



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

and

An Application by Centra Gas British Columbia Inc.
for a Certificate of Public Convenience and Necessity
to Extend its Natural Gas Distribution System to Sooke, B.C.

BEFORE: P. Ostergaard, Chair)
K.L. Hall, Commissioner) December 30, 2002
P.G. Bradley, Commissioner)

CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY

WHEREAS:

- A. On February 11, 2002, Centra Gas British Columbia Inc. ("Centra Gas") applied for a Certificate of Public Convenience and Necessity ("CPCN") to provide natural gas service to the District of Sooke, B.C.; and
- B. On April 5, 2002, Centra Gas requested approval to withdraw the CPCN application, as the Sooke School Board had voted against conversion of Sooke schools to natural gas. Centra Gas anticipated that it would refile the application if conditions changed sufficiently to make the project feasible; and
- C. On November 7, 2002, Centra Gas again applied for a CPCN for the Sooke Distribution Extension Project (the "Application") to provide natural gas service to Sooke by constructing an intermediate pressure pipeline from Langford to Sooke (the "Pipeline"), and installing certain distribution mains in Sooke in 2003. Centra Gas proposes to start construction of the Pipeline by March 2003, so that the system extension will be in service by September 2003. The extension work in 2003 is estimated to cost \$4,261,881; and
- D. Centra Gas has entered into a Construction Terms and Conditions Agreement, dated June 26, 2000 and amendments dated November 30, 2001 and August 6, 2002, with BC Transportation Financing Authority ("BCTFA") and Capital Regional District Parks ("CRD Parks"), and has proposed a third amendment that was approved by the Capital Regional District Board on December 11, 2002; and
- E. The Construction Terms and Conditions Agreement sets out terms and conditions for installation of the Pipeline in the route that was previously the Canadian National Railway right-of-way, and which is now owned by BCTFA and leased to CRD Parks (the "Galloping Goose right-of-way"). The Galloping Goose right-of-way is reserved by the Province of British Columbia for future transportation needs, has been designated by the BCTFA as a utility corridor, and a portion of the right-of-way is used for the Galloping Goose Regional Trail; and
- F. On December 13, 2002, Centra Gas responded to an Information Request from Commission staff and filed a draft Natural Gas Pipeline Corridor License agreement with BCTFA for the use of the Galloping Goose right-of-way for 20 years; and

G. The Commission has reviewed the Application and the other submissions, and considers that the Application should be approved for the reasons set out in the Reasons for Decision that are attached as Appendix A to this Order.

NOW THEREFORE the Commission orders as follows:

1. The Commission approves for Centra Gas a CPCN for the Sooke Distribution Extension Project as described in the Application, subject to Centra Gas filing, by February 28, 2003 and in a form that is acceptable to the Commission, an agreement with BCTFA and CRD Parks or other documentation that provides Centra Gas with the right to use the Galloping Goose right-of-way for the Pipeline over the long term under reasonable terms and conditions and usage fees.
2. Centra Gas will file project progress reports within 30 days of the end of each month, and a comprehensive final report. In these reports, Centra Gas will be expected to justify any cost overruns relative to the estimate of \$4,261,811 in the Application.
3. Centra Gas will file annual reports that compare actual customer and load additions for the Sooke distribution extension to the forecast in the Application.
4. The Commission approves Centra Gas' request to record Allowance for Funds Used During Construction at a rate equivalent to its weighted average cost of capital.

DATED at the City of Vancouver, in the Province of British Columbia, this 30th day of December 2002.

