



November 20, 2006

British Columbia Utilities Commission
Sixth Floor
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Vancouver, B.C. V6Z 2N3

Scott A. Thomson
VP, Finance & Regulatory Affairs and
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Regulatory Affairs Correspondence
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Attention: Mr. Robert J. Pellatt, Commission Secretary

Dear Sir:

**Re: Terasen Gas Inc. ("Terasen Gas", "TGI" or the "Company")
Annual Review and Mid Term Review Workshop
Response to Undertakings**

On October 16, 2006, Terasen Gas filed its Annual Review and Mid-Term Assessment Review material. On November 15, 2006, Terasen Gas' 2006 Annual Review and Mid-Term Assessment Review Workshop (the "Workshop") was held in accordance with the Regulatory Timetable established by British Columbia Utilities Commission ("BCUC" or the "Commission"). Included in Attachment 1 is a listing of the Workshop participants.

During the Workshop, Terasen Gas committed to several undertakings for additional information with response due by November 20, 2006. This submission represents the Terasen Gas response to these undertakings.

Amalgamation of Terasen Gas and Terasen Gas (Squamish) Inc.

On October 5, 2006 Terasen Gas, Terasen Gas (Vancouver Island) Inc. ("TGVI"), Terasen Gas (Squamish) Inc. ("TGS") and the Province executed the Termination Agreement (the "Agreement") which terminates the Rate Stabilization Agreement and Rate Stabilization Facility Continuation Agreement and amends the Transportation Service Agreement ("TSA"). The Agreement provides for a payment to be made by TGS to the Province in addition to terminating the main extension obligations of TGS. Additionally, as part of the Agreement, the Province also issued Special Direction No. 3, an amendment to the Special Direction 1510 issued in 1995, and a regulation under the *Vancouver Island Natural Gas Pipeline Act* by Order in Council 766. Lastly, the Agreement enables the Amalgamation of TGI and TGS (the "Amalgamation").

At the Workshop, TGI was asked a number of items related to the Amalgamation proposed for January 1, 2007, including confirmation of the specific approvals required of the Commission.

Approval of Amalgamation

At the Workshop TGI was asked about the applicability of Sections 40, 50, 52, 53 and 54 of the *Utilities Commission Act* (the "Act") to the Amalgamation. Included under Attachment 2 is a legal opinion provided to TGI with respect to the sections identified above. It is the position of TGI and TGS that these sections do not apply to either TGI or TGS with respect

to the Amalgamation and that no approval of the Amalgamation by the Commission is required.

Amendments Agreement s and Tariff provisions

Special Direction No. 3, by Order in Council 768, is effective January 1, 2007. Immediately after January 1, 2007, the following two applications will be made separately to the Commission to be effective January 1, 2007:

- (1) An application by TGVI for the Commission's consent to the amendment of the Transport Service Agreement ("TSA"), effective January 1, 2007, as described in Section 2.4 of the Agreement. The amendments fix the toll paid to TGVI by TGS for transportation on the TGVI system at \$1.05 per gigajoule. The amendments also fix the term of the TSA so that it terminates on the later of the date the TGVI revenue deficiency deferral account is reduced to zero or the date which the Commission establishes a new transportation rate for transportation of gas to Squamish. Sections 3 and 4 of Special Direction No. 3 relate to the TSA and its amendments.
- (2) An application by TGI for Commission approval, effective January 1, 2007, of revised page D-6 of the TGI Tariff to include "Squamish" within the defined area of the Lower Mainland Service Area. Sections 8 and 9 of Special Direction No. 3, relate to the inclusion of the Squamish area within the Lower Mainland Service Area. Section 5.3 of the Agreement states that when the Special Direction is effective, amalgamated TGI will request a change of the Tariff to include Squamish within the definition of Lower Mainland Service Area.

Rate Base Deferral Account

TGI hereby requests Commission approval of the establishment of the Rate Base Deferral Account for amalgamated TGI to record costs related to the Amalgamation and variances in operation and maintenance expenses as it impacts the 2007 Revenue Requirement as applied for in the 2006 Annual Review materials. Section 14 of Special Direction No. 3, which takes effect January 1, 2007, directs the Commission to approve establishment of this deferral account.

