



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

and

An Application by Terasen Gas (Vancouver Island) Inc.
for Approval of Long-Term Service Agreements
with British Columbia Hydro and Power Authority

BEFORE: L.A. O'Hara, Commissioner
P.E. Vivian, Commissioner November 15, 2007

O R D E R

WHEREAS:

- A. By letter dated September 28, 2007, Terasen Gas (Vancouver Island) Inc. ("TGVI") applied (the "Application") to the Commission for approval pursuant to Section 61 of the Act for the suite of long-term service agreements comprised of the Transportation Service Agreement ("TSA") between TGVI and British Columbia Hydro and Power Authority ("BC Hydro"), Peaking Agreement ("PA") between TGVI and BC Hydro, and the Capacity Assignment Agreement ("CAA") between TGVI, BC Hydro and Terasen Gas Inc. ("TGI"), (collectively the "Agreements"); and
- B. The Application contained a proposed regulatory schedule on page 6; and
- C. On October 2, 2007, the Commission issued Letter No. L-79-07 requesting Intervenor comments regarding the type of regulatory review process that the Commission would apply to this process; and
- D. By letter dated October 4, 2007, BC Hydro supported the regulatory timetable proposed on page 6 of the Application and indicated that since the Agreements are similar to the current arrangements which have been approved by the Commission, an expedited review process is reasonable and in the interests of customers. The review of the Agreements should be separate from the much broader review of TGVI's 2006-2007 Negotiated Settlement and the 2007 Settlement Update as matters beyond the scope of these Agreements could potentially delay the review process; and
- E. By letter dated October 5, 2007, TGVI indicated that it was in the best interest of customers that the review of the Application be a separate process following the proposed regulatory timetable in the Application. The proposed timetable is compatible with the TGVI 2007 Settlement Update including proposals related to the 2008 customer rates impacted by the Agreements; and
- F. On October 11, 2007, the Commission issued Order No. G-123-07 that established a written review process and the Regulatory Timetable; and

**BRITISH COLUMBIA
UTILITIES COMMISSION**

**ORDER
NUMBER** G-139-07

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- G. BC Hydro, the B.C. Old Age Pensioners' Organization *et al.* and the Vancouver Island Gas Joint Venture intervened in the proceeding. The Ministry of Energy, Mines and Petroleum Resources registered as an Interested Party; and
- H. The Commission has considered the Application, the interrogatory responses, the positions taken by the Applicant and Intervenor in the review of the Application and has concluded that the Agreements are generally in the public interest and should be approved subject to certain conditions, for the Reasons for Decision that are Appendix A to this Order.

NOW THEREFORE, the Commission orders that the Agreements be approved pursuant to Section 61 effective January 1, 2008 subject to the parties filing by December 15, 2007 for Commission approval the following:

- A fully executed and acceptable amendment to the PA that deletes subsection 3.1(3) from the agreement;
- A fully executed and acceptable amendment to the Wheeling Agreement that reduces the amount of Coastal Transmission System (CTS) wheeling capacity provided to TGVI, and the payments by TGVI, to amounts that correspond to the net amount of CTS wheeling capacity that TGVI requires in addition to the wheeling capacity it receives under the CAA.

DATED at the City of Vancouver, in the Province of British Columbia, this 15th day of November 2007.

BY ORDER

Original signed by

L.A. O'Hara
Commissioner

Attachment

AN APPLICATION BY TERASEN GAS (VANCOUVER ISLAND) INC.
FOR THE APPROVAL OF LONG-TERM SERVICE AGREEMENTS
WITH BRITISH COLUMBIA HYDRO AND POWER AUTHORITY

REASONS FOR DECISION

1.0 INTRODUCTION

On September 28, 2007 Terasen Gas (Vancouver Island) Inc. (“TGVI”) applied (the “Application”) to the Commission for approval pursuant to Section 61 of the Utilities Commission Act (the “Act”) for the suite of long-term service agreements comprised of the Transportation Service Agreement (“TSA”) between TGVI and British Columbia Hydro and Power Authority (“BC Hydro”), the Peaking Agreement (“PA”) between TGVI and BC Hydro, and the Capacity Assignment Agreement (“CAA”) among TGVI, BC Hydro and Terasen Gas Inc. (“TGI”), (collectively, the “Agreements”).

