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**BRITISH COLUMBIA  
UTILITIES COMMISSION**

**ORDER  
NUMBER** C-22-06

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

**and**

**An Application by Terasen Energy Services Inc.  
for Approval of a Certificate of Public Convenience and Necessity  
for a Propane Gas Distribution System for Gateway Lakeview Estates  
and  
Approval of a Rate Tariff and General Terms and Conditions of Service and Deferral Accounts**

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

**CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY**

**WHEREAS:**

- A. On September 6, 2006, Terasen Energy Services Inc. ("TES") applied to the Commission for a Certificate of Public Convenience and Necessity ("CPCN") for the construction of an underground propane gas distribution grid system for a resort community located at Lee Creek, British Columbia (the "Project") and for approval of a proposed Gas Tariff Rate and General Terms and Conditions of Service ("Propane Tariff") and approval of a revenue deficiency deferral account, an outsource billing and meter costs deferral account, and a propane cost deferral account (the "Application"); and
- B. The Project is proposed to serve the new "The Falls" resort community located on the North Shore of Shuswap Lake at Lee Creek, which is being developed by Gateway Lakeview Estates Inc. ("Gateway") and which will include approximately 345 homes and 105 mobile homes upon completion of Phases 1 and 2 (the resort community is herein referred to as "Gateway Lakeview Estates"); and
- C. TES states that there is no existing natural gas service in the area and Gateway has chosen to have an underground propane distribution grid system and as such Gateway Lakeview Estates residents will not have the option of using either oil or bottled propane for their space heating needs; and
- D. The Project consists of a single 30,000 US Gallon tank for bulk propane storage, a vapourization facility, underground gas distribution mains, gas service lines and customer meter sets with a total storage facility and distribution plant capital cost estimate of \$425,000; and
- E. TES and Gateway have entered into a "Gateway/TES Propane Utility Agreement" and Gateway will provide both right-of-way to TES and a refundable capital contribution of \$188,700 plus GST to offset costs; and

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- F. TES is a newly formed wholly-owned subsidiary of Terasen Inc. which is a wholly-owned subsidiary of Kinder Morgan, Inc.; and
- G. TES operates existing propane grid systems at Sun Peaks and Furry Creek and its affiliates Terasen Gas (Whistler) Inc. and Terasen Gas Inc. ("TGI") operate Commission-regulated propane grid systems at Whistler and Revelstoke, respectively; and
- H. TES and TGI have entered into a Shared Service Agreement dated May 19, 2006 that TGI filed on November 2, 2006, which includes a provision that the operation of propane plants and distribution plants, and financial accounting and administration will be contracted to TGI; and
- I. Meter reading and billing services are being negotiated with Corix Multi Utility Services Inc. (formerly Terasen Utility Services Inc.), a former subsidiary of Terasen Inc.; and
- J. TES proposes to finance the Gateway Lakeview Estates rate base with 50 percent debt at an interest rate of 6 percent and 50 percent common equity at a 15 percent rate of return, for an average rate of return on rate base of 10.5 percent; and
- K. By Order No. G-119-06, the Commission established a Written Public Hearing to review the Application, required the publishing of a Notice of Written Public Hearing and indicated that further details regarding the Regulatory Timetable would be provided at a later date; and
- L. On October 23, 2006, TES responded to an Information Request from the Commission; and
- M. By Order No. G-135-06 dated October 31, 2006, the Commission established a Regulatory Timetable for the Written Public Hearing to review the Application; and
- N. The Commission did not receive any written submissions regarding the Application from Intervenor or Interested Parties; and
- O. On November 15, 2006, TES filed its Final Submission on the Application; and
- P. The Commission has considered the Application and the other evidence and submissions, and has determined that a CPCN for the Project is necessary and properly conserves the public interest, and that the Propane Tariff and deferral accounts requested in the Application should be approved subject to certain changes and conditions that are set out in this Order and the Reasons for Decision attached as Appendix A to the Order.

