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**BRITISH COLUMBIA
UTILITIES COMMISSION**

**ORDER
NUMBER** G-52-06

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

and

**An Application by 0745848 B.C. Ltd.
for Approval of the Acquisition of the Common Shares of Terasen Utility Services Inc.**

BEFORE: L.F. Kelsey, Commissioner May 10, 2006
L.A. Boychuk, Commissioner

O R D E R

WHEREAS:

- A. On January 30, 2006, 0745848 B.C. Ltd. (the "Applicant") applied pursuant to Section 54 of the Utilities Commission Act ("the Act") for an Order approving the acquisition of the common shares of Terasen Utility Services Inc. ("TUS") from Terasen Inc. ("Terasen") which would cause the Applicant to have indirect control of Terasen Multi-Utility Services Inc. ("TMUS") (the "Application"); and
- B. TMUS is a public utility as defined in the Act and is regulated by the British Columbia Utilities Commission (the "Commission"); and
- C. The Applicant and Terasen have entered into a January 16, 2006 agreement to complete a transaction under which the Applicant, a B.C. company owned by CAI Capital Management Co. ("CAI"), British Columbia Investment Management Corporation ("BCIMC") (as to an approximately 48 percent interest each) and the current senior management of TUS, will acquire all of the issued and outstanding common shares of TUS; and
- D. Immediately following the acquisition, the Applicant and TUS intend to amalgamate, which will result in TMUS being a wholly-owned subsidiary of the amalgamated entity; and
- E. TMUS informed each of its customers at Panorama Mountain Village, Sun Rivers and Sonoma Pines by individual letter about the Application and referred them to the Commission's website for information on the regulatory review process of the Application; and

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F. Section 54(9) of the Act states:

“The commission may give its approval under this section subject to conditions and requirements it considers necessary or desirable in the public interest, but the commission must not give its approval under this section unless it considers that the public utility and the users of the service of the public utility will not be detrimentally affected.”; and

G. The Commission has considered the Application and submissions obtained during the written hearing process and has determined that the public utility and the users of the service will not be detrimentally affected by the proposed acquisition.

NOW THEREFORE the Commission orders as follows:

1. The Commission approves, pursuant to Section 54 of the Act, the acquisition by 0745848 B.C. Ltd. of the common shares of TUS from Terasen which would cause the Applicant to have indirect control of TMUS.
2. This approval is subject to the conditions contained in the attached Reasons for Decision.

DATED at the City of Vancouver, in the Province of British Columbia, this 11th day of May 2006.

BY ORDER

Original signed by:

L.F. Kelsey
Commissioner

Attachment

**An Application by 0745848 B.C. Ltd.
for Approval of the Acquisition of the Common Shares
of Terasen Utility Services Inc.**

REASONS FOR DECISION

1.0 THE APPLICATION

On January 30, 2006, 0745848 B.C. Ltd. (the “Applicant”) applied to the British Columbia Utilities Commission (“Commission”, “BCUC”) pursuant to Section 54 of the Utilities Commission Act (the “Act”) for an order approving the acquisition of the common shares of Terasen Utility Services Inc. (“TUS”) from Terasen Inc. (“Terasen”) which would cause the Applicant to have indirect control of Terasen Multi-Utility Services Inc. (“TMUS”) (the “Application”). TMUS is a public utility as defined in the Act and is regulated by the Commission.

The Applicant and Terasen entered into a January 16, 2006 agreement to complete a transaction under which the Applicant, a B.C. company owned by CAI Capital Management Co. (“CAI”), British Columbia Investment Management Corporation (“BCIMC”) (as to an approximately 48 percent interest each) and senior management of TUS, will acquire Terasen’s entire water and utility services business (the “Transaction”). The Transaction is the acquisition by the Applicant from Terasen of the all the issued and outstanding common shares of TUS and through two separate subsidiaries of the Applicant, all of the outstanding common shares of Terasen Water & Utility Services Inc. and Inland Pacific Resources Inc. As part of this transaction, an affiliate of the Applicant will acquire all of the outstanding shares of Terasen Waterworks (Supply) Inc. (the “WUS Business”, the “WUS Entities”).

Immediately following the acquisition, the Applicant and TUS intend to amalgamate, which will result in TMUS being a wholly-owned subsidiary of the amalgamated entity. TUS owns all of the outstanding shares of TMUS.

CAI is a private equity firm which makes investments in North American companies, with an emphasis on Canada. BCIMC provide professional funds management services for public bodies and publicly administered trust funds. Public sector pension plans constitute BCIMC’s largest client group.

