges, Avista questioned whether the Swing Premium is high enough to cover the cost of peaking supply during such periods of curtailment. Terasen Gas stated that it believes the Swing Premium is sufficient to cover costs associated with sourcing incremental supply or UOR charges, and observed that Annual Fixed Rate customers have less dramatic swings than marketer-managed monthly balanced groups.

In Order No. G-64-04 Reasons for Decision for 2004/05 rates, the Commission considered the risk to the Core Market from Rate Schedules 14 and 14A sales that is due to price risks related to daily swing volumes and also to the cost of providing the midstream storage and other physical resources that are needed to balance day to day variations in load. The Commission went on to state:

"Taking both these considerations together, the proposed Swing Premium of \$0.93 per gigajoule for Annual Fixed Rate sales appears to be reasonable."

The arguments that Terasen Gas makes on the basis of fairness for a change to the methodology that would result in a \$0.69/GJ premium appear to have some merit. Furthermore, the current methodology would result in a \$1.05/GJ Swing Premium for 2005/06. At the same time, the Commission is concerned that the Core Market be adequately compensated for the risks it assumes under the Annual Fixed Rate option, and is not persuaded that these risks have gone down over the past year. **Weighing these considerations, the Commission determines that the Swing Premium should continue at its present level of \$0.93/GJ for 2005/06.**

A matter that is somewhat related to the Swing Premium, is the compensation to the Core Market for the midstream gas resources that are used to balance nominations and deliveries for transportation service customers. In its February 9, 2005 report, Terasen Gas provided information suggesting the cost of these resources could be in the range of \$0.05/GJ to \$0.11/GJ of gas consumed. Terasen Gas submitted that, aside from the Annual Fixed

Rate option, Rate Schedules 14 and 14A customers do not expose the Core Market to price risk and do not use incremental midstream resources beyond those currently available to all transportation customers. Consequently, Terasen Gas felt that the Swing Premium should only apply for the Annual Fixed Rate option.

The Commission accepts Terasen Gas' position that the Swing Premium should only apply for the Annual Fixed Rate option, but notes that transportation service customers in general may not be adequately compensating the Core Market for the use of midstream gas supply resources. As this issue relates to all transportation service customers, a Terasen Gas rate design proceeding would be the appropriate place to address the matter.

Reporting of Rate Schedule 14A Activity

Avista raised several questions about the monthly reports to the Commission regarding Rate Schedule 14A gas purchases and sales. Terasen Gas responded to the questions, noting that the monthly Gas Purchases and Sales Reports are summary reports, and stating that they are not available for review due to some of the confidential information contained within.

The Commission believes that the level of detail in the current monthly reports is satisfactory. The Commission considers that the monthly reports should generally not be considered confidential, and will make them available upon request. An exception to the public disclosure of the reports will typically be information about contracts for physical supply and financial hedging that Terasen Gas files on a periodic basis, as discussed on page 6 of the Application.

Single Combined Billing Option

In its January 10, 2005 report, Terasen Gas presented information about the costs of developing a single combined billing option for customers buying their commodity through marketers, and the response from marketers which led Terasen Gas to conclude that the demand for a combined bill is insufficient to warrant further action.

Direct stated that the Terasen Gas single billing option was costly and inflexible, but requested that further analysis be conducted on the matter. Direct also stated that Terasen Gas should be required to place a marketer's logo and contact information on the bill at a reasonable cost. Terasen Gas responded that in discussion with marketers and customers, it found no evidence that combined billing was a factor impacting any customer's

decision to purchase its commodity through Rate Schedules 14 and 14A rather than a marketer. Terasen Gas concluded the issue of the fairness of joint billing does not warrant further consideration.

The Commission concludes that it should not direct Terasen Gas to take any further action regarding single combined billing at this time. Nevertheless, the Commission encourages Terasen Gas and marketers to engage in constructive discussions about billing options and measures like providing marketer logos and contact information on utility bills that will foster the development of a competitive marketplace.

4.0 RATE SCHEDULE 10 – LARGE VOLUME INTERRUPTIBLE SALES

Rate Schedule 10 provides for the sale of surplus Core Market gas to on-system customers and marketers on an interruptible basis at the interconnection with the Duke Energy Gas Transmission system. A Rate Schedule 10 customer currently selects between a Daily Index option and a Monthly Index option. The Monthly Index rate includes a 3 percent discount in the winter. Terasen Gas requested that Rate Schedule 10 continue without changes for 2005/06. Avista and PremStar supported the Application with respect to Rate Schedule 10.

The Commission considers that the proposed rate options each reasonably represent the competitive market value of the gas. **The Commission approves Rate Schedule 10 for 2005/06 as applied for in the Application.**

5.0 RATE SCHEDULE 7 – GENERAL INTERRUPTIBLE SERVICE

Rate Schedule 7 provides interruptible bundled (burner-tip) service to customers who have the ability to switch to alternate fuels. Although the delivery service is interruptible and can be curtailed in times of capacity constraints on the Terasen Gas system, the supply of the gas commodity is considered to be firm. Currently Rate Schedule 7 service is provided under the Fixed Rate option, where the rate is equivalent to the sum of the Rate Schedule 5 Commodity Cost Recovery Charge, Midstream Cost Recovery Charge and related Gas Cost Riders. Terasen Gas requested that Rate Schedule 7 continue without changes for 2005/06. Avista and PremStar supported the Application with respect to Rate Schedule 7.

The Commission approves Rate Schedule 7 for 2005/06 as applied for in the Application.