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**NOW THEREFORE** pursuant to Sections 45, 46, 59, 60, 61, and 90 of the Utilities Commission Act (the “Act”), the Commission orders as follows:

1. The Commission grants a Certificate of Public Convenience and Necessity to TES for the construction and operation of an underground propane grid distribution system to serve Gateway Lakeview Estates as set out in the Application, with TES being responsible for obtaining all other necessary licences, permits and agency approvals.
2. TES will furnish the Commission with a copy of the approval from the Provincial Gas Inspector for the propane grid system.
3. TES will file with the Commission a final report upon project completion that provides explanations for any material variances from the schedule and cost estimate in the Application.
4. The Commission approves the revenue requirements methodology as set out in the Application, except that the revenue requirements will be calculated using a capital structure that has a 35 percent equity and a return on equity (“ROE”) that is 0.60 percent higher than the benchmark ROE that the Commission establishes for a low-risk benchmark utility. This methodology will apply for 2006 and 2007, and for subsequent years unless changed by Commission Order.
5. TES will file a recalculated Revenue Requirement Summary as set out in Figure 3.3.1 and include supporting schedules, by January 12, 2007.
6. The Commission approves the Propane Tariff for Gateway Lakeview Estates as set out in Appendix B of the Application effective the date of this Order on a permanent basis, except that the Basic Charge in the General Service Rate that is on page S-2 is approved on an interim basis. TES will review its proposed Basic Charge rate in consideration of the determinations on capital structure and ROE in this Order, and will file by January 12, 2007, an amended page S-2 showing the revised rate that result from these determinations, for Commission approval.
7. The Commission approves the following deferral accounts as proposed in the Application, except that the outstanding balances in each account will not be included in rate base, and instead will receive or be charged interest at the rate that TES uses for the period to calculate the revenue requirements for Gateway Lakeview Estates:
  - Revenue Deficiency Deferral Account
  - Propane Cost Deferral Account
8. The Commission approves the Outsource Billing and Metering Costs Deferral Account as proposed in the Application with the \$10,000 to be amortized over five years.

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9. TES will maintain separate accounts for the propane grid system at Gateway Lakeview Estates and will file Annual Reports and financial statements which summarize the results of utility operations within 60 days of its fiscal year-end, in a form to be developed in consultation with Commission staff. Each Annual Report will be consistent with TGI's reporting of detailed Operations and Maintenance and plant accounts to the Commission.
10. Each Annual Report will include the opening and closing balances in each deferral account, and a schedule showing the transactions each month in the Propane Cost Deferral Account.
11. Pursuant to Section 71 of the Act, TES will file its executed propane supply contract for Gateway Lakeview Estates by January 12, 2007.
12. At least 30 days prior to the beginning of each financial year, and at such other times as TES considers advisable, TES will file a report on the current and projected balances in the Propane Cost Deferral Account, forecast propane sales and costs and Commodity Charge revenue for the following 12 months, and the Commodity Charge that TES proposes to implement at the start of the following 12 month period.
13. TES will provide a copy of this Order and the 24-hour emergency contact number to each current and new customer, and will maintain a copy of its approved Propane Tariff for inspection by customers.

**DATED** at the City of Vancouver, in the Province of British Columbia, this 14<sup>th</sup> day of December 2006.

BY ORDER

*Original signed by:*

L.F. Kelsey  
Commissioner

Attachment

An Application by Terasen Energy Services Inc.  
for Approval of a Certificate of Public Convenience and Necessity  
for a Propane Gas Distribution System for Gateway Lakeview Estates  
and  
Approval of a Rate Tariff and General Terms and Conditions of Service and Deferral Accounts

**REASONS FOR DECISION**

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**1.0 INTRODUCTION**

On September 6, 2006, Terasen Energy Services Inc. (“TES”) applied to the Commission for a Certificate of Public Convenience and Necessity (“CPCN”) for the construction of an underground propane gas distribution grid system for the resort community located at Lee Creek, British Columbia (the “Project”) and for approval of a proposed Gas Tariff Rate and General Terms and Conditions of Service (“Propane Tariff”) and approval of a revenue deficiency deferral account, an outsource billing and meter costs deferral account, and a propane cost deferral account (the “Application”) (Exhibit B-1, pp. 3,4; Exhibit B-2, BCUC IR 1.1; TES Reply Submission).

