

**BRITISH COLUMBIA
UTILITIES COMMISSION**

**ORDER
NUMBER** G-160-06

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

and

Terasen Gas Inc.
Application for Approval of 2007 Revenue Requirements and Delivery Rates

BEFORE: L.F. Kelsey, Commissioner December 14, 2006
L.A. Zaozirny, Commissioner

O R D E R

WHEREAS:

- A. Commission Order No. G-51-03 approved for Terasen Gas Inc. (“Terasen Gas”, “the Company”), the Settlement Agreement for a 2004-2007 Multi-Year Performance-Based Rate Plan (“PBR”); and
- B. The terms of the Settlement Agreement for the 2004-2007 PBR (the “Settlement”) for Terasen Gas included an expanded annual review to provide considerable information on its current and future years’ activities, along with statistics on its quality of service provided and its compliance with the code of conduct and transfer pricing policy. At each annual review, the Company will update its forecast of customer additions, use per account and industrial revenues. The impact on revenues resulting from the updated forecasts will be flowed through in delivery rates in the following year. The Settlement also provides for the flow-through of the impacts of changes approved by the British Columbia Utilities Commission (“BCUC”, “Commission”) orders and exogenous factors; and
- C. The terms of the Settlement also requires Terasen Gas to hold a Mid-Term Assessment Review prior to the end of the third year (2006) of the 2004-2007 PBR. Based on the language included in the Settlement, the Company is of the view that the Annual Review and Mid-Term Assessment Review should be held concurrently; and
- D. On September 15, 2006, Terasen Gas proposed a regulatory timetable for its 2006 Annual Review and Mid-Term Assessment Review that included the filing of the Annual Review and Mid-Term Assessment Review materials by October 16, 2006, an Annual Review and Mid-Term Assessment Review on November 15 and a Commission Decision by December 8, 2006; and
- E. By Order No. G-121-06 the Commission accepted the Company’s proposal and established a regulatory timetable for the 2006 Annual Review and Mid-Term Assessment Review; and
- F. On October 16, 2006, Terasen Gas filed Advance Annual Review materials in accordance with the 2004-2007 PBR Settlement approved by Commission Order No. G-51-03 and the regulatory timetable established by Order No. G-121-06; and

- G. The Advance Annual Review materials address the 2006 actual results, the 2007 forecasts, and the 2006 earnings sharing that are used in setting 2007 rates. The Advance Annual Review materials also includes a request that the Commission approve the amalgamation of Terasen Gas and Terasen Gas (Squamish) Inc. (“Terasen Squamish”, “TGS”), effective January 1, 2007; and
- H. On October 25, 2006, the Commission and Intervenors issued information requests to Terasen Gas related to the advance materials. The Company responded to the information requests on November 6, 2006; and
- I. The Province of British Columbia (“the Province”) issued Order of the Lieutenant Governor in Council (“OIC”) No. 766, dated November 2, 2006 which ordered that Section 53 of the Utilities Commission Act (the “Act”) not apply in respect of Terasen Squamish or Terasen Gas in relation to an amalgamation of those two corporations; and
- J. The Province issued OIC No. 767, dated November 2, 2006, which ordered that effective January 1, 2007, the Vancouver Island Natural Gas Pipeline Special Direction issued to the Commission by Order in Council 1510/95 is amended:
- (a) by repealing the definitions of “Rate Stabilization Facility”, “Rate Stabilization Facility Continuation Agreement”,
 - (b) by repealing sections 3.1(d), 3.3 and 3.8,
 - (c) in section 3.7 by striking out “3.3”, and
 - (d) by repealing Part 5; and
- K. The Province issued OIC No. 768, dated November 2, 2006, with the attached Vancouver Island Natural Gas Pipeline Special Direction No. 3 to the BCUC; and
- L. At the November 15, 2006 Terasen Gas 2006 Annual Review and Mid-Term Assessment Workshop, the Company committed to undertakings regarding the following:
- The applicability of Sections 41, 50, 52, 53 and 54 of the Act to the amalgamation of Terasen Gas and Terasen Squamish.
 - How the Terasen Gas main extension (“MX”) test would be applied to customers in the Terasen Squamish service area on a go-forward basis and whether Terasen Gas would re-run the MX test for current mains.
 - The amortization of Terasen Squamish intangible plant of \$777,000.
 - The treatment of pensionable bonuses.
 - The 2007 return on equity (referred to collectively as “the Undertakings”); and