After approval, the Agreements will establish the arrangements under which TGVI will provide gas transportation service to BC Hydro for the Island Cogeneration Plant (“ICP”) on Vancouver Island. These Agreements will replace the generally similar short-term agreements dated October 20, 2005 and approved by the Commission pursuant to Order No. G-113-05.

The existing agreements have been in effect since November 1, 2005 and their initial term expires on December 31, 2007. BC Hydro exercised its option to extend the existing agreements for 2008 and, if the Agreements are not approved by the Commission, the existing agreements will continue in effect until December 31, 2008 (Exhibit B-2, BCUC IR 1.2).

By Letter No. L-79-07, the Commission requested comments regarding the regulatory process for the review of the Application, and by Order No. G-123-07 established a written hearing process and Regulatory Timetable. Submissions in the review process concluded with the filing of TGVI Reply Comments on November 2, 2007.

2.0 APPLICATION

The TSA, PA and CAA are described in detail in Sections 2, 3 and 4 of the Application, respectively (Exhibit B-1). TGVI also provided a comparison of the terms of each of the Agreements to the terms of the corresponding existing agreement (Exhibit B-8, BCUC IR 5.1).

2.1 Transportation Service Agreement (“TSA”)

Under the terms of the TSA, TGVI will provide BC Hydro long-term firm transportation service for ICP. The initial term of the TSA is from January 1, 2008 to April 12, 2022, matching the remaining period of the initial term of BC Hydro’s electricity purchase agreement with ICP. The agreement also provides BC Hydro the flexibility to terminate the agreement after November 1, 2015 subject to a termination payment that is intended to ensure that the remaining customers are not impacted relative to where they would be if ICP had not been a customer on the system.

The principal terms are as follows:

- The initial Contract Demand is 45 TJ/d and can be adjusted to a minimum of 40 TJ/d or maximum of 50 TJ/d upon BC Hydro giving 12 months notice. Any increases are subject to capacity being available.
- The initial term commences on January 1, 2008 and expires April 12, 2022. BC Hydro can elect to extend for renewal terms of one or more years by providing two years notice and subject to a maximum term of 35 years. If expansion facilities are required for any renewal period, TGVI can require a minimum renewal term of up to 10 years.
- BC Hydro has the following early termination rights, subject to a termination payment if expansion facilities have been added:
 - If TGVI gives BC Hydro an expansion notice, BC Hydro can elect to reduce its Contract Demand or increase the maximum allowed curtailment under the PA to allow deferral of an expansion or can terminate the TSA, either action being effective on the date the expansion facility would have otherwise been required to be in-service.
 - BC Hydro can elect to terminate on or after November 1, 2015 upon giving two years prior notice.
- If BC Hydro elects to terminate prior to the expiry date, it may be required to make a termination payment based on the incremental revenue requirement associated with any expansion facilities. The determination of the termination payment will be based on the period between the termination date and when the facilities would have been required to be put in service to meet remaining demands on the system or the expiry date which ever is earlier (the “Excess Capacity Period”). For the purposes of the termination rights and the determination of a termination payment, expansion facilities are those facilities added to the TGVI system after the commencement of the TSA but exclude the proposed Mt. Hayes Storage Facility and associated system facilities.
- BC Hydro maintains the right to alternate delivery points in the case of an Outage Event, and also has the right to use a portion of its capacity to transport natural gas to the Elk Falls Mill in the case where ICP is not operating as a result of a dispatch event. This clause recognizes the fact that ICP provides steam to the Elk Falls Mill as well as electricity to BC Hydro and that if the ICP is not operating due to power market conditions, the mill’s gas requirements may increase to meet its steam requirements.
- The Demand Toll and Interruptible Tolls will be as determined from time to time by the Commission.

2.2 Peaking Agreement (“PA”)

The term of the PA matches that of the TSA and provides TGVI a right to call back a portion of BC Hydro's firm capacity under the TSA if it requires it to meet the remaining firm demands on its system. The availability of the capacity right is based on ICP's fuel switching capability. The terms of this agreement are substantially the same as the current arrangements other than under this long-term arrangement, TGVI has agreed to a Capacity Right Payment that is applicable whether or not the Capacity Right is used in any winter period. In addition, if the proposed Mt. Hayes LNG Storage Facility proceeds, TGVI must make reasonable efforts to use gas available to it from the Mt. Hayes LNG Storage Facility to minimize the exercise of the Capacity Right.