TGI Tariff Supplement I-3

Tariff Supplement I-3 provides for the sale of Gas from TGI to TGS at rates pegged to either TGI Rate Schedule 1 or 3 commodity and midstream charges. As per Section 8 and 9 of Special Direction No. 3, TGS customers will become TGI Lower Mainland customers as of January 1, 2007. TGS and TGI will amalgamate effective January 1, 2007. As such, Tariff Supplement I-3 will no longer have any effect. TGI hereby requests Commission approval to cancel Tariff Supplement I-3 effective January 1, 2007.

Included in Attachment 3, please find in duplicate for Commission endorsement the following revised Terasen Gas Tariff pages effective January 1, 2007.

First Revision of Index Page I i
Second Revision of Page i

TGI requests Commission endorsement of these tariff supplements pages, and that one set be returned to TGI for its records.

TGS Tariff Changes

The effect of Special Direction No. 3, Sections 8 and 9, is that as of January 1, 2007, customers who, as at December 31, 2006, were customers of TGS will, as at January 1, 2007, be treated as Lower Mainland customers of amalgamated TGI. Further, TGI and TGS will be amalgamating effective January 1, 2007. TGS hereby requests Commission approval to cancel the TGS Gas Tariff effective January 1, 2007.

Main Extension (“MX”) Test Review

During the Workshop, TGI was asked how the TGI MX test would apply to customers in what is now the TGS service area on a go-forward basis, as well as whether TGI would re-run the MX test for current mains. In its response to 2006 Annual Review and Mid-Term Settlement Review BCUC IR No. 1 (“BCUC IR No. 1”), Question 21.3.1, TGI responded that *“Consistent with current TGI practice, contributing main extensions are reviewed annually to determine if a refund is warranted”*. The review would be conducted using TGI inputs and, if warranted, those developers who paid a contribution under the TGS MX Test may see a refund of their contribution. Special Direction No. 3, Section 9 directs that the area served by TGS, as at December 31, 2006, as being within the “Lower Mainland Service Area”. As such, customers who were within the TGS service area prior to December 31, 2006, will be Lower Mainland customers as at January 1, 2007. Section 8 of Special Direction No. 3 directs the Commission to apply the TGI Tariff to amalgamated TGI. Therefore, main extensions in what was the TGS service area, should be conducted as per the TGI Tariff.

As part of TGVI’s Settlement Update proceeding, TGVI has stated that it is of the view that a generic review of system extension policies and customer connection policies should occur, and that TGVI is committed to reviewing these policies including MX tests during 2007 for implementation in 2008. Terasen Gas confirms that this review would be for both TGI and TGVI. Terasen Gas further confirms that items such as the treatment, within the MX Test, of the \$1.05 toll paid to TGVI for service to customers in Squamish, will be considered during the review.

Intangible Plant Costs – TGS Conversion Costs

During the Workshop, TGI was also asked to further explain the \$777,000 in intangible TGS plant in the response to BCUC IR No. 1, Question 3.1. The intangible plant is the remaining unamortized balance pertaining to the conversion of the TGS propane system to natural gas. TGS had been depreciating the plant at 2%, however, it had been amortized at 1% in the October 16, 2006 submission. In response to a query from Commission Staff, TGI proposes to revise its amortization of this account such that commencing January 1, 2007, amalgamated TGI will amortize the amount included in the intangible plant account over a ten-year period. TGI will reflect this revised treatment of this account in its revised Application, which is described below.

Pensionable Bonuses

During the Workshop, Commission Staff requested clarification of the treatment of non-executive bonuses related to pension expense that is to be recovered from customers, which had been discussed in the response to BCUC IR No. 1, Question 10.5. Commission Staff referred to the Commission Decision dated February 4, 2003, in the matter of the BC Gas Utility Ltd. [now Terasen Gas Inc.] 2003 Revenue Requirements Application. In the Decision, under Section 4.4 (Pensions) on page 21, it stated “*Consistent with the Commission’s 1992 and 1994 Decisions, the bonus is not to be included in the pension costs to be passed on to customers*”. The 2003 Commission Decision in effect states that bonuses are to be treated in a manner consistent with the Commission’s 1992 and 1994 Decisions.