The Application provided a chart that set out the ownership structure of the WUS Business before giving effect to the Transaction, after the closing of the acquisition and after the completion of the Transaction (Application, pp. 2-4). Certain amalgamations are proposed to occur after the closing of the acquisition and after the completion of the Transaction. By letter dated May 3, 2006, the Applicant advised the Commission that it is considering making changes to the corporate structure originally filed on page 4 of the Application to more clearly delineate those portions of the new entity at the close of the Transaction, which will be subject to regulatory oversight by the Commission. In the Applicant’s view, the contemplated changes to the corporate structure result in no change to the ownership or to the direct or indirect control of TMUS and have no material impact on the Commission’s review of the Application. By letter dated May 5, 2006, the Applicant explained that the contemplated revisions to the ownership structure are intended to separate the regulated from the non-regulated operations.

2.0 THE UTILITIES COMMISSION ACT

Section 54(7) of the Act states:

“A person must not acquire or acquire control of such numbers of any class of shares of a public utility as

(a) in themselves, or

(b) together with shares already owned or controlled by the person and the person’s associates,

cause the person to have a reviewable interest in a public utility unless the person has obtained the Commission’s approval.”

Section 54(4) states that for the purposes of Section 54,

“a person has a reviewable interest in a public utility if

(a) the person owns or controls, or

(b) the person and the person’s associates own or control,

in the aggregate more than 20% of the voting shares outstanding of any class of shares of the utility.”

Section 54(9) states:

“The commission may give its approval under this section subject to conditions and requirements it considers necessary or desirable in the public interest, but the commission must not give its approval under this section unless it considers that the public utility and the users of the service of the public utility will not be detrimentally affected.”

3.0 THE REGULATORY PROCESS

The Act provides the Commission with discretion in regard to its process for assessing the acquisition of a reviewable interest. TMUS informed each of its customers at Panorama Mountain Village, Sun Rivers and Sonoma Pines by individual letter about the Application and referred them to the Commission’s website for information on the regulatory review process of the Application.

By Order No. G-15-06 dated February 17, 2006, the Commission established a written public hearing process and, as part of a stakeholder consultation process, required the Applicant to conduct workshops in the service areas to inform the public of the Application and respond to questions from the public concerning the Application and the process to consider the Application. The Commission directed the Applicant to publish the Notice of Written Public Hearing Process, including workshops, in such appropriate local news publications in the service area so as to properly provide adequate notice to the customers served in the service areas of TMUS. TMUS advised the Commission that workshops were held in Panorama Mountain Village, Sun Rivers and Sonoma Pines as required by Order No. G-15-06 and that there were no attendees at the workshops (Commission IR No. 1, question 8.1).

Appendix A to Order No. G-15-06 provided a regulatory timetable with deadlines for interventions, information requests and responses, and comments and submissions by Intervenor and the Applicant. On March 8, 2006, the Commission issued Commission Information Request No. 1 with the Applicant filing a reply on March 14, 2006.

Three requests for intervenor status were received by the due date and one letter of comment was received related to the Application.

4.0 THE INTERVENOR SUBMISSIONS COMMENTS

Information requests and a submission were received from only one intervenor, Mr. Binette. In his submission, Mr. Binette submitted that the Application should be denied, without a detailed explanation.

5.0 THE KINDER MORGAN, INC. DECISION AND THE APPLICATION

The Kinder Morgan Inc., Decision

On August 17, 2005, Kinder Morgan, Inc. (“KMI” or “Kinder Morgan”) and 0731297 B.C. Ltd. (“Subco”) (collectively the “Kinder Morgan Companies”) applied to the Commission pursuant to Section 54 of the Act for approval of the acquisition by the Kinder Morgan Companies of the common shares of Terasen. The acquisition of the shares of Terasen will cause KMI to have indirect control of Terasen Gas Inc. (“TGI”), Terasen Gas (Vancouver Island) Inc. (“TGVI”), Terasen Gas (Squamish) Inc. (“TGS”), Terasen Gas (Whistler) Inc. (“TGW”), and Terasen Multi-Utilities Services Inc. (“TMUS”). Each of TGI, TGVI, TGW and TMUS are wholly-owned subsidiaries of Terasen. TGI owns all of the outstanding shares of TGS and TGS is an indirect wholly-owned subsidiary of Terasen. Each of TGI, TGVI, TGS, TGW and TMUS (collectively, the “Terasen Utilities”) are public utilities regulated by the Commission. Terasen also owns all of the outstanding shares of Terasen Pipelines (Trans Mountain) Inc. (“TM”). TM is not regulated by the BCUC, but rather by the National Energy Board. TM owns all of the outstanding shares of Terasen Pipelines (Jet Fuel) Inc. (“TPJF”). While the tolls of TPJF are regulated by the BCUC, TPJF is not a “public utility” as that term is defined in the Act and the provisions of Section 54 of the Act are not applicable to TPJF (the “KMI Acquisition”).