The principal terms of the agreement are as follows:

- TGVI holds a Capacity Right giving it limited access to a portion of BC Hydro's firm capacity under the TSA during each winter period. The maximum annual rights are limited to capacity equivalent of 100 TJ in aggregate (53 hrs) over any winter, based on the amount of distillate storage available to BC Hydro for fuel switching.
- TGVI must curtail all interruptible transportation service prior to calling on the Capacity Right and make reasonable efforts to use gas available to it from the Mt. Hayes LNG Storage Facility to minimize the exercise of the Capacity Right.
- BC Hydro has the right to increase the annual curtailment amount, at its risk, to 150 TJ if doing so would allow deferral of an expansion facility for at least one year. The parties have also agreed that this 150 TJ will apply for the winter 2010/11 as a bridging resource to ensure TGVI has enough system capacity through that winter.
- TGVI will make a Capacity Right Payment each month based on the sum of a demand charge credit and a distillate carrying charge whether or not it exercises its Capacity Right. The estimated annual cost of the Capacity Right Payment based on current costs is \$250,000.
- TGVI maintains its Intraday Right giving it limited rights to BC Hydro's firm capacity and gas commodity if circumstances require. TGVI will make capacity and commodity payments if and when the Intraday Right is called.

2.3 Capacity Assignment Agreement

TGI provides transportation service on its Coastal Transmission System (the "CTS") to TGVI from Huntington to the beginning of the TGVI System at Eagle Mountain through the TGVI Wheeling Agreement. Currently the CTS capacity TGVI holds under the Wheeling Agreement is less than the take-away capacity at Eagle Mountain. BC Hydro holds CTS capacity under its Bypass Transportation Agreement ("BTA") with TGI that is greater than its requirement to serve Burrard Thermal. As part of this long-term arrangement, TGI has agreed to allow BC Hydro to assign to TGVI a portion of its CTS capacity matching its contract demand under the TSA.

The principal terms of the agreement are as follows:

- TGVI takes assignment of a quantity of BC Hydro's BTA capacity equal to the BC Hydro Contract Demand under the TSA.
- TGI increases the minimum delivery pressure under the Wheeling Agreement to Eagle Mountain to 300 psig.
- BC Hydro, at its election, can allow TGI to reduce deliveries to Burrard Thermal or to Eagle Mountain for ICP if required to maintain sufficient delivery pressure at Eagle Mountain to meet the remaining firm requirements on the TGVI System.
- BC Hydro is providing the assigned capacity at no cost to TGVI and will continue to be responsible for payments to TGI for the assigned capacity under the BTA.
- TGVI will not apply for Demand Tolls under the TSA that include any allocation of any CTS wheeling costs.
- The CAA will terminate the earlier of the expiry of the TSA, the BTA, or with two years prior formal notice from BC Hydro.

The CAA will result in TGVI initially holding more CTS capacity than it requires to match the takeaway capacity at Eagle Mountain. However, TGVI believes that the benefits that the Agreements bring by way of long-term revenue certainty under the BC Hydro TSA significantly outweigh the potential for underutilized wheeling capacity and the associated costs to the remaining TGVI customers. In addition, TGVI and TGI are currently investigating options to reduce the capacity and associated potential wheeling costs under the Wheeling Agreement as part of the renewal of the agreement in 2011. This might also allow TGI to defer future expansions of the CTS.

If the BTA is terminated prior to the end of the term of the TSA, TGVI will contract directly with TGI for the required wheeling capacity by requesting an expansion of its Wheeling Agreement capacity. Under this scenario TGI will have sufficient capacity to be able to provide the service without expansion to its system as it would no longer be required to provide firm service to Burrard Thermal. In the unlikely scenario that BC Hydro terminates the CAA without terminating the BTA or the TSA, TGI may require an expansion on its system and will have two years to install any facilities needed.