- M. Terasen Gas submitted responses to the Undertakings on November 20, 2006. The response discussed how the Terasen Gas main extension (“MX”) test would be applied to customers in the Terasen Squamish service area on a go-forward basis, whether Terasen Gas would re-run the MX test for current mains, and requested approval of the following:
- The establishment of a rate base deferral account to record costs related to the amalgamation of TGI and TGS and variances in operation and maintenance expenses, effective January 1, 2007.
 - Cancellation of TGI Tariff Supplement I-3, effective January 1, 2007.
 - Cancellation of the Terasen Squamish Tariff, effective January 1, 2007.
 - The amortization of Terasen Squamish intangible plant of \$777,000 over 10 years.
 - The treatment of pensionable bonuses.
 - The 2007 return on equity; and
- N. The BC Old Age Pensioners Organization et al. and the Ministry of Energy, Mines and Petroleum Resources submitted Comments dated November 24, 2006; and
- O. On December 1, 2006, Terasen Gas provided Reply Comments and applied for approval of its 2007 Revenue Requirements; and
- P. The Commission has reviewed the Application and Comments received.

NOW THEREFORE pursuant to Sections 58, 60 and 61 of the Act, the Commission orders the following for Terasen Gas with Reasons for Decision attached as Appendix A:

1. The Commission accepts Terasen Gas’ opinion regarding the applicability of sections 41, 50, 52, 53 and 54 of the Act to the amalgamation of TGI and TGS. The Commission agrees that Commission approval is not required for the amalgamation of Terasen Gas and Terasen Squamish.
2. The Commission approves the cancellation of TGI Tariff Supplement I-3, effective January 1, 2007.
3. The Commission approves the cancellation of the Terasen Squamish Tariff, effective January 1, 2007.
4. The Commission approves for the amalgamated TGI and TGS the following:
 - A common equity component of 35.01 percent, effective January 1, 2007.
 - A return on common equity of 8.37 percent, effective January 1, 2007.
 - The establishment of a rate base deferral account to record costs related to the Amalgamation and variances in operation and maintenance expenses as it impacts the 2007 Revenue Requirements as applied for in the 2006 Annual Review materials.

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5. The Commission approves the \$0.021/GJ decrease in the Rate Stabilization Adjustment Mechanism rider from the currently approved level of \$0.16/GJ to \$0.145/GJ, effective January 1, 2007.
6. The Commission approves the Earnings Sharing Mechanism rider for customers served under Rate Schedules 1, 1S, 2, 2U, 3, 3U, 4, 5, 6, 7, 22, 22A, 22B, 23, 25 and 27 effective January 1, 2007, ranging from (\$0.108)/GJ for customers served under Rate Schedule 1 to (\$0.018)/GJ for those served under Rate Schedule 22B.
7. The Commission approves the establishment of a rate base deferral account to record the \$10 million payment and the cost of the Social Service Tax appeal, subject to the \$414 million SCP Project maximum capital cost approved by Commission Order No. G-95-00.
8. In accordance with the attached Reasons for Decision, Terasen Gas is directed to file a 2006 Squamish Main Extension Report with the Commission for all TGS main extensions completed and/or in progress in 2006.
9. The Commission approves the amortization of the Terasen Squamish intangible plant of \$777,000 over a 10-year period.
10. The Commission accepts the Terasen Gas submission that the inclusion of non-executive bonuses in pension costs recovered from customers and the exclusion of executive bonuses in pension costs recovered from customers is consistent with Commission's 1992, 1994 and 2003 Decisions.
11. The Commission accepts Terasen Gas' submission that terms of the Settlement prevent it from increasing the Demand-Side Management ("DSM") incentive grants over the \$1.5 million during the period of the Settlement.
12. The Company is instructed to include the Ratepayer Impact Measure test, the Participant Cost test and the percentage of "free riders" for the each program in the 2006 DSM portfolio and in future DSM reports.

