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February 10, 2011

British Columbia Public Interest Advocacy Centre
Suite 209 – 1090 West Pender Street
Vancouver, BC
V6E 2N7

Attention: Mr. James L. Quail, Executive Director

Dear Mr. Quail:

Re: Terasen Gas Inc. ("Terasen Gas")
Application for Approval of a Service Agreement for Compressed Natural Gas ("CNG") Service and for Approval of General Terms and Conditions ("GT&Cs") for CNG and Liquified Natural Gas ("LNG") Service (the "Application")

Response to the British Columbia Public Interest Advocacy Centre on behalf of the British Columbia Old Age Pensioners Organization et al ("BCOAPO") Information Request ("IR") No. 2

On December 1, 2010, Terasen Gas filed the Application as referenced above. In accordance with Commission Order No. G-181-10 setting out the Regulatory Timetable for review of the Application, Terasen Gas respectfully submits the attached response to BCOAPO IR No. 2.

If you have any questions or require further information related to this Application, please do not hesitate to contact Shawn Hill at (604) 592-7840.

Yours very truly,

TERASEN GAS INC.

Original signed:

Diane Roy

Attachment

cc (e-mail only): Erica Hamilton, Commission Secretary
Registered Parties

1.0 Reference: BCUC IR 1.3.4 and BCUC IR 1.6.1

1.1 Would TGI ever consider negotiating terms with a particular customer that did not provide for the recovery of all incremental costs caused by the customer, including return on and return of assets, plus a contribution to system costs? Please explain fully.

Response:

TGI is proposing to have "take or pay" rates structured so that it recovers the forecast cost of service occurring during the initial contract term. There will still be unrecovered costs at the end of the term unless the term is as long as the life of the underlying facility assets. Potential customers are unlikely to agree to a fixed term of that length because it requires them to take on considerable volume risk under the "take or pay" contract. In most cases, customers will expect a term as long as the expected life of their vehicle assets. Renewals will reduce or potentially eliminate the risk and achieve full recovery of all incremental costs, as will provisions like the one in the WM Agreement that require the customer to pay to TGI the unrecovered amount if there is no renewal.

The contribution to system costs flows from the additional use of gas secured by the "take or pay" volume. The benefits secured from this during the life of a contract, even with a relatively short term, might well exceed the value of the assets potentially at risk at the end of the contract. In such cases, customers are benefitting even where assets are stranded. Thus, the risk posed by stranding is only that the ratepayer benefit won't be quite as large as it otherwise would have been had the CNG/LNG service costs also been recovered in full. The only real downside risk to customers in such circumstances is that the potential for the customer to default during the initial term, thus negating the contribution to system costs. TGI has credit review processes in effect to mitigate this potential (please see CEC IR 2.9.1 in that regard).

There is actually less risk associated with adding a creditworthy NGV customer than there is when adding other non-NGV customers through main extensions. The reason is that the MX test for system extensions is based on forecast volumes and the customers are not subject to a minimum contract demand. NGV customers must pass the MX test for distribution system extensions if necessary, but also meet the criteria in Section 12B of the GT&Cs. These require CNG/LNG service customers to agree to a "take or pay" volume, thus securing a contribution to system costs. In the responses to CEC IR 2.2.1 and 2.2.2, TGI explains why it believes that requiring more security of new NGV customers than other new commercial and residential customers is fair at the present time.

2.0 Reference: BCUC IRs 1.9.6, 1.9.7, 1.9.8, and 1.9.9

2.1 Please identify the risks that TGI's shareholder is bearing under the proposal that justify the shareholder rewards sought under the proposal.

Response:

TGI's shareholder only "benefits" from the proposal in the sense that it earns an allowed return on equity on the capital it has invested in facilities used to provide NGV service. The risks for which TGI is compensated are the same as in any instance where capital is invested in the Utility. These risks are recognized and compensated through the requirement to provide the shareholder with an opportunity to earn a fair return. The fair return is determined, in practice, in an ROE proceeding.