2.4 Ability of TGVI to Provide Firm Service

The Application discusses two scenarios whereby TGVI will provide the transmission system capacity needed to provide firm service to BC Hydro under the TSA. Under either scenario, the PA provides TGVI with a Capacity Right that is based on ICP's fuel switching capacity. If the Mt. Hayes Liquefied Natural Gas ("LNG") Storage Facility (the "Mt. Hayes LNG Storage Facility") is approved, TGVI will not require significant expansion of its transmission system throughout the life of the Agreements. If the Mt. Hayes LNG Storage Facility is not approved, system requirements will be met through compression and pipeline additions commencing in 2011 (Exhibit B-1).

3.0 SUBMISSIONS OF PARTICIPANTS

BC Hydro, the B.C. Old Age Pensioners' Organization *et al.* ("BCOAPO") and the Vancouver Island Gas Joint Venture ("VIGJV") intervened in the proceeding. The Ministry of Energy, Mines and Petroleum Resources registered as an Interested Party.

BC Hydro in its October 1, 2007 Submission states that it relies on ICP for dependable capacity and firm energy, and that it believes that assurance of gas delivery to ICP can only be achieved through a long-term service agreement. BC Hydro supports the Application for approval of the Agreements (Exhibit C2-2).

The BCOAPO in its submission dated October 26, 2007, states that its clients are ratepayers of both TGVI and BC Hydro, and that their interests call for a balanced set of arrangements. BCOAPO recognizes the Agreements are a negotiated package, and states it is satisfied that the outcome, while imperfect, significantly improves the deployment of the available facilities and provides a measure of stability that is beneficial.

In its Submission, BCOAPO discusses the excess capacity on the TGI CTS that TGVI receives under the CAA. BCOAPO considers this is a short-run problem as the current Wheeling Agreement between TGVI and TGI which also provides TGVI with CTS capacity expires in 2011. While TGVI could elect to extend the Wheeling Agreement, BCOAPO notes that TGI and TGVI are open to reviewing this matter in the future. Furthermore, the result of reduction in CTS capacity and charges under the Wheeling Agreement is "zero sum" as the impacts on the revenue requirements of TGI and TGVI would offset each other.

BCOAPO also notes that BC Hydro could terminate the CAA without terminating the TSA or the BTA, and expresses concern that TGI could be required to expand its facilities to meet a shortfall in CTS capacity to meet all requirements. Nevertheless, BCOAPO accepts TGVI's characterization of this possibility as remote.

In conclusion, BCOAPO submits that the Agreements are a reasonably measured and balanced treatment of the utilities and their ratepayers, and that the Agreements should be approved.

The VIGJV in its Submission dated October 29, 2007 does not explicitly support or oppose approval of the Agreements, but raises a number of issues and concerns. It refers to Section 59(2) of the Act, which states:

“A public utility must not

- (a) as to rate of service, subject any person or locality, or a particular description of traffic, to an undue prejudice or disadvantage, or
- (b) extend to any person a form of agreement, a rule or a facility or privilege, unless the agreement, rule, facility or privilege is regularly and uniformly extended to all persons under substantially similar circumstances and conditions for service of the same description.”

The VIGJV submits that the proposed transportation service arrangements for BC Hydro do not comply with the requirements of this Section of the Act, compared to the terms of service for TGI related to the Mt. Hayes LNG Storage Facility. In its Reply Submission dated November 5, 2007, TGVI responds that the VIGJV submissions repeats its comments with respect to the TGVI/TGI Storage and Delivery Agreement in the Mt. Hayes LNG Storage Facility proceeding, and have little to do with the proposed Agreement with BC Hydro. Furthermore TGVI argues that the VIGJV submissions are not correct.

The VIGJV also submits that the Agreements are not consistent with the contractual obligations of TGVI under the TGVI transportation service agreement with the VIGJV, or with the Special Direction to the Commission under Order in Council 1510/95. TGVI replies that entering into the long-term agreements with BC Hydro will not cause a breach of its transportation service agreement, or be contrary to any provision of the Special Direction.

In addition, the VIGJV expresses concern about the quality of firm service provided to BC Hydro, and about the Capacity Right to curtail firm service to BC Hydro that TGVI obtains under the PA. The VIGJV submits that the “...treatment of BC Hydro is unduly prejudicial to the interests of BC Hydro and its customers and is unduly preferential to TGVI's affiliate.” TGVI replies that the PA and the Capacity Right are part of a negotiated

package of arrangements that includes the TSA and the CAA, and that BC Hydro supports the approval of these Agreements.