The 1992 Decision referenced above was with respect to the 1992 BC Gas Inc. [later BC Gas Utility Ltd. and now Terasen Gas Inc.] Revenue Requirements Application. Under Section 5.8 of that Decision entitled “*Executive Manpower and Compensation*”, the Commission dealt at length with the issue of executive compensation, bonuses and pension costs, while compensation matters for employees other than executives were discussed under Section 5.7. Pension costs for executives were dealt with in particular in Section 5.8.6, which was entitled “*Executive Pension Plan*”. It is within this section of the 1992 Decision, specifically, on page 85 of the Decision under Section 5.8.6 where the Commission stated “*For rate-making purposes the bonus is not to be included in the pension costs to be passed on to customers*”. The context of the discussion preceding that statement indicates that the ‘bonus’ referred to in the quotation relates only to the ‘bonuses’ for executives and does not include bonuses for non-executive management and exempt employees or bargaining unit employees.

The 1994 Commission Decision relating to BC Gas Utility Ltd. also refers to executive bonuses. In Section 5.4 Executive Compensation, at page 15, the 1994 Decision states: “*Until then [referring to a study and report] BC Gas will comply with the 1992 Decision that bonuses not be included in determining executive pensions for funding by customers*”. It is clear from the 1994 Decision that bonuses to be excluded from the pension costs recovered in rates were the executive bonuses.

The 2003 Decision also makes it clear that only the executive bonuses were excluded from pension costs recovered in rates. In Section 4.4 of that Decision, on page 20 it states “*The Application also contained, as a portion of pension expenses, a pension provision on bonuses paid to employees. This was disallowed by the Commission in its June 16, 1994 Decision.*” The 2003 Decision further states “*BC Gas [now Terasen Gas Inc.] withdrew its request to have this expense included in its 2003 Revenue Requirements... The Downward adjustment to the 2003 Revenue Requirement was provided as part of BC Gas’ [now Terasen Gas Inc.] last set of revisions to its Application and was measured at a value of \$0.460 million (Exhibit 42).*” In its Final Argument dated December 2, 2002, the Company, on page 19 under the heading “*Pension Expense*”, stated “*The increased pension expense for the M&E and union plans requested in Exhibit 1C (after the adjustment at the commencement of the hearing and the withdrawal of the request for the pension expense relating to executive bonuses on day 7 of the hearing - Exhibit 41) is \$652,000.*”

On page 13 of the 2003 Decision under Section 4.1.1 entitled “*Executive Pay*” the Commission also notes that the cost of stock options and the portion of pension expenses on bonuses has been allocated to shareholders. The 2003 Decision goes on to state “*This reduces the ratepayer cost of executive compensation.*” The Company submits that the 2003 Decision is referring to only executive bonuses when directing the exclusion of bonuses from pension expense.

TGI has included bonuses for employees, with the exception of executive employees, as a pension cost to be recovered from customers in the Application currently before the Commission. TGI believes that this treatment is consistent with the Commission’s 2003, 1994 and 1992 Decisions.

Revisions to Application

The Company anticipates that the Commission will issue an Order setting the benchmark allowed Return on Equity (“ROE”) for 2007 by Friday, November 24, 2006. After the Order is issued, consistent with past practice, Terasen Gas will revise its Application (and rate proposals), to reflect the allowed ROE. Terasen Gas will submit this revision on Friday, December 1, 2006, which is the date set for the Company to submit its Reply Comments. Two additional items will also be reflected in the December 1 revision. First, the adjustment to the TGS O&M Variance deferral account from \$158,000 to \$170,551 as described in the response to BCUC IR No. 1, Question 8.3. Second, the revision to the amortization period for TGS conversion costs as described above.

If there are any questions regarding this submission please contact Tom Loski, Director, Regulatory Affairs at (604) 592-7464).

Sincerely,

TERASEN GAS INC.

Original signed by: Tom Loski

For: Scott A. Thomson

Attachments

c. 2004 – 2007 PBR NSP Participants

Attachment 1

TERASEN GAS INC.