BY ORDER

Original signed by:

Peter Ostergaard
Chair

Attachment

**An Application by Centra Gas British Columbia Inc.
for a Certificate of Public Convenience and Necessity
to Extend its Natural Gas Distribution System to Sooke, B.C.**

REASONS FOR DECISION

1. INTRODUCTION

On November 7, 2002, Centra Gas British Columbia Inc. (“Centra Gas”, the “Company”) applied to the British Columbia Utilities Commission (the “Commission”) pursuant to Sections 45 and 46 of the Utilities Commission Act for a Certificate of Public Convenience and Necessity (“CPCN”) to extend its natural gas distribution system to Sooke, B.C. (the “Application”). The extension includes 24.5 kilometres of 114.3 mm (4.5”) steel intermediate pressure pipeline from a regulator station near Jacklin and Kelly Roads in Langford, to Sooke (the “Pipeline”). Centra Gas proposes to build the Pipeline in the first half of 2003. Also, approximately six kilometres of distribution mains will be installed along Highway 14 through the commercial core of Sooke, and a further four kilometres will be built on municipal roadways, to be in service by September 2003. An additional 28 kilometres of distribution mains will be required over the following four years to connect additional residential and commercial customers.

The Application requests approval for the facilities that are to be installed in 2003. The \$4,261,811 cost estimate is based on updated information, and has been adjusted to reflect workspace constraints when working in the right-of-way. The estimate for the Pipeline and the distribution mains include a 4.35 percent contingency allowance, which Centra Gas considers to be adequate considering the amount of investigation it has done on the project and the proposed route.

Centra Gas states that all significant regulatory approvals need to be completed by the end of 2002 in order for construction along the Pipeline right-of-way to start by early March, for completion by the end of June 2003.

2. PIPELINE ROUTING

Centra Gas proposes to install the Pipeline in the Galloping Goose right-of-way, which was formerly the Canadian National Railway right-of-way. The right-of-way is owned by the BC Transportation Financing Authority (“BCTFA”), is reserved by the Province for future transportation needs, and has been

designated by the BCTFA as a utility corridor. It is leased to Capital Regional District Parks (“CRD Parks”), which manages the Galloping Goose Regional Trail.

Centra Gas evaluated three other routes for the Pipeline:

- a route along Sooke Road (Highway 14) between Langford and Sooke,
- a route along an abandoned water line that generally parallels Sooke Road, and
- a cross-country route through the Capital Regional District watershed.

The cost of the Pipeline would be higher along any of the alternative routes. Specifically, the Sooke Road route would increase costs by \$0.4 million, and the Ministry of Transportation (“MoT”) stated that the Galloping Goose route is preferred over the Sooke Road route. Centra Gas concluded that the Galloping Goose right-of-way is the only feasible route.

The Application includes an Environmental Impact Study for the Pipeline along the Galloping Goose right-of-way that was completed by Golder Associates in October 2000. The Study concluded:

“All identified potential impacts can be effectively managed by implementing mitigation strategies consistent with regulatory requirements and best management practices. As a result, the project is not anticipated to result in any residual impacts which would otherwise require compensation.”

The Pipeline has received required approvals from the Districts of Langford, Metchosin and Sooke. Approvals from the Oil and Gas Commission and the MoT for the Pipeline are expected by the end of 2002. MoT approvals related to the distribution mains are expected by the end of January 2003.

Centra has negotiated a Construction Terms and Conditions Agreement with BCTFA and CRD Parks. Centra Gas expects to complete a Natural Gas Pipeline Corridor License agreement with BCTFA in January 2003. The agreements require Centra Gas to pay a license fee of \$500,000 to BCTFA for a 20-year term. Most of the fee will be used for enhancements to the Galloping Goose Regional Trail. The Operating Agreement with the District of Sooke has been approved in principle and is expected to be completed by the end of January 2003.

Agreements with BCTFA and CRD Parks are necessary to use the right-of-way, but several provisions of the agreements that Centra Gas has negotiated increase the risk profile of the system extension project. A discussion of these concerns follows.

A condition of the draft Natural Gas Pipeline Corridor License agreement is that Centra Gas is responsible for relocation of the pipeline to accommodate the construction of a Light Rapid Transit (“LRT”) system, if required. Centra Gas states that the Galloping Goose right-of-way is wide enough to accommodate both the pipeline and a LRT system, and the construction of an LRT system along the section of the right-of-way beyond Langford is very unlikely. The Commission accepts Centra Gas’ position that the risk of having to relocate the pipeline for LRT is very low.