In its Reply Submission, TGVI summarized its position as follows:

“In summary, TGVI and BC Hydro have negotiated long-term arrangements under which TGVI will provide service to the ICP. The arrangements are supported by BC Hydro. BCOAPO submits that the long-term agreements should be approved by the Commission. The VIGJV has made submissions that have little, if anything, to do with the long-term agreements and also appears to argue that TGVI should be required to invest in additional and unnecessary facilities rather than have available the Capacity Right that has been negotiated with BC Hydro. TGVI submits that the arguments of the VIGJV are without merit and provide no basis for denial of the application. TGVI submits that the long-term agreements are in the interests of all customers of TGVI and each of the agreements should be approved by the Commission.”

4.0 COMMISSION DETERMINATION

The TSA, PA and CAA are long-term agreements that have been negotiated by the parties to replace similar short-term agreements that are currently in effect, in order to provide gas delivery for BC Hydro to the ICP. The terms of long-term Agreements are generally similar to those of the existing agreements, but differ in a number of material ways (Exhibit B-2, BCUC IR 5.1) The Agreements have been negotiated as a package, and it is to be expected that the parties made certain trade-offs and concessions in order to achieve agreement.

Approval of the Agreements is supported by the submissions of all parties in the proceeding except for the VIGJV. The Commission generally agrees with TGVI that the concerns and issues raised by the VIGJV do not provide a basis for denial of the Application. Furthermore, the Demand Toll and the Interruptible Tolls under the TSA are not at issue in this proceeding, as they will be as determined from time to time by the Commission in other proceedings.

While the Agreements are the result of bilateral negotiations, they are long-term agreements and the Commission believes that it has a responsibility to carefully evaluate whether terms of the Agreements have the potential to cause problems in the future. After reviewing the evidence and submissions, the Commission has concerns in the following two areas.

Restrictions on Use of Capacity Right

TGVI will pay a Capacity Right Payment as a demand charge of approximately \$250,000 per year for the Capacity Right (Exhibit B-1; Exhibit B-2, BCUC IR 3.9). TGVI was unable to identify other similar arrangements where the customer is provided with a credit for capacity curtailments in instances where capacity is not actually curtailed (Exhibit B-2, BCUC IRs 3.4, 3.5). TGVI has to date not had to exercise the Capacity Right or any curtailment rights under the existing or previous Peaking Arrangements with BC Hydro. This may in part be explained by occasions when the ICP was not operating during cold weather for other reasons (Exhibit B-2, BCUC IR 3.7). This situation is likely to prevail in a number of future years, particularly if the Mt. Hayes LNG Storage Facility goes ahead (Exhibit B-2, BCUC IR 3.8).

Section 3.1 of the PA describes the conditions under which TGVI may call on the Capacity Right, and states:

- “3.1 Capacity Right. Subject to the provisions of this Agreement TGVI shall have the right (the “Capacity Right”) to use the Firm Capacity up to the quantity specified in section 3.2. The Capacity Right is subject to the following conditions:
- (1) TGVI requires the use of all or a portion of the Firm Capacity for the purpose of supplying gas to its Core Market customers;
 - (2) TGVI has curtailed all interruptible Transportation Service and intends to use all the TGVI System capacity available to it after provision of Firm Transportation Service to its other Shippers. For clarity, provision of Firm Transportation Service to other Shippers will be on the basis of the Contract Demand which is specified for a Shipper in its Service Agreements; and
 - (3) If the Mt. Hayes LNG Storage Facility is in service, TGVI has made reasonable efforts to use gas available to it from the Mt. Hayes LNG Storage Facility to minimise the exercise by TGVI of its Capacity Right under this Agreement.”

TGVI states that subsection 3.1(3), in the event that the Mt. Hayes LNG Storage Facility goes ahead, is an obligation it will need to take into consideration for both its portfolio planning on an annual basis and on day-to-day decisions during the winter period (Exhibit B-2, BCUC IR 3.2). TGVI explains the obligation as follows:

“On an annual basis, TGVI will determine the amount of storage capacity it reserves for its own use based on an expectation that its requirement for the Capacity Right over the applicable winter period is minimised. In other words TGVI cannot elect to reduce the amount of storage capacity it reserves for its own use if that decision is expected to result in an increase in its exercise of the Capacity Right.