2006 ANNUAL REVIEW MID-TERM SETTLEMENT REVIEW

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	PLEASE PRINT NAME	COMPANY	EMAIL	PHONE
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28	Jennifer Davison	NEMPR	participated via teleconference	

Attachment 2

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November 16, 2006
File No.: 240148.00584/14186

VIA EMAIL AND MAIL

Terasen Gas Inc.
16705 Fraser Highway
Surrey, B.C. V4N 0E8

Attention: Scott Thomson
VP Finance and Regulatory Affairs and Chief Financial Officer

Dear Sirs/Mesdames:

**Re: Amalgamation of Terasen Gas Inc. ("TGI")
and Terasen Gas (Squamish) Inc. ("TGS")**

During the Annual Review yesterday there were questions regarding the amalgamation of TGS and TGI. Reference was made to the August 18, 2006 application of FortisBC Inc. ("FBC") and Princeton Light and Power Company, Limited ("PLP") respecting the acquisition by FBC of PLP. In that application approvals from the British Columbia Utilities Commission ("Commission") are sought under sections 41, 50, 52, 53 and 54 of the *Utilities Commission Act* ("UCA"). You have requested that we provide our opinion on the applicability of those sections to the amalgamation of TGI and TGS.

At the current time TGS is a subsidiary of TGI, with 100% of the shares of TGS being owned by TGI.

Section 273 of the *Business Corporation Act* permits a holding corporation (in this case TGI) to amalgamate with its subsidiary (TGS) by way of a "short form" amalgamation. As noted in both sections 273 and 269 of the *Business Corporation Act*, the two companies amalgamate "and continue as one company". It is important to understand this concept of the two companies continuing as one company to understand why certain sections of the UCA are not applicable to the TGI/TGS amalgamation when they may be applicable to the FBC/PLP transactions. On the amalgamation of TGI and TGS neither company will cease to exist, rather the two companies will "continue as one company".

Section 41 - Section 41 deals with discontinuance of service by a public utility. In our opinion section 41 is not applicable to the TGS/TGI amalgamation since there will be no

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*Fasken Martineau DuMoulin LLP is a limited liability partnership and includes law

Vancouver Calgary Toronto Montréal Québec City New York London Johannesburg

discontinuance of service by the public utility. TGS and TGI will amalgamate, continuing as one company (one legal entity). That continuing legal entity will still be providing service to the customers in both the Squamish area and the areas in which TGI now provides service; so there will be no discontinuance of service.

Section 50 - Section 50 relates to the issuance of securities. To the best of our knowledge, the amalgamation of TGS and TGI will not give rise to the issuance of securities, and therefore we do not consider section 50 to be applicable.

Section 52 – Section 52 provides that a public utility must not dispose of property, other than in the ordinary course of business, except with approval of the Commission. Similar to the opinion expressed above with respect to section 41, there will not be a disposal of property on the amalgamation since the legal entity continuing as a result of the amalgamation will remain the owner of the gas distribution assets both in the Squamish area and in the areas now served by TGI. The assets now owned by TGS will not be transferred or sold to TGI, or otherwise disposed of by TGS. As a result of the amalgamation the assets now owned by both TGS and TGI will be owned by the one company that continues after the amalgamation. In our opinion there will be no disposition of assets by either TGS or TGI, and section 52 is not applicable to the TGI/TGS amalgamation.

Section 53 – Section 53 provides that a public utility must not consolidate, amalgamate or merge with another person without specified events occurring. The regulation made by Order in Council 766 orders that section 53 of the UCA does not apply to TGS or TGI in relation to an amalgamation of those two corporations. Order in Council 766 is made pursuant to section 7(2) of the *Vancouver Island Natural Gas Pipeline Act*. That section of the *Vancouver Island Natural Gas Pipeline Act* provides that the Lieutenant Governor in Council may make regulations ordering that prescribed sections of the UCA do not apply in respect of local distribution utilities. “Local distribution utility” is defined in section 1 of the *Vancouver Island Natural Gas Pipeline Act* to mean a public utility that operates a system, directly connected to the pipeline [defined to mean the natural gas pipeline of the company then named Pacific Coast Energy Corporation, and which is now named Terasen Gas (Vancouver Island) Inc. (“TGVI”)] for the transmission, sale or delivery of natural gas. Both TGI and TGS operate systems for the sale and delivery of natural gas that are directly connected to the pipeline of TGVI, and therefore both TGI and TGS are “local distribution utilities” for purposes of the *Vancouver Island Natural Gas Pipeline Act*. In our opinion section 53 of the UCA does not apply to the amalgamation of TGS and TGI because by regulation made under the *Vancouver Island Natural Gas Pipeline Act* it has been prescribed that the section does not apply in relation to such amalgamation.

