



LETTER NO. L-4-06

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VIA E-MAIL

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January 24, 2006

Mr. Stirling Bates, Director
Regulatory Section
Ministry of Energy, Mines and Petroleum Resources
PO Box 9323, Stn Prov Gov't
5th Floor, 1810 Blanshard Street
Victoria, BC V8W 9N3

Dear Mr. Bates:

Re: Terasen Gas (Squamish) Inc.
Thunderbird Creek Main Extension

On October 28, 2005, Terasen Gas (Squamish) Inc. ("TG Squamish") filed its Thunderbird Creek Main Extension ("the Application") with the Ministry of Energy, Mines and Petroleum Resources ("the Ministry"). The Commission's responsibility is to provide the Ministry a financial review of the main extension. The Commission has reviewed the financial projections contained in the Application and also the December 9, 2005 TG Squamish response to BCUC Information Request No. 1.

The current main extension ("MX") test, as approved by the Commission and the Ministry, is a Rate Stabilization Facility ("RSF") test using four inputs:

- 1) capital costs including mains and services;
- 2) projected gross revenue based on the current TG Squamish rates;
- 3) projected customer attachments and volume based upon TG Squamish's forecast; and
- 4) current gas costs and resulting net revenue.

A main extension is recommended for approval if the projected net revenue in the first six years equals or exceeds the estimated cost of construction and the 20-year cumulative discounted RSF balance is positive. In previous applications TG Squamish has taken responsibility for increased RSF funding resulting from:

- 1) capital costs that are higher than forecast; and
- 2) customer consumption and attachments less than forecast.

TG Squamish in its Application stated it is not prepared to assume the volume risk and therefore economic risk for a development's main extension. Consequently, TG Squamish is requiring developers to pay for the entire capital costs of the main extension and service lines up to the property lines with a Contribution in Aid of Construction ("CIAOC").

The Application requested approval for the Thunderbird Creek main extension and also appeared to request approval for a change to the methodology of the MX process. The Application included a financial analysis of the main extension with costs for the mains and services to attach 82 customers using 90 GJ per customer, based on a modified TG Squamish test. The revenue in the financial analysis was calculated using a "notional revenue" of \$4.80/GJ based on the difference between the current cost of service and current cost of gas. The revenue

calculation was a departure from the currently approved methodology, which uses inputs of \$11.26/GJ for revenue and \$9.941/GJ for gas costs.

The TG Squamish information response to BCUC Information Request No. 1, particularly to Question 2.1, clarified that TG Squamish was only seeking approval for the Thunderbird Creek main extension and not for a change in the methodology of the MX process ("Revised Application").

The Revised Application is based on a CIAOC from the developer of \$101,500 without the addition of customers, which would come at a later time. Based on this test, TG Squamish believes that the Thunderbird Creek main extension should be approved. The result of this test provided in Appendix 2.1 of the information response shows the estimated RSF draw is approximately \$2,000 per year that is attributable to property tax and it also shows the 20-year cumulative discounted RSF draw is \$23,492. However, the information response shown in Appendix 5.2 based on the current MX test with a CIAOC of \$101,500 but with 82 customers using 90 GJ/year indicates a significant 20-year cumulative discounted RSF draw of \$116,445. These results indicate that the Thunderbird Creek main extension is uneconomic when no customers are attached and highly uneconomic when 82 customers are attached.

TG Squamish, in its information response to Question 2.1, stated that TG Squamish in its initial Application estimated that future attachments would result in additional capital costs of \$22,032, \$22,473, and \$23,771 for the years 2006, 2007 and 2008, respectively, to serve a total of 82 customers that use 90 GJ/year. However, since TG Squamish did not know when these customers would attach, TG Squamish was not requesting approval for those capital projects in the Revised Application. Instead, TG Squamish proposed that when the new individual owner requests gas service TG Squamish will then determine whether or not the customer can be added economically and how/if they should be attached to the system.

In the Revised Application TG Squamish eliminated the forecast customer attachments and consequently did not take into account any forecast consumption and customer activity related to the main extension that would unfavourably impact the RSF.

The Commission finds that the initial Application with the estimated customers and volume usage are reasonable to use as inputs to assess the economics of this main extension. Main extensions are to be assessed on the best available information including all the forecast revenues, costs, consumption, and customers. The Revised Application does not consider all of these components. The TG Squamish proposal to wait until each customer requests gas service to determine the economic of each attachment, is not appropriate. The financial analysis using the approved main extension test methodology including the four inputs identified above indicates the Thunderbird Creek main extension is uneconomic with large annual RSF draws.

The currently approved main extension test is based on a threshold where the projected net revenue in the first six years equals or exceeds the estimated cost of construction and the 20-year cumulative discounted RSF balance is positive. The Commission recommends approval to the Ministry when a proposed main extension meets the test threshold. The Thunderbird Creek main extension has not met the approved main extension test and therefore approval is not warranted.

Yours truly,

Original signed by

Robert J. Pellatt

DC/dg

cc: Mr. Scott A. Thomson
Senior Vice President and CFO
Terasen Gas (Squamish) Inc.

Mr. Paul Wieringa, A/ Executive Director
Oil and Gas Policy Branch
Ministry of Energy, Mines and Petroleum Resources