DATED at the City of Vancouver, in the Province of British Columbia, this 18th day of December 2006.

BY ORDER

Original signed by:

L.F. Kelsey
Commissioner

Attachment

**TERASEN GAS INC.
APPLICATION FOR APPROVAL OF
2007 REVENUE REQUIREMENTS AND DELIVERY RATES**

REASONS FOR DECISION

1.0 INTRODUCTION

1.1 Regulatory Timetable and Application

On October 16, 2006 Terasen Gas Inc. (“Terasen Gas”, “TGI”) filed Advance Annual Review materials in accordance with the 2004-2007 Multi-Year Performance-Based Rate (“PBR”) Settlement approved by Commission Order No. G-51-03 and the regulatory timetable established by Order No. G-121-06. The Advance Annual Review materials address the 2006 actual results, the 2007 forecasts, and the 2006 earnings sharing that are used in setting 2007 rates. The Advance Annual Review materials also included a request that the British Columbia Utilities Commission (“BCUC”, “Commission”) approve the amalgamation of Terasen Gas and Terasen Gas (Squamish) Inc. (“Terasen Squamish”, “TGS”), effective January 1, 2007.

The Terasen Gas 2006 Annual Review and Mid-Term Assessment Review Workshop (“the Workshop”) was held on November 15, 2006. During the Workshop, Terasen Gas committed to several undertakings for additional information (“the Undertakings”). In the November 20, 2006 responses to the Undertakings, Terasen Gas provided a legal opinion of the applicability of sections 41, 50, 52, 53 and 54 of the Utilities Commission Act (“the Act”) to the amalgamation of TGI and TGS, and requested Commission approval of the following:

- The establishment of a rate base deferral account to record costs related to the amalgamation of TGI and TGS and variances in operation and maintenance expenses, effective January 1, 2007.
- Cancellation of TGI Tariff Supplement I-3, effective January 1, 2007.
- Cancellation of the Terasen Squamish Tariff, effective January 1, 2007.
- How the Terasen Gas main extension (“MX”) test would be applied to customers in the Terasen Squamish service area on a go-forward basis and whether Terasen Gas would re-run the MX test for current mains.
- The amortization of Terasen Squamish intangible plant of \$777,000 over 10 years.
- The treatment of pensionable bonuses.
- The 2007 return on equity.

The BC Old Age Pensioners Organization et al. (“BCOAPO”) and the Ministry of Energy, Mines and Petroleum Resources (“MEMPR”) submitted Comments dated November 24, 2006. On December 1, 2006, Terasen Gas submitted its Reply Comments and Application for 2007 Revenue Requirements and Delivery Rates (“the Application”). The Application requested Commission approval of the following:

- An allowed common equity component of 35.01277 percent.
- A return on equity of 8.37131 percent.
- A 1.97 percent decrease in the applicable rate schedules to eliminate the anticipated revenue surplus after earnings sharing of \$22.3 million, effective January 1, 2007.
- Rate Stabilization Adjustment Mechanism (“RSAM”) rider change from \$0.166/GJ to \$0.145/GJ, effective January 1, 2007.
- Earnings Sharing Mechanism (“ESM”) rider change for customers served under Rate Schedules 1, 1S, 2, 2U, 3, 3U, 4, 5, 6, 7, 22, 22A, 22B, 23, 25 and 27 effective January 1, 2007 ranging from (\$0.108)/GJ for customers served under Rate Schedule 1 to (\$0.018) for those served under Rate Schedule 22B.
- The establishment of a rate base deferral account to record the \$10 million Social Services Tax payment and the cost of appealing the \$36 million Social Service Tax assessment.