The Project is proposed to serve the new “The Falls” resort community located on the North Shore of Shuswap Lake at Lee Creek which is being developed by Gateway Lakeview Estates Inc. (“Gateway”) and which will include approximately 345 homes and 105 mobile homes upon completion of Phases 1 and 2 (the resort community is herein referred to as “Gateway Lakeview Estates”).

The Order that accompanies these Reasons for Decision describes the Application, and the regulatory process that the Commission established by Orders No. G-119-06 and G-135-06 for the review of the Application. Only one property owner at Gateway Lakeview Estates registered as an Intervenor in the proceeding, and the Commission did not receive any submissions from Intervenors or Interested Parties.

**2.0 CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY**

TES is a newly formed subsidiary of Terasen Inc. and is carrying on certain activities that previously had been handled by Terasen Utility Services Inc. (“TUS”). Commission Order No. G-52-06 approved the sale by Terasen Inc. of the common shares of TUS, which is now known as Corix Multi Utility Services Inc. (“Corix”) (Exhibit B-1, p. 4).

Appendix A of the Application is a Propane Utility Agreement between TES and Gateway whereby TES will design, build, own and operate a propane storage and distribution system to serve the resort community that is

being developed at Gateway Lakeview Estates. The Application anticipates that Corix will provide meter reading and billing services. TES and Terasen Gas Inc. (“TGI”) have entered into a Shared Services Agreement whereby TGI will provide operations management, operations and maintenance services for the propane and distribution plant, management of propane supply, emergency response, and financial accounting and administration (Exhibit B-1, pp. 7, 14; Exhibit B-2, BCUC IR 4.2, 4.3).

The Application states that a natural gas main extension by TGI is not economically feasible due to the 13 km distance from the existing natural gas service (Exhibit B-1, p. 9; Exhibit B-2, BCUC IR 1.2, 1.3). TES states that its proposed rate for piped propane is slightly higher than the cost of bottled propane at a service station, but less than the estimated cost of delivered propane. TES submits that, when the convenience of piped propane is taken into consideration, propane from its proposed distribution system is comparable in cost to the alternatives.

Although TES does not have staff to carry out the day-to-day operation of a propane utility as noted above, it has an agreement with TGI for the provision of most of these services, including operations and maintenance, propane supply, emergency response and financial accounting. TGI has considerable experience in these areas. The evidence of TES is that the proposed propane grid system will provide convenient service to customers at Gateway Lakeview Estates at a competitive cost. **Based on the evidence and submissions before it, the Commission concludes that a CPCN for TES for Gateway Lakeview Estates is necessary and properly conserves the public interest, and grants a CPCN to TES for the Project.**

The Commission notes that most operational and accounting activities related to Gateway Lakeview Estates will be handled by TGI, while Corix will provide meter reading and billing services. The Commission expects that TGI can competently carry out its responsibilities, and there is no evidence that other TGI customers will be adversely affected. Nevertheless, TGI has propane customers in Revelstoke, and it is not evident how TES Gateway Lakeview Estates, as a separate small utility, adds value, from the perspective of customers in the resort community, as compared to having these customers served directly by TGI, a separate but larger and related utility. As well, TES has stated, but has provided no support other than reference to the Transfer Pricing Policy and the Shared Service Agreement, that this arrangement ensures that TGI customers do not subsidize the resort community customers. Certainly, it is likely to be less efficient and more costly from the Commission’s perspective to regulate a number of small utilities, rather than one larger utility serving the same customers. Going forward, the Commission expects TES and TGI to consider and address this concern when they are developing plans to serve new developments and groups of customers that are in or near TGI’s service area. The Commission is not certain that a proliferation of small, but related utilities, all under the same parent, TI or KMI, is necessarily in the public interest.