Section 54 - Section 54 relates to the acquisition of control of a public utility. The test is whether or not there has been the acquisition of a reviewable interest (20% of any class of shares of the utility). Prior to amalgamation TGI owns 100% of the shares of TGS, and in turn TGI is owned and controlled by Terasen Inc. Since the amalgamation of TGI and TGS will be the amalgamation of a public utility with its immediate parent (which is also a public utility), and since ownership and control of the one company that will continue will remain with Terasen Inc., we are of the opinion that section 54 is not applicable. In our opinion there is no change in control and no acquisition of a reviewable interest.

It may be worthwhile to briefly distinguish the FBC/PLP transactions from the TGI/TGS amalgamation. In the table below transactions that the August 18, 2006 FBC/PLP application indicates will occur are identified and compared to the TGI/TGS amalgamation.

FBC/PLP Transactions

FBC will acquire all the shares of PLP, thereby acquiring a reviewable interest

The assets of PLP will be transferred to FBC effective December 31, 2006

PLP will be wound up

PLP will discontinue electric service on January 1, 2007

TGI/TGS Amalgamation

TGI and TGS will amalgamate; there will be no acquisition of the shares of one company by the other

TGI and TGS will amalgamate; there will be no transfer of assets. The one company continuing from the amalgamation will own the assets of the two amalgamating companies.


Neither TGI nor TGS will be wound up. The two companies will continue as one company.

Neither TGI nor TGS will discontinue gas service. The one company continuing from the amalgamation will continue to provide service in the areas formerly served by TGI and TGS.

In conclusion, it is our opinion that none of sections 41, 50, 52, 53 or 54 of the *Utilities Commission Act* are applicable to the amalgamation of Terasen Gas Inc. and Terasen Gas (Squamish) Inc.

Yours truly,

FASKEN MARTINEAU DuMOULIN LLP


C.B. Johnson, Q.C.

CBJ/vde

Attachment 3

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Tariff Supplement No.	Customer	Contract Date	Expiry Date
I-1	Reserved for Future Use.		
I-2	British Columbia Hydro and Power Authority Firm Tendered Transportation Service Agreement (as amended)	11/01/00	11/01/20
I-3	Reserved for Future Use.		
I-4	Reserved for Future Use.		
I-5	International Forest Products Limited - Amended and Restated Interruptible Liquefied Natural Gas Agreement	11/01/02	11/01/07
I-6	Northwest Natural Gas Company Firm Transportation Service Agreement	11/01/04	10/31/20
I-7	Fording Coal Ltd. Pipeline Agreement Fording Coal Mountain	01/01/03	12/31/17

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Order No.:

Effective Date: January 1, 2007

BCUC Secretary: _____

Issued By: Scott Thomson, Vice President
Finance & Regulatory Affairs and
Chief Financial Officer
Tariff Supplements
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TARIFF SUPPLEMENT NO. I-3

COPY

The July 1, 2004 Amended and Restated Gas Sales Agreement between Terasen Gas Inc. (Formerly BC Gas Utility Ltd.) and Terasen Gas (Squamish) inc. (Formerly Squamish Gas Co. Ltd.) is no longer in effect.

Pages 1 to 10 are cancelled and reserved for future use.

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Order No.:

Effective Date: January 1, 2007

BCUC Secretary: _____

Issued By: Scott Thomson, Vice President
Finance & Regulatory Affairs and
Chief Financial Officer
Tariff Supplement I-3
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