Declining throughput and use per customer among traditional gas users represents a challenging business risk for TGI and is contributing directionally to a requirement for a higher ROE on invested capital (all else equal). It is incumbent on the utility to do what it can to mitigate such risks. Investing in the ability to promote and serve the NGV market is one way that TGI is seeking to mitigate the increasing business risk facing TGI by building cost effective load.

By pursuing increased throughput related to NGV service, TGI is attempting to reduce the longterm business risk for customers and TGI's shareholder. With little opportunity to increase total throughput from traditional sources, this service offering is one of the few ways in which cost effective load can be built given government GHG policies. It is consistent with British Columbia's energy objectives, mitigates load erosion and related rate pressure, and contributes in a positive way to TGI's competitive position and benefits all customers.

2.2 Please provide an analysis that shows the estimated payback period from WM's point of view that is reflected in the current arrangements (including incentive payments and forecasted or estimated fuel savings, capital cost differentials, other O&M cost differentials, etc.,) assuming minimum contract demand. Please make explicit any other required assumptions.

Response:

Terasen Gas cannot speak for Waste Management, nor provide their point of view. Terasen Gas believes that Waste Management has chosen to accept the terms and conditions contractually offered to them in part due to an economic benefit that will accrue to Waste

Management as a result of that decision, but TGI is not in a position to speculate as to the specifics of that economic benefit.

Terasen Gas has provided some guidance on what a theoretical customer might see as the business plan for NGV conversion in the text of the Application. Section 3.2.1.1 speaks to the potential payback period for new NGV vehicles based on fuel savings, which is further elaborated on in Section 3.2.1.2.

3.0 Reference: BCUC IR 1.10.6

3.1 Upon expiry of the current contract, in the event that WM does not agree to a contract extension and there is no other customer for the services that were previously provided to WM (i.e., the assets are stranded), what would be the estimated value of all of the assets thus stranded? For the purpose of this IR, please assume that WM takes its minimum contract demand over the life of the contract and explicitly make any other assumptions required in the analysis.

Response:

As stated on page 65 of the Application, 50% to 70% of the plant costs are portable and can removed and relocated somewhere else. At the end of 10 years 50% of the asset value (excluding capitalized overhead) would have been depreciated and recovered in rates; leaving 50% of the asset cost not yet recovered. Of the 50% of unrecovered asset costs only 30% to 50% would be potentially stranded (15% to 25% of the original asset cost). Therefore, using the $700,000 LNG example provided on page 12 of the Application this would result in approximately $105,000 - $175,000 ($700,000 x 50% x 30% and $700,000 x 50% x 50%) in assets.

The WM Agreement includes a clause requiring the customer to pay for the undepreciated plant costs (net book value of the assets) should WM determine not to renew the contract for a further 10 years (i.e. to extend the contract term to match the life of the assets). The net book value of the assets, including capitalized overhead, at the end of the initial 10 year term, has been pre-calculated and specified in Clause 9(c) of the WM Agreement. Since this provision results in the full recovery of the net book value, there are no stranded assets. The risk to customers of stranded WM fueling station assets is thus limited to the hypothetical risk that WM will default on its obligation to pay TGI the undepreciated net book value if it does not renew. TGI has every expectation that WM will honour its obligations under the WM Agreement, thus protecting existing customers from stranded assets.

Please see the response to BCUC IR 2.9.2.

4.0 Reference: BCSEA IR 1.6.1

4.1 Please provide an update with respect to completion of the fueling station.

Response:

Please see TGI’s response to BCSEA IR 2.12.1.

5.0 Reference: Exhibit B-1-3, December 20, 2010 Amended Evidence, Application, Section 8.4, page 70

5.1 What rate of return or interest would the proposed rate base deferral account attract?

Response:

The approved TGI return on rate base is applied to the mid-year balance of all TGI rate base deferral accounts. Consistent with this treatment, the approved TGI return on rate base will be applied to the mid-year balance of the proposed rate base deferral account set up to capture the incremental CNG and LNG Service revenue from volumes in excess of minimum contract demand. The 2011 TGI return on rate base is 7.93% and is described on page 61 of the Application.