In its Decision dated November 10, 2005, the Commission approved the KMI Acquisition subject to conditions and directions contained in the Decision. Pages 43 to 46 of the KMI Decision provide a summary of the assurances made by KMI regarding the KMI Acquisition. These assurances relate to:

- Senior Management and Employees of Terasen Utilities
- Location of Headquarters for Terasen Utilities
- Customer Service
- Environmental and Safety Management Practices
- Organization Structure and Management Practices
- Finances
- Governance
- Natural Gas Resources/ Exports

The Application

In the current Application, the Applicant states that is “prepared to make the same assurances having regard to the relative size and scope of operations of TMUS and its current levels of service as compared to those under consideration in the Kinder Morgan Decision” (Commission IR No. 1, question 9.1).

On pages 49-51 of the KMI Decision, the Commission established conditions for the approval of the KMI Acquisition. The Applicant provided its views on the Commission establishing the same conditions for the approval of the current Application (Commission IR No. 1, question 9.2 and Exhibit E).

The following excerpts from Exhibit E repeat the conditions from the KMI Decision and provide the Applicant’s Response to those conditions:

- “(1) Each Terasen Utility shall maintain, on a basis consistent with BCUC orders and accounting practices, a percentage of common equity to total capital that is at least as much as that determined by the Commission from time to time for ratemaking purposes.

Response: The Commission has not currently set an approved capital structure for TMUS operations.

- (2) No Terasen Utility will pay a common dividend without prior Commission approval if the result would reasonably be expected to violate the restriction in (1) above.

Response: Agreed.

- (3)(a) No Terasen Utility will lend to, guarantee or financially support any affiliates of the Terasen Utilities, other than between TGI and TGS, or as otherwise accepted by the Commission.

Response: As stated in response to 1.4, our bank financing commitment requires guarantees from each subsidiary entity in the business to be acquired by the Applicant, including TMUS. Other than this guarantee (given in connection with the financing contemplated in the bank commitment letter or a similar financing provided by another lender), TMUS will not lend to, guarantee or financially support its affiliates.

- (b) TGI and TGS shall together maintain separate banking and cash management arrangements from other affiliates. TGV shall establish separate banking and cash management arrangements from other affiliates once it has completed its proposed refinancing.

Response: It is anticipated that separate bank accounts will be maintained for the TMUS operations as they currently exist. These accounts are currently concentrated (rolled up) into the parent company for cash management purposes in order to keep financing costs to a minimum. If required, TMUS accounts could be kept separate. However, since TMUS currently runs a negative cash balance due to negative earnings and high capital requirements, interest charges would be incurred. The positive cash balance on the current consolidated group arrangement avoids interest charges.

- (c) No Terasen Utility will enter into a tax sharing arrangement with any affiliate of the Terasen Utility, unless the agreement has been approved by the Commission.

Response: Agreed.

- (4) No Terasen Utility will enter into transactions with affiliates that are not in compliance with Commission guidelines, policies or directives regarding affiliate transactions, and no Terasen Utility will enter into transactions with affiliates on terms less favorable to the Terasen Utility than those available from third parties on an arms-length basis, unless otherwise approved by the Commission.

Response: Agreed.

- (5) No Terasen Utility will engage in, provide financial support to or guarantee non-regulated businesses, unless otherwise approved by the Commission.

Response: Agreed, subject to the guarantee discussed in the response to 1.4

These conditions may be revised and/or supplemented in future by the Commission as required to protect the public interest.

7.2.2 Governance

The Commission Panel finds that the Terasen Utilities should be required to maintain existing governance policies and that any changes in these policies should be approved by the Commission. In particular, the Commission Panel concludes that the continued independence of Directors, as required in existing governance policies, will provide a further assurance that the Terasen Utilities will comply with the ring-fencing conditions.

Response: It is anticipated that there will be no changes to the existing governance policies in respect of TMUS.

7.2.3 Location of Functions and Data

In order to address privacy concerns, the Commission Panel determines that it would be appropriate to attach a condition to approval of the Transaction that requires KMI not to change the geographic location of any existing functions or data currently in TGI's service area without prior approval of the Commission.