In response to concerns that were raised during public meetings, the Construction Terms and Conditions Agreement provides that Centra Gas will fund a CRD Parks Monitor. The Monitor or BCTFA will have the power to stop construction work if the contractor is not working within the terms of the agreement. These terms include typical construction activities, avoidance of environmental impact, hours of work and restricting construction activities to the traveled portion of the right-of-way. Centra Gas expects that any delays that result will be relatively minor, and have agreed that any cost savings from the project budget will be shared with CRD Parks. The Commission questions whether the additional level of oversight is needed, considering the responsibilities of the Oil and Gas Commission and monitoring of contractor activities by Centra Gas. Nevertheless, the Commission anticipates that the CRD Monitor and the BCTFA, acting responsibly, will not materially delay the project or increase the cost of the Pipeline.

The Application justifies the \$500,000 license fee for use of the right-of-way by a statement that:

“The fee is based on similar uses of right-of-way corridors by utilities in other jurisdictions and was set by BCTFA at approximately \$1.00 per meter per year over a twenty-year period.”

The fee is a significant cost factor for the system extension, which has marginal economic feasibility. Moreover, the situation at the end of the 20-year period is of concern as the draft Natural Gas Pipeline Corridor License agreement indicates that the terms and conditions and license fee for any Renewal Period will be determined by BCTFA. This could leave Centra Gas in an untenable situation, where it might be obliged to pay an unreasonable fee in order to continue to serve customers in Sooke. The Sooke system extension is a project that is only viable over the longer term. This is consistent with the 1.89 percent (53 years) depreciation rate for the Pipeline that was used in the feasibility analysis in the Application.

The Galloping Goose right-of-way has been designated as a utility corridor, and the pipeline is compatible with this use for the long term. **The Commission approves the proposed Galloping Goose right-of-way route for the Pipeline.** The provisions in the draft Natural Gas Pipeline Corridor License agreement related to the Removal of Pipeline at the end of the agreement and the license fee for any renewal period are under discussion. **The Commission is generally prepared to accept the arrangements for the use of**

the right-of-way for the pipeline, providing the final agreements for its use provide Centra Gas with the ability to extend its use of the right-of-way beyond the 20-year term currently contemplated by a draft agreement, under terms and conditions and license fees that are reasonable. This may include a dispute resolution clause.

3. LOAD FORECAST

Centra Gas carried out the load forecast by first assessing the number of potential customers, then estimating the proportion of potential customers that will use natural gas, and finally estimating the level of usage of the various customer groups. The Application included three forecast scenarios based on a range of saturation rates (Conservative, Moderate, Aggressive) for residential customers over a ten-year period to test the project feasibility.

According to census statistics from Statistics Canada, the number of dwellings in the District Municipality of Sooke increased by 2.6 percent per year between 1991 to 2001. The 2 percent per year growth assumed by Centra Gas for the next ten years is therefore not unreasonable. Centra Gas identified 532 and 1,765 potential customers respectively in Year 1 and Year 5 based on its construction plan for distribution mains. Growth in potential customers identified after Year 5 is expected to be much lower than during the first five years, estimated to rise from 1,765 in Year 5 to 2,000 in Year 10. The figures for growth in potential customers appear cautious. The Application identified a proposed development with 650 residential lots for which an approval bylaw recently received third reading by Sooke Council, but did not include these potential customers in the base case. If these additional customers are included while holding all other assumptions constant, the forecast load of this modified Moderate Scenario would be higher than the base case Aggressive Scenario.

The saturation rates used by Centra Gas for the benchmark years for residential customers are:

<u>Scenario</u>	<u>Year 1</u>	<u>Year 5</u>	<u>Year 10</u>
Conservative	15%	35%	45%
Moderate	20%	40%	55%
Aggressive	25%	55%	65%

The Conservative Scenario is cautious for both Year 1 and Year 5 and the rates under the Aggressive Scenario may be considered unlikely, given the Centra Gas historical capture rate of 30 percent for Year 1 and 50 percent by Year 5. The rates under the Moderate Scenario are acceptable and are supported by Centra Gas' market research studies on stated intention to convert. The saturation rate for Year 10 shows

that the saturation rate increases from 40 percent in Year 5 to 55 percent. This is a 15 percentage point jump, higher than the 10 percentage point increase from the two other scenarios. Although the Commission considers that a 50 percent saturation rate would have been a more realistic figure for the project feasibility analysis, the effect on the load forecast is considerably less than the difference between the Moderate and Conservative Scenarios.