1.2 Background

The terms of the Settlement Agreement for the 2004-2007 PBR (the “Settlement”) for Terasen Gas included an expanded annual review to provide considerable information on its current and future years’ activities, along with statistics on its quality of service provided and its compliance with the code of conduct and transfer pricing policy. At each annual review, the Company will update its forecast of customer additions, use per account and industrial revenues. The impact on revenues resulting from the updated forecasts will be flowed through in delivery rates in the following year. The settlement also provides for the flow-through of the impacts of changes approved by Commission Orders and exogenous factors.

The terms of the Settlement also requires Terasen Gas to hold a Mid-Term Assessment Review prior to the end of the third year (2006) of the 2004-2007 PBR. The terms of reference of the Mid-Term Assessment Review are two fold:

- “(1) If any one (or more) particular element of the PBR Plan appears to be inducing unintended outcomes or results in deterioration of service quality, then the parties will jointly address that element and mediate a cure.

- (2) To determine if the results of operating under the PBR Plan have resulted in financial distress and, if so, to mediate a cure.”

2.0 AMALGAMATION OF TERASEN GAS AND TERASEN SQUAMISH

2.1 Amalgamation

Terasen Squamish and the Province of British Columbia (“the Province”) agreed on a process to resolve the financial obligations between the two parties in the summer and fall of 2006. As part of the resolution of the financial obligations, Terasen Gas will amalgamate with Terasen Squamish, effective January 1, 2007 (“the Amalgamation”). On October 5, 2006, a termination agreement was put in place between TGI, Terasen Gas (Vancouver Island) Inc. (“TGVI”), TGS and the Province to amend and terminate certain agreements. In regards to the Amalgamation, the Province issued Order of the Lieutenant Governor in Council (“OIC”) No. 766, OIC No. 767, OIC No. 768 and Vancouver Island Natural Gas Pipeline Special Direction No. 3 (“SD No. 3”) to the British Columbia Utilities Commission (attached to BCUC IR No. 19) on November 2, 2006. As requested in the Undertakings, TGI provided a legal opinion of the applicability of sections 41, 50, 52, 53 and 54 of the Act to the amalgamation of TGI and TGS.

Excerpts of the TGI legal opinion

“At the current time TGS is a subsidiary of TGI, with 100 percent of the shares of TGS being owned by TGI.

Section 41 – Section 41 deals with discontinuance of service by a public utility. In our opinion Section 41 is not applicable to the TGS/TGO amalgamation since there will be no discontinuance of service by the public utility.

Section 50 – Section 50 relates to the issuance of securities. To the best of our knowledge, the amalgamation of TGS and TGI will not give rise to the issuance of securities, and therefore we do not consider Section 50 to be applicable.

Section 52 – Section 52 provides that a public utility must not dispose of property, other than in the ordinary course of business, except with the approval of the Commission. ...As a result of the amalgamation the assets now owned by TGS and TGI will be owned by the one company that continues after the amalgamation. In our opinion there will be no disposition of assets by either TGS or TGI, and Section 52 is not applicable to the TGI/TGS amalgamation.

Section 53 – Section 53 provides that a public utility must not consolidate, amalgamate or merge with another person without specified events occurring. The regulation made by Order in Council 766 orders that Section 53 of the UCA does not apply to TGS or TGI in relation to an amalgamation of those two corporations.

Section 54 – Section 54 relates to the acquisition of control of a public utility...Since the amalgamation of TGI and TGS will be the amalgamation of a public utility with its immediate parent (which is also a public utility), and since ownership and control of the one company that continue will remain Terasen Inc., we are of the opinion that Section 54 is not applicable.”

The Commission accepts Terasen Gas’ opinion regarding the applicability of Sections 41, 50, 52, 53 and 54 of the Act to the amalgamation of TGI and TGS. The Commission agrees that Commission approval is not required for the amalgamation of Terasen Gas and Terasen Squamish.