### **3.0 CAPITAL STRUCTURE AND RETURN ON EQUITY**

At page 13 of the Application (Exhibit B-1), TES proposes to finance the rate base of the project with a combination of 50 percent debt and 50 percent common equity. TES proposes that the allowed return on common equity (“ROE”) to be collected in rates be 15 percent. In support of its proposal TES submits that the Project is a small project with no existing customers and “...as such is highly dependent upon customers’ addition growth.” TES proposes establishing this return on capital structure until the utility is more established, at which time it may be revisited.

In its Application (Exhibit B-1, p. 10) TES states that the most significant risks for the Project are the timing and certainty of the forecast customer additions and corresponding energy demand, and the risk of construction cost escalation. TES submits that the volume risk arises because most of the developments have not been sold or built and because the volume per customer may be significantly different than expected (Exhibit B-2, IR 10.1).

In response to BCUC Information Request 20.2, TES states that:

“The principal risk the utility faces is the timing of when the customers will attach and whether the revenues generated will cover the total cost of service. There is still the risk the revenue deficiency account or some amount of it may be a stranded unrecoverable cost especially if the utility had to attempt to recover fixed costs through a variable delivery charge” (Exhibit B-2, BCUC IR 20.2).

At page 10 of the Application, TES notes that both the volume risk and the construction cost risk have largely been mitigated:

“The most significant risk for the project is the timing and certainty of the forecast customer additions and corresponding energy demand. This risk has been mitigated in large part through the agreement whereby Gateway makes a refundable contribution of \$188,700 plus G.S.T. that will only be refunded if both the total number of customers reaches 273 and annual propane consumption reaches 734,000 litres. The other significant risk is construction cost escalation, which generally may occur due to unanticipated ground conditions. This has been mitigated under the agreement whereby Gateway will provide the trench and backfill for the distribution mains.”

TES submits that its proposed rate structure, a single monthly basic charge to recover the fixed costs of the system, mitigates the volume per customer risk although it further submits that, if a variable component of the

delivery charge is added to the rate structure, the risk will increase and justify a higher equity proportion on a higher ROE (Exhibit B-2, IR 10.1).

A table filed in the TES response to BCUC IR 9.1, shows that the ROE for other small B.C. utilities ranges between 0.40 and 0.75 percent above that of the benchmark ROE determined under the Commission's ROE automatic adjustment mechanism. The common equity component ranges between 33.5 percent and 36.53 percent, with the exception of Sun Peaks Utilities Co. Ltd., which is substantially different from the others in its financial arrangements and rate setting.

TES is relying on TGI for operational, gas supply and administrative support, and notes in the Application that TES and its affiliates have ample experience operating piped propane systems (Exhibit B-1, p. 9; Exhibit B-2, IR 7.1).

#### Commission Determination

The Commission Panel is not persuaded that an equity proportion and ROE as high as that proposed by TES is justified. Although Gateway Lakeview Estates is a small greenfield utility, TES acknowledges that its risks are mitigated by the refundable contribution to the construction by Gateway, by the supply of trenching and backfilling by Gateway and by the proposed rate structure. The proposed revenue deficiency deferral account also addresses the uncertainty in the forecast of customer additions.

**Therefore the Commission approves a capital structure consisting of 35 percent equity and 65 percent debt, which is within the range of capital structures for the other small utilities. The Commission also approves an ROE for TES that is 60 basis points above that approved for the low-risk benchmark utility, which is equal to the average of the risk premiums allowed for the other small utilities in the table presented in the response to BCUC IR 9.1 (Exhibit B-2). Consequently, as the ROE for a low-risk benchmark utility is set at 8.37 percent for 2007, the 2007 ROE for TES will be 8.97 percent.**

#### **4.0 REVENUE DEFICIENCY DEFERRAL ACCOUNT**

TES requests a revenue deficiency account that would attract AFUDC [Allowance for Funds Used During Construction] at the rate of return on rate base. TES, in its information response, clarifies that the revenue deficiency account would not be included in rate base and the account is forecast to reach a zero balance by 2012 though if there is a balance the deferral account would continue on (Exhibit B-2, BCUC IR 20.1). TES explains



that the purpose of charging AFUDC to the account is to compensate the investors for their investment (debt and equity) in the revenue deficiency account (Exhibit, B-2, BCUC IR 20.3).