Response: It is anticipated that there will be no change of location for any of the existing functions or data in respect of TMUS."

6.0 THE APPROVAL CRITERIA

In past decisions, the Commission has applied certain criteria to assist in determining whether there is potential for detrimental effects to the utility and its customers and, in the broader sense, to the public interest.

In the KMI Decision the Commission also applied specific criteria to assist in determining whether the public utility and the users of the services of the public utility will be detrimentally affected by a proposed acquisition. The criteria used were that:

- (a) the utility's current and future ability to raise equity and debt financing not be reduced or impaired;
- (b) there be no violation of existing covenants that will be detrimental to the customers;
- (c) the conduct of the utility's business, including the level of service, either now or in future, be maintained or enhanced;
- (d) the application be in compliance with appropriate enactments and/or regulations;
- (e) the structural integrity of the assets be maintained in such a manner as to not impair utility service; and
- (f) the public interest be preserved.

1. The Utility's current and future ability to raise equity and debt financing not be reduced or impaired.

The Applicant states that the Transaction will not reduce or impair the ability of TMUS to raise debt and equity capital. The Applicant also states that it will continue to ensure that TMUS will be adequately funded with debt and equity capital in accordance with applicable regulations of the Act (Application, p. 11).

The Transaction has an estimated purchase price of \$125 million representing the Consolidated Net Book Value of the WUS Entities and the Applicant confirmed that no acquisition premium is being paid (Application, p. 4, Commission IR No. 1, question 4.1). The Transaction will be financed by a share subscription for a price of \$41.525 million each by CAI and BCIMC with the remaining portion (approximately \$43 million) financed by debt. Copies of share subscription agreements and a capital loan commitment letter for \$50 million from HSBC Bank Canada were filed as Exhibits A and C to Commission IR No. 1, question 1.3. Under the terms of the HSBC commitment letter, all of the companies in the WUS Business including TMUS are guarantors in respect of the \$50 million capital loan and a \$20 million operating loan. With the exception of credit arrangements like the one provided by HSBC, the Applicant does not anticipate that TMUS will have any other guarantee obligations (Commission IR No. 1, question 1.4).

The current financing arrangements for TMUS are provided through inter-company loans originating from Terasen and the Applicant anticipates that similar financing arrangements will be provided by the parent company of TMUS by way of debt and equity financing. The Applicant does not anticipate that any fees in addition to the all-in cost of internally or externally arranged financing will be charged to TMUS. While the source of financing may change over time, the Applicant states that it has secured financing for the Transaction,

the current year's budgeted additional and replacement capital for all the WUS Entities including TMUS and the forecasted capital over the next five years for existing and expected new projects (Commission IR No. 1, questions 1.1, 1.2, 1.5)

2. There be no violation of existing covenants the effect being detrimental to the customers.

The Applicant submits that there will be no violation of existing covenants as a result of this Transaction. The "existing covenants" referred to in the Application are the contractual obligations of TMUS under the terms and conditions of its agreements with developers of Sun River, Panorama Mountain Village and Sonoma Pines. The Applicant states that each of these parties were advised of the Transaction and none of them have expressed any concerns (Commission IR No. 1, question 2.1).

3. The conduct of the Utility's business, including the level of service, either now or in future, will be maintained or enhanced.

The Applicant submits that the conduct of TMUS' business including the level of service, both now and in the future, will be maintained or enhanced (Application, pp. 1-5). TMUS received services from Terasen and its affiliated companies for 24/7 emergency call-out, emergency first response, limited planning and drafting services, legal, regulatory and risk/insurance in accordance with the Terasen transfer pricing policy. The Applicant states that the WUS Business has already set up its own in-house legal and regulatory group and will also manage risk/insurance after the closing of the Transaction. TMUS will continue to contract out for 24/7 emergency call-out, emergency first response and limited planning and drafting services from qualified service providers. As these services were previously provided under transfer pricing provisions, no significant price impact on TMUS customers is expected from contracting out for these services (Commission IR No.1, question 3.1).

The Applicant considers that TMUS will have enhanced access to legal and regulatory oversight in all of its operations due to the hiring of in-house staff compared to the past where TMUS received services from Terasen or its affiliate companies. TMUS will comprise a more significant part of the overall business of the Applicant than it does within the Terasen group of companies. The new Board of Directors of the Applicant, which includes former executives of Terasen, will be able to focus more on the business in which TMUS is engaged (Commission IR No. 1, question 3.3).