However, from day to day during the winter period, TGVI decision to use its storage inventory and versus the Capacity Right will depend largely when during the winter period the peaking demand is being experienced and TGVI's forecast of its ability to meet requirements for the remaining winter period. As a result there may be occasions when TGVI will be exercising its Capacity Right before it has used all of its Mt. Hayes LNG inventory. This would likely only occur in situations where colder than normal weather events occur early in the heating season when there is greater uncertainty related to the requirements for the remaining winter period."

It is apparent that this obligation would seriously constrain TGVI's portfolio planning, particularly its ability to determine that it is likely to need less than the full amount of LNG capacity and deliverability available to it and that it can contract to provide the excess LNG supply to TGI or others. This would materially reduce TGVI's ability to optimize the use of a LNG facility and the revenue and other benefits derived from it.

When considering whether the terms of the Agreements should unreasonably constrain TGVI's use of its LNG capacity, the Commission notes that the costs of the Mt. Hayes LNG Storage Facility are excluded from the termination payment calculation in the event that BC Hydro terminates the TSA (Exhibit B-2, BCUC IR 2.3).

Particularly when TGVI pays a fixed demand charge for the Capacity Right, the Commission believes it is unreasonable for TGVI to be constrained in this way from the use of the Capacity Right. In this situation, the Commission concludes that subsection 3.1(3) of the PA unreasonably constrains TGVI's use of the Capacity Right and consequently its use of the Mt. Hayes LNG Storage Facility in the event that facility goes ahead, and concludes that any approval of the Agreements should require that the subsection be removed from the PA.

Excess Wheeling Capacity on CTS

As identified by BCOAPO, the CTS wheeling capacity that TGVI obtains through the CAA together with the CTS wheeling capacity under the Wheeling Agreement with TGI means that TGVI will hold a considerable excess of wheeling capacity. Although TGVI submits that the CAA wheeling capacity comes without additional cost, in 2008 the payment by TGVI to TGI under the Wheeling Agreement for the amount of redundant capacity is estimated at \$975,000 (Exhibit B-2, BCUC IRs 4.1, 4.2).

TGVI states that it and TGI intends to review TGVI's long-term requirement across the CTS once the Agreements are approved and it is known whether the LNG Storage Facility will proceed. TGVI states that it would not be unreasonable to amend the Wheeling Agreement, but that the parties believe it is preferable to do so after there is more certainty about TGVI's long-term requirements for wheeling capacity across the CTS.

The Commission is concerned that the Agreements cause TGVI to put itself into the position of being over contracted for CTS wheeling service. This serves no useful purpose, and could potentially result in an indicated requirement for TGI to expand the CTS sooner than it would otherwise need to. The Commission recognizes the good intentions of TGVI and TGI to resolve this matter at a future date based on more complete information, but sees no sufficient justification to delay the resolution of the matter in the content of the current Wheeling Agreement.

Therefore, the Commission concludes that any approval of the Agreements should be conditional on the amendment of the Wheeling Agreement so that the amount of CTS wheeling capacity provided by TGI to TGVI, and the payment for this capacity, corresponds to the net amount of CTS wheeling capacity that TGVI requires in addition to the amount provided by the CAA.

In summary, the Commission concludes that the Agreements are generally a balanced and reasonable package of arrangements that provide BC Hydro with the long-term service it needs and improves TGVI's long-term revenue certainty, and which are generally in the public interest. However, for the foregoing reasons, the Commission believes that certain conditions to approval of the Agreements are necessary. **Therefore, the Commission approves the TSA, PA and CAA effective January 1, 2008, subject to the parties filing by December 15, 2007 for Commission approval the following:**

- **A fully executed and acceptable amendment to the PA that deletes subsection 3.1(3) from the agreement;**
- **A fully executed and acceptable amendment to the Wheeling Agreement that reduces the amount of CTS wheeling capacity provided to TGVI, and the payments by TGVI, to amounts that correspond to the net amount of CTS wheeling capacity that TGVI requires in addition to the wheeling capacity it receives under the CAA.**