The Commission accepts that a revenue deficiency deferral account is appropriate in the special circumstances of Gateway Lakeview Estates and that the utility should be compensated for the carrying cost of the deferral account balance, but is not persuaded that the Revenue Deficiency Deferral Account should earn a return on equity.

**Therefore, the Commission approves a non-rate base Revenue Deficiency Deferral Account that attracts interest.**

## **5.0 OUTSOURCE BILLING AND METERING COSTS DEFERRAL ACCOUNT**

As part of Corix's charges for billing services, TES expects a one time \$10,000 set up fee. TES requests in its Application approval to charge the cost to a deferral account on an after tax basis and to recover the cost in rates as part of its annual cost of service over the following five years (Exhibit B-1, p. 13).

**The Commission approves the Outsource Billing and Metering Costs Deferral Account as proposed in the Application with the \$10,000 to be amortized over five years.**

## **6.0 PROPANE SUPPLY, COMMODITY RATE AND PROPANE COST DEFERRAL ACCOUNT**

TES states that it will submit its propane supply contract to the Commission pursuant to Section 71 of the Utilities Commission Act, following approval of the Application (Exhibit B-2, BCUC IR 1.4, 4.1). Since TES indicates that it intends to commence serving customers at Gateway Lakeview Estates in the winter of 2006/07, the Commission expects that TES has a propane supply arrangement in place. **TES is directed to submit the propane supply contract for Gateway Lakeview Estates to the Commission by December 31, 2006.** In the filing, TES should include justification why the Commission should accept the energy supply contract for filing.

TES requests approval of a separate Commodity Charge of \$0.343 per litre of liquid propane equivalent to recover propane commodity costs, and proposes that the Commodity Charge be reviewed and adjusted periodically. TES proposes to file a report on commodity costs and recovery two to four times per year (Exhibit B-1, pp. 13, 20-22; Appendix B, p. S-2). The proposed Commodity Charge is based on the forecast cost of propane, and is equivalent to a rate of \$13.20 to \$13.40 per gigajoule, depending on the energy content of the propane (Exhibit B-2, BCUC IR 5.1). Variances between the cost of propane and the revenue from the Commodity Charge would be recorded in a Propane Cost Deferral Account, and balances in this account would periodically be paid to, or recovered from, customers over the following 12 months (Exhibit B-2, BCUC IR 3.5. 3.6).

The Commodity Charge, Propane Cost Deferral Account and commodity cost reporting mechanism that TES proposes are reasonably conventional for a small propane utility. However, it is also conventional to recognize the carrying cost or value related to balances in the deferral account. **The Commission approves a Commodity Charge of \$0.343 per litre as a permanent rate effective the date of the Order that accompanies these Reasons for Decision. The Commission approves the Propane Cost Deferral Account as requested in the Application, except that balances in the account will receive or be charged interest at the rate that TES uses for the period to calculate the revenue requirement for Gateway Lakeview Estates.**

**At least 30 days prior to the beginning of each financial year, and at other times as TES considers advisable, TES is directed to file a report on Propane Cost Deferral Account balances, forecast propane sales and costs and Commodity Charge revenue and the Commodity Charge that TES proposes to implement at the start of the following 12 month period.**

## **7.0 ANNUAL REPORT AND UNIFORM SYSTEM OF ACCOUNTS**

TES provided a revised response to BCUC IR 12.5 that states: “TES will file an Annual Report. TES will use the SAP Code of Accounts, rather than the Uniform System of Accounts.”

The use of the SAP Code of Accounts by TES would be a departure from the Commission’s Uniform System of Accounts prescribed for gas utilities. TES did not provide reasons for the departure. The Commission recognizes that TES will procure accounting, operations and gas supply resources from TGI, under a shared services agreement. **Therefore, TES is directed to provide annual reporting to the Commission in a manner consistent with the manner that TGI reports detailed Operations & Maintenance and plant accounts to the Commission.**