With regards to the level of ownership and expertise in operating regulated utilities, the Applicant explains that, prior to the acquisition of Terasen by Kinder Morgan, BCIMC was a significant shareholder in Terasen and has familiarity with regulated utilities. A key factor in the decision for both CAI and BCIMC to invest in the WUS Business was that the existing management of the WUS Business would participate as owners and remain in place. CAI and BCIMC would mainly provide its support to the management team of the WUS Business in the form of capital and business experience and governance through the Board of Directors (Commission IR No. 1, question 3.4).

4. The Application be in compliance with appropriate enactments and/or regulations.

The proposed Transaction is subject to various consents and approvals of the Commission and other regulatory authorities. These requirements must be met before the Applicant will be able to close the transactions contemplated in the January 30, 2006 Application.

5. The structural integrity of the assets be maintained in such a manner as to not impair utility service.

The Application states that the completion of the Transaction does not involve any material change in the operation of the assets of TMUS and accordingly the structural integrity of the assets of TMUS will be preserved. Following completion of the Transaction, the Commission will retain regulatory control of TMUS and its assets and operations. The Application acknowledges that TMUS has an obligation to provide safe, reliable and secure service to its customers under the jurisdiction of the Commission. The Application also acknowledges that TMUS operations remain subject to the continuing oversight of the BC Safety Authority, BC Oil and Gas Commission and the BC Workers Compensation Board (Application, p. 13).

6. The public interest be preserved.

The Applicant submits that based on the criteria applied by the Commission in its earlier Decisions under Section 54 of the Act, that neither TMUS nor the users of the services of TMUS will be detrimentally affected and that the public interest will be preserved by the completion of the Transaction. The Applicant states that the Transaction will have no material impact on TMUS, its operations or services provided by TMUS and it will not change the Commission's authority to regulate the operations of TMUS (Application, p. 11).

In conclusion the Application states that:

“In all of the circumstances of this Application, it is clear that, following completion of the Transaction:

- (a) there will be unaffected continuity in the management, business and operations of TMUS;
- (b) the structural integrity of the assets of TMUS will be maintained;
- (c) there will be unaffected continuity in the utility services provided by TMUS to its customers;
- (d) there will be unaffected continuity in the regulation of TMUS and its services by the Commission under the UCA;
- (e) there will be no adverse impact on the ability of TMUS to access capital;
- (f) there will be no breach of existing covenants given by or in respect of TMUS;
- (g) there will be compliance with applicable Provincial and Federal statutes and regulations; and
- (h) the public interest will be preserved.

Completion of the Transaction will not detrimentally affect TMUS or the users of the services of TMUS” (Application, p. 13).

7.0 COMMISSION PANEL DETERMINATION

The Commission finds that there is no evidence of detrimental impact resulting from approval of the proposed acquisition. The Commission also notes that, as acknowledged by the Applicant, the Commission's ongoing jurisdiction with respect to the Utility is not altered as a result of the Transaction.

The Commission Panel approves the application by 0745848 B.C. Ltd. to acquire the common shares of TUS from Terasen, which will cause 0745848 B.C. Ltd. to have indirect control of TMUS, subject to the following conditions.

Conditions:

- (a) The Commission accepts that the Applicant is prepared to make the same assurances having regard to the relative size and scope of operations of TMUS and its current levels of service as compared to those under consideration in the Kinder Morgan Decision (Commission IR No. 1, question 9.1).**
- (b) The Commission considers that all of the conditions of approval established in the KMI Decision are not necessary for a utility the size of TMUS. In order to prevent possible financial harm to TMUS the Commission has set the following conditions on the Application, which the Commission considers to be necessary or desirable in the public interest:**
 - i) TMUS will not lend to, guarantee or financially support any affiliates of the Applicant, other than the banking commitment required for this Application, or as otherwise accepted by the Commission.**
 - ii) TMUS will not enter into a tax sharing arrangement with any affiliate of the Applicant, unless the agreement has been approved by the Commission.**
 - iii) TMUS will not enter into transactions with affiliates that are not in compliance with Commission guidelines, policies or directives regarding affiliate transactions, and not enter into transactions with affiliates on terms less favorable to TMUS than those available from third parties on an arms-length basis, unless otherwise approved by the Commission.**
 - iv) These conditions may be revised and/or supplemented in future by the Commission as required to protect the public interest.**
- (c) TMUS is to operate on a stand-alone basis, unless otherwise approved by the Commission.**