2.2 Terasen Gas Tariff Supplement I-3

TGI states that “Tariff Supplement I-3 provides for the sale of Gas from TGI to TGS at rates pegged to either TGI Rate Schedule 1 or 3 commodity and midstream charges”. As per Sections 8 and 9 of SD No. 3, TGS will amalgamate with TGI, and TGS’ customers will become TGI Lower Mainland customers effective January 1, 2007. Since the TGS customers will become TGI customers, Tariff Supplement I-3 will no longer have any effect. TGI requests Commission approval to cancel Tariff Supplement I-3, effective January 1, 2007. **The Commission approves the cancellation of TGI Tariff Supplement I-3, effective January 1, 2007.**

2.3 Terasen Squamish Gas Tariff

As a result of the Amalgamation, the area served by TGS will be treated as an area within the TGI Lower Mainland service area and subject to the TGI Tariff.

SD No. 3, Section 8 states:

“In regulating and fixing rates for amalgamated TGI, the commission must apply the Terasen Gas Inc. Tariff and must not apply the Terasen Gas (Squamish) Inc. Gas Tariff.”

SD No. 3, Section 9 states:

“In regulating and fixing rates for amalgamated TGI, the commission must treat the area served by TGS as at December 31, 2006 as being within the “Lower Mainland Service Area” as defined in the General Terms & Conditions of the Terasen Gas Inc. Tariff.”

Since the Terasen Squamish Tariff will no longer apply to TGS customers, TGS has requested approval to cancel the TGS Tariff effective January 1, 2007.

The Commission approves the cancellation of the Terasen Squamish Tariff, effective January 1, 2007.

3.0 2007 REVENUE REQUIREMENTS AND DELIVERY RATES

3.1 Common Equity Component, ROE and Amalgamation Cost Rate Base Deferral Account

As a result of the Amalgamation, Terasen Gas has requested Commission approval of the following:

- An increase in the common equity component of the TGI capital structure from 35 percent to 35.01238 percent.
- A 8.37131 percent return on equity.
- The establishment of a rate base deferral account to record costs related to the Amalgamation and variances in operation and maintenance expenses as it impacts the 2007 Revenue Requirements as applied for in the 2006 Annual Review materials.

The Province issued OIC No. 768, dated November 2, 2006, with the attached SD No. 3 to the Commission, effective January 1, 2007. SD No. 3 includes instructions to the Commission regarding the determination of the common equity component and ROE for the amalgamated TGI and TGS. Other issues addressed in SD No. 3 include the establishment of a rate base deferral account to record costs related to the Amalgamation and the difference between the 2007 allowed operating and maintenance expenses for TGS on stand-alone basis and TGI operating and maintenance expenses under the PBR based on the number of TGS customers at December 31, 2006.

In accordance with Special Direction No. 3, the Commission approves for the amalgamated TGI and TGS the following:

- **A common equity component of 35.01 percent, effective January 1, 2007.** The Commission considers that an equity component rounded to the nearest two decimal places is sufficient for TGI rate setting.
- **A return on common equity of 8.37 percent, effective January 1, 2007. The unrounded ROE of 8.37131 percent is rounded to the nearest two decimal places in accordance with Commission Order No. G-109-01.**

- **The establishment of a rate base deferral account, effective January 1, 2007, to record costs related to the Amalgamation and variances in operation and maintenance expenses as it impacts the 2007 Revenue Requirements as applied for in the 2006 Annual Review materials.**
- **TGI is to inform the Commission if a revision to the proposed 2007 rates is required due to the allowed common equity component and return on common equity.**

3.2 RSAM Rider Change

Due to warmer than normal weather, Terasen Gas has forecasted \$7.99 million (net-of-tax) of RSAM additions at the end of 2006. The balance in the RSAM account at the end of 2006 is projected to be \$34.58 million on a net-of-tax basis. In accordance with the Settlement, the RSAM balance is to be amortized over three years. The net-of-tax RSAM balance to be amortized in 2007 is \$11,527,000; this is equivalent to \$17.2 million on a pre-tax basis, or \$0.145/GJ. Terasen Gas requests Commission approval to decrease the RSAM rider by \$0.021/GJ from the currently approved level of \$0.16/GJ to \$0.145/GJ, effective January 1, 2007.