Capture rates for commercial customers were derived from a field survey, which identified that many commercial establishments currently use propane. The provincial government has agreed to extend Clean Choice Grants to commercial customers in Sooke who convert from propane to gas.

Centra Gas estimated use per customer based on a field review of potential customers in each class, historical usage values and discussions with customers. The estimated annual usage in GJ for the various rate classes generally fall within the current annual actual usage for similar classes in the Company's other service areas. The Commission accepts the projections as reasonable.

The Sooke School Board and the Seaparc Recreation Centre have signed commitments to convert to natural gas and will receive substantial financial assistance to offset the cost of conversion. These customers represent 21,300 GJ of demand, which is one-half of the forecast load for Year 1.

Natural gas rates relative to the cost of other forms of energy will affect Centra Gas' ability to attract customers to gas, and cause uncertainty in forecasts of load for the extension to Sooke. Although the likely Year 10 saturation rate may be closer to 50 percent rather than 55 percent, the **Commission accepts the load forecast results from the Moderate Scenario, as increased loads should also materialize from the new residential development that Centra Gas did not include in its forecast.**

4. PROJECT FEASIBILITY

Centra Gas evaluated the project using a methodology that is generally consistent with the Main Extension Test in its tariff. The test compared the net present value ("NPV") of revenue requirements with the NPV of revenue over a 15-year period. Results were summarized in a Profitability Index where numbers greater than 1.0 indicate the additional revenue generated exceeds the incremental cost of the project.

The analysis included the cost of the Pipeline to Sooke plus the cost of the distribution mains that will be built over the first five years. A \$0.14/GJ allowance for expansion of the transmission system was included. The revenue is for customers that are forecast to be attached over the first ten years. Centra Gas' standard Main Extension Test includes revenue from customers who are forecast to be attached in the first

five years. The five-year criterion is based on the Commission's Utility System Extension Guidelines, which noted the greater forecast uncertainty associated with longer periods. Centra Gas justifies its use of ten years by the phased build approach to installing distribution mains in Sooke, and the fact that the project will introduce natural gas to an area that has not had service before. The Company considers that customer additions will continue to be made after Year 5, and that it is reasonable to include them in the feasibility test.

Centra Gas also used the proposed sales rates for 2003 from its September 2002 Rate Design Application, and increased the rates by annual CPI increments of 2 percent through 2007. The standard Main Extension Test specifies "...the most recently approved sales rates in the Company's tariffs for the initial year of the test...". Centra Gas confirmed that the other Key Variables shown in Appendix L of the Application generally reflect the July 2002 Revenue Requirements and September 2002 Rate Design Application, except for cost of gas, additional emergency response expense, and sales and marketing expense. The additional emergency response expense was estimated at \$22,000 per year, while sales and marketing expense was forecast at a one-time amount of \$50,000 in 2003.

The results of the feasibility analysis in terms of the Profitability Index are:

	<u>Conservative</u>	<u>Moderate</u>	<u>Aggressive</u>
10 Years customer additions	0.971	1.000	1.042
Pipeline costs 20% lower*		1.038	
Pipeline costs 20% higher		0.964	
5 Years customer additions	0.850	0.880	0.933

* The 20 percent reduction in the cost of the Pipeline reduces project costs by \$392,000.

In response to an Information Request from Commission staff, Centra Gas calculated a Profitability Index of 1.051 for a Moderate Scenario case that included the effect on forecast load of the 650 lot residential subdivision development that has recently been approved.

Centra Gas also evaluated a Moderate Scenario case using factors from the proposed Settlement for the July 2002 Revenue Requirements Application, cost of gas information for 2003 to 2005 from the September 2002 Rate Design Application, and the load for the new subdivision in Sooke. The calculated Profitability Index for this scenario is 1.054.

