



ERICA HAMILTON
COMMISSION SECRETARY
Commission.Secretary@bcuc.com
web site: <http://www.bcuc.com>

SIXTH FLOOR, 900 HOWE STREET, BOX 250
VANCOUVER, BC CANADA V6Z 2N3
TELEPHONE: (604) 660-4700
BC TOLL FREE: 1-800-663-1385
FACSIMILE: (604) 660-1102

Log No. 40567

VIA EMAIL

gas.regulatory.affairs@fortisbc.com

September 17, 2012

Ms. Diane Roy
Director, Regulatory Affairs – Gas
FortisBC Energy Inc.
16705 Fraser Highway
Surrey, BC V4N 0E8

Dear Ms. Roy:

Re: FortisBC Energy Inc.
An Application to Recover Final Project Costs
in the Fraser River South Arm Crossing Upgrade Project

Further to your April 30, 2012 filing regarding the above-noted application, enclosed please find Commission Order G-122-12 and Reasons for Decision.

Yours truly,


Erica Hamilton

TS/dg

Enclosures

cc: Leigha Worth, British Columbia Public Interest Advocacy Centre
(lworth@bcpiac.com)
Tannis Braithwaite, British Columbia Public Interest Advocacy Centre
(Tbraithwaite@bcpiac.com)

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**BRITISH COLUMBIA
UTILITIES COMMISSION**

**ORDER
NUMBER G-122-12**

TELEPHONE: (604) 660-4700
BC TOLL FREE: 1-800-663-1385
FACSIMILE: (604) 660-1102

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

and

An Application by FortisBC Energy Inc.
for Approval of a Negotiated Settlement Agreement in the
Fraser River South Arm Crossing Upgrade Project
between FortisBC Energy Inc. and North American Pipelines Inc.

BEFORE: L.F. Kelsey, Commissioner
N.E. MacMurchy, Commissioner September 13, 2012
B.A. Magnan, Commissioner
D.M. Morton, Commissioner

O R D E R

WHEREAS:

- A. On November 6, 2008, FortisBC Energy Inc. (FEI) (formerly Terasen Gas Inc.) applied (the Application) to the British Columbia Utilities Commission (the Commission), pursuant to section 45 of the *Utilities Commission Act* (the Act), for a Certificate of Public Convenience and Necessity (CPCN) for two horizontal directional drilled (HDD) natural gas transmission pipeline crossings of the South Arm of the Fraser River between Delta and Richmond near Tilbury Island (the Fraser River South Arm Crossing Upgrade Project or the Project);
- B. On March 12, 2009, the Commission granted a CPCN for the Project by Order C-2-09, subject to a number of conditions, which include requirements that FEI file a quarterly progress report within 30 days of the end of each reporting period and a final report within six months of the end or substantial completion of the Project;
- C. On April 30, 2012, FEI filed a final report (Final Report) for the Fraser River South Arm Crossing Upgrade Project in compliance with Order C-2-09, reporting that during the fourth quarter of 2011, the prime contractor for the Project - North American Pipelines Inc. (North American) substantially completed field construction of both pipeline crossings which were placed into service on October 22, 2011 (NPS 20) and on December 3, 2011 (NPS 24). North American cleaned up the site and de-mobilized on December 12, 2011;
- D. The Final Report also reports that FEI and North America have reached a Settlement Agreement relating to disputes arising from the construction and installation of the HDD, which include provisions releasing FEI from any further claims from North American and North American indemnifying FEI from any claims by third parties, a guarantee of North American's obligations secured from North American's parent company, and a condition precedent that the Settlement Agreement be approved by the Commission, in exchange for a specific settlement amount;

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- E. The Final Report further reports that the final Project cost is \$34 million inclusive of the settlement amount;
- F. FEI requests Commission approval of the Settlement Agreement between FEI and North American and specifically of an amount of \$34 million to be included in FEI's rate base;
- G. By letter dated May 17, 2012, the Commission sought comments from Registered Interveners of the 2012-2013 FortisBC Energy Utilities Revenue Requirements proceeding on the need and form of public review process that the Commission should undertake in order to review for approval the Settlement Agreement and inclusion of the final project costs of \$34 million into rate base;
- H. The British Columbia Old Age Pensioners' Organization (BCOAPO) responded, requesting a written public review process and willingness to enter into an undertaking of confidentiality;
- I. On June 29, 2012 by Order G-93-12, the Commission established a written hear process, agreeing to keep the Settlement Agreement, Final Report and proceeding material confidential during the proceeding with BCOAPO as the only Intervener;
- J. The Commission has reviewed the submissions in the proceeding, Final Report and the Settlement Agreement and determines that the Settlement Agreement should be approved and \$34 million should be allowed in rate base.

NOW THEREFORE pursuant to sections 59 to 61 of the *Utilities Commission Act*, the Commission orders, for the reasons set out in the Reasons for Decision attached as Appendix A to this Order, that:

- 1. The Settlement Agreement is approved.
- 2. The \$34 million is included in rate base pursuant to the financial schedules filed in accordance with Item 15 of Commission Order G-44-12.
- 3. The Commission agrees to keep the Settlement Agreement and the Final Report confidential.
- 4. FEI is directed to file a redacted publicly available Final Report to the Commission within 30 days of the date of this Order and post on its website.

DATED at the City of Vancouver, in the Province of British Columbia, this 17TH day of September 2012.

BY ORDER



D.M. Morton
Commissioner

Attachments

An Application by FortisBC Energy Inc.
for Approval of a Negotiated Settlement Agreement in the
Fraser River South Arm Crossing Upgrade Project
between FortisBC Energy Inc