In accordance with the terms of the Settlement, the Commission approves the \$0.021/GJ decrease in the RSAM rider from the currently approved level of \$0.16/GJ to \$0.145/GJ, effective January 1, 2007.

3.3 ESM Rider Change

Terasen Gas is projecting a 2006 return on equity of 10.098 percent; this is 1.298 percent higher than the 2006 allowed ROE of 8.8 percent. Under the ESM, differences between the actual utility earnings and the authorized level of earnings determined by the Settlement are shared equally between TGI and its customers. The customers' portion of the 2006 earnings surplus is \$8.23 million and the true-up of the prior year's earnings surplus is \$4.507 million. The total earnings sharing surplus to be distributed in 2007 is \$12.74 million. Terasen Gas proposes to distribute the earnings sharing surplus in 2007 via a rider and requests Commission approval to set an ESM rider for customers served under Rate Schedules 1, 1S, 2, 2U, 3, 3U, 4, 5, 6, 7, 22, 22A, 22B, 23, 25 and 27 effective January 1, 2007, ranging from (\$0.108)/GJ for customers served under Rate Schedule 1 to (\$0.018)/GJ for those served under Rate Schedule 22B.

In accordance with the terms of the Settlement, the Commission approves the ESM rider for customers served under Rate Schedules 1, 1S, 2, 2U, 3, 3U, 4, 5, 6, 7, 22, 22A, 22B, 23, 25 and 27 effective January 1, 2007 ranging from (\$0.108)/GJ for customers served under Rate Schedule 1 to (\$0.018)/GJ for those served under Rate Schedule 22B.

3.4 Social Service Tax Appeal Rate Base Deferral Account

The B.C. Ministry of Small Business and Revenue assessed Terasen Gas \$36 million under the Social Services Tax Act related to the construction of the Southern Crossing Pipeline Project (“SCP Project”). TGI is appealing the assessment, but has remitted a \$10 million payment to avoid the accrual of interest. If the appeal is successful, the \$10 million and the accrued interest will be refunded. Terasen Gas seeks approval to record in a rate base deferral account the \$10 million payment and the cost of the appeal, because these costs are imposed by authorities outside of its control.

The Commission accepts TGI’s submission that the Social Services Tax assessment is beyond its control. The Settlement provides for the flow-through of exogenous factors and Commission Order No. G-95-00 approved the maximum capital cost of the SCP Project included in rate base of \$414 million if BC Gas Utility Ltd. (now TGI) did not achieve the provincial sales tax savings that it expected. **The Commission approves the establishment of a rate base deferral account to record the \$10 million payment and the cost of the appeal, subject to the \$414 million SCP Project maximum capital cost approved by Commission Order No. G-95-00.**

4.0 OTHER ISSUES

4.1 Terasen Squamish Contributory MX test Review

The TGI Response to BCUC IR 21.3.1 stated:

“Consistent with current TGI practice, contributing main extensions are reviewed annually to determine if a refund is warranted. The reviews for TGS main extensions, post amalgamation, will be reviewed per the TGI tariff and will use the TGI rates at the time the main is reviewed.”

Furthermore, in response to the Undertakings, TGI stated “The review would be conducted using TGI inputs and if warranted, those developers who paid a contribution under the TGS MX test may see a refund of their contribution.”