Centre Gas considers that the Profitability Index of 1.000 for the base case Moderate Scenario may understate the likely financial results from the project, due to the conservative approach to demand forecasting and the updated capital cost estimate.

For the feasibility analysis of the Sooke project, the Commission accepts Centra Gas' rationale for including the incremental revenue from customer additions over the first ten years. With the phasing of distribution mains, customers will continue to be added after Year 5, although it must be recognized that there is more uncertainty in the forecast of these later additions. The Commission also accepts that the use of proposed 2003 and subsequent gas sales rates in the analysis is appropriate for planning purposes. Overall, the Commission accepts the feasibility analysis in the Application.

The Profitability Index of 1.000 for the base case Moderate Scenario in the Application is the minimum criteria of acceptability. The Commission notes that this is a relatively large project, the cost estimate includes a minimal contingency allowance, and several risks and uncertainties have been identified. However, the effect of including the new subdivision in Sooke increases the Profitability Index slightly to 1.05, and incremental revenue will continue to be generated after 15 years. Notwithstanding the uncertainty in several factors used in the analysis, **the Commission accepts that the economics of the project justify its approval.**

5. PUBLIC CONSULTATION

Centra Gas held two open houses in Sooke and Metchosin in April 2000 and two public meetings in August 2002 in the area. The Company considers that all members of the public who may be affected by the project have had an opportunity to express their views. Issues raised by the public have been addressed in the Construction Terms and Conditions Agreement with BCTFA and CRD Parks for the Pipeline in the Galloping Goose right-of-way, and the Operation Agreement with the District of Sooke for the distribution mains.

Centra Gas published a notice regarding the Pipeline in local papers in September 2002 on behalf of the Oil and Gas Commission. Three letters and e-mails were received by Centra Gas and the Oil and Gas Commission, one of which opposed locating the Pipeline in the Galloping Goose right-of-way.

In a recent amendment to the Construction Terms and Conditions Agreement, Centra Gas committed to hold public information meetings on construction scheduling in Langford, Metchosin and Sooke in February 2003.

Centra Gas is close to finalizing agreements for the project with BCTFA, CRD Parks and the District of Sooke. The Application includes commitment letters from Seaparc Recreation Centre and Sooke School District, and letters of support from the District of Sooke and the Sooke Harbour Chamber of Commerce.

Centra Gas has held several public meetings over a period of time, and has committed to hold public meetings on project scheduling. The response to the most recent public notice about the Pipeline was minimal. **The Commission considers that the public has been sufficiently informed about the extension to Sooke and has had adequate opportunity to express views on the matter. No further public process is needed at this time, but Centra Gas will be expected to be responsive to concerns that are raised about construction scheduling, while remaining cognizant of the cost and scheduling constraints for the project.**

6. COMMISSION DETERMINATION

The Commission has considered the routing, cost estimate, load forecast, economic feasibility, and public consultation for the project, and has found each to be acceptable. Two areas of concern are project cost containment and the absence to date in a draft agreement with the BCTFA of assured access at reasonable cost to use the Galloping Goose right-of-way after 20 years.

The Galloping Goose right-of-way has been designated as a utility corridor. There is little point in proceeding with the Pipeline unless service can be provided to Sooke customers for the longer term. **The Commission grants a CPCN as requested in the Application; however, as a condition of the CPCN the parties need to conclude an agreement acceptable to the Commission by February 28, 2003 for Centra Gas to use the right-of-way for the long term under reasonable terms and usage fees. Also, in recognition of the marginal economics of the project, the Commission will expect the parties involved with the project to take all possible actions to limit costs, so that gas service can be provided to customers in Sooke without increasing costs for other Centra Gas customers. Any cost overruns, while not expected, must be fully explained and justified by Centra Gas in its monthly progress reports and final report.**

The Application requested approval to record an Allowance for Funds Used During Construction at the Company's weighted average cost of capital, which is approximately 7 percent. **The Commission approves this request.**