The TGI proposal to review contributions paid under the TGS MX Test using the TGI MX test is not consistent with past and current TGI practices. When TGI revised its MX test in 1996 (“the Revised MX test”), contributions paid under the pre-1996 MX test were reviewed using the pre-1996 MX test. Similarly, Commission Order No. G-126-05 approved the TGVI proposal to adopt the TGI MX test with appropriate

revisions to the inputs, commencing January 1, 2006. Since the TGI MX is more stringent than the TGVI MX test, TGVI has not proposed that pre-2006 contributing main extensions be reviewed using the TGI MX test to determine if additional contributions were warranted.

In keeping with past and current practices regarding the review of contributory main extensions, the Commission directs Terasen Gas to review contributions paid under the TGS MX Test using the TGS MX test. Terasen Gas is also directed to file a 2006 Squamish Main Extension Report with the Commission for all TGS main extensions completed or in progress in 2006. The report is to be filed in the second quarter of 2007 and include the following information for each main extension:

- **Work order number**
- **Name**
- **Construction start date**
- **In service date**
- **Estimated and actual direct costs**
- **Main extension test used (TGS/TGI)**
- **Contribution amount**

4.2 Intangible Plant Costs – TGS Conversion Costs

In its response to the Undertakings, TGI elaborated on the \$777,000 of TGS intangible plant costs discussed in the response to BCUC IR No. 1, Question 3.1. The \$777,000 represents the remaining unamortized balance related to the conversion of the TGS propane system to natural gas. TGI stated that it had depreciated the intangible plant at a rate of two percent in prior years, but an amortization rate of one percent was used in the Advance Annual Review materials. In response to a query from Commission Staff, Terasen Gas proposes to amortize the amount included in the intangible plant account over a 10-year period. This revision is reflected in the Application.

The TGI proposal to amortize the intangible plant account over a 10-year period reflects the amortization period typically used by other utilities for intangible plant. **The Commission approves the amortization of the intangible plant account over a 10-year period.**

4.3 Pensionable Bonuses

In the response to BCUC IR No. 1, Question 10.5, TGI stated that non-executive bonuses were included in the 2007 pension expense and executive bonuses were excluded from the 2007 pension expense. During the Workshop, Commission Staff requested clarification of the treatment of non-executive bonuses included in pension costs recovered from customers. Terasen Gas submits that treatment of bonuses for employees, with the exception of executive employees, as a pension cost to be recovered from customers is consistent with the Commission's 1992, 1994 and 2003 Decisions.

In the 1992 BC Gas Inc. [subsequently BC Gas Utility Ltd. and now Terasen Gas Inc.] Revenue Requirements Decision, Section 5.8.6, Executive Pension Plan, page 85, the Commission stated:

“For rate-making purposes the bonus is not to be included in the pension costs to be passed on to customers.”

The BC Gas Utility Ltd. 1994/95 Revenue Requirements Phase 1 Decision, Section 5.4, Executive Compensation, page 15 states:

“A report is to be made later this year. Until then BC Gas will comply with the 1992 Decision that bonuses not be included in determining executive pensions for funding by customers.”

The BC Gas Utility Ltd. (“BC Gas”) 2003 Revenue Requirements Decision, discussed treatment of pension costs. In its 2003 Revenue Requirements Application, BC Gas included a portion of pension expenses, a pension provision on bonuses paid to employees. At BC Gas' request, this provision was later withdrawn from the 2003 Revenue Requirements Application. The 2003 Revenue Requirements Decision, Section 4.4, Pensions, pages 20-21 states:

“Consistent with the Commission's 1992 and 1994 Decisions, the bonus is not to be included in the pension costs to be passed on to customers.”

The Commission accepts the Terasen Gas submission that the inclusion of non-executive bonuses in pension costs recovered from customers and the exclusion of executive bonuses in pension costs recovered from customers is consistent with Commission's 1992, 1994 and 2003 Decisions.

4.4 Conservation Potential Review (“CPR”) and Demand Side Management (“DSM”) Funding

Terasen Gas received comments from BCOAPO and the MEMPR regarding the current and future levels of DSM activities. The MEMPR submits that TGI’s approved funding for DSM is inadequate and should be increased in line with other jurisdictions. BCOAPO submits that it has concerns regarding the benefits of DSM programs and the number of “free riders” (customers that would have undertaken the conservation initiative without an incentive/subsidy from the utility) participating in the programs. BCOAPO also submits that the CPR should be examined in further detail in a subsequent proceeding.

In response to the BCOAPO and the MEMPR submissions, Terasen Gas stated that the terms of the Settlement prevent it from increasing the DSM incentive grants above \$1.5 million during the period of the Settlement. TGI also indicated that it is considering DSM funding increases in the future such as load building programs that are allowed under the Settlement. Regarding the number of “free riders” in DSM programs, Terasen Gas submits that the impact of “free riders” is incorporated into the Total Resource Cost (“TRC”) economic test. TGI also stated that application for additional DSM funding would be subject to a regulatory process involving stakeholders.

The Commission accepts Terasen Gas’ submission that terms of the Settlement prevent it from increasing the DSM incentive grants above \$1.5 million during the period of the Settlement. The TRC test incorporates the impact of “free riders”, but it does not show the impact of DSM programs on customers that do and do not participate in the programs. TGI is instructed to provide the Ratepayer Impact Measure (“RIM”) test, the Participant Cost test and the percentage of “free riders” for the each program in the 2006 DSM portfolio and in future DSM reports.

4.5 Comprehensive Review of System Extension and Customer Connection Policies

In the response to the Undertakings, Terasen Gas committed to conduct a comprehensive review of its system extension and customer connection policies, including the MX test, in 2007, for implementation in 2008. TGI is also of the view that a generic review of these policies for all utilities is required and that the Province’s Energy Policy must be taken into consideration in the evaluation of the extension connection policies. The British Columbia Hydro and Power Authority (“BC Hydro”) has delayed filing its Rate Design Application (the “BC Hydro Application”) until March 15, 2007. The BC Hydro Application is expected to review BC Hydro’s system extension and customer connection policies. Terasen Gas states that the policies of BC Hydro are critical in the

assessment of the most appropriate policies for TGI and that delays in the BC Hydro Application will delay the TGI, system extension and customer connection policies. In its submissions, BCOAPO supported Terasen Gas' proposal to review the MX test in 2007.

The Commission agrees with the Terasen Gas submission that it should conduct a comprehensive review of its system extension and customer connection policies, including the MX test, in 2007. By Commission Order No. G-50-95, a generic public hearing into gas main and electrical extension policies was held on October 18, 1995. The Commission will consider the TGI submission that a generic review of system extension and customer connection policies for all utilities is required. Terasen Gas states that the policies of BC Hydro are critical in the assessment of the most appropriate policies for TGI, but TGI has not substantiated this statement. Delays in the BC Hydro Application should not delay the review of the TGI system extension and customer connection policies. **Accordingly, the Commission directs Terasen Gas to conduct a comprehensive review of its system extension and customer connection policies, including the MX test by the end of the second quarter of 2007, for implementation in 2008.**

4.6 Depreciation and Overheads Capitalization Studies

During the TGVI 2006 Settlement Update proceeding ("the TGVI proceeding"), TGVI stated that it included expenses for a Depreciation study and Overheads Capitalization study in its 2007 Cost of Service. TGVI explained that it has completed a Depreciation study, but has not finalized plans the Overheads Capitalization study. TGVI also explained that both TGVI and TGI are completing both studies. TGVI submitted that if an extension of the existing TGVI settlement is achieved, it will not pursue an application specific to these items for the period of the extension.

In the TGVI proceeding, BCOAPO submitted that the two studies could have significant impacts on residential customers. Since TGI and TGVI are both in their final year of their settlements, it would be inappropriate for the companies to further pursue or implement any changes during the settlement period.

The Commission notes that if an extension of the existing Settlement is achieved and an application specific to the two studies are not pursued the benefits of the two studies may be limited. **The Commission orders that TGI is to suspend further expenditures on these two studies until such time that TGI determines that an extension of the existing Settlement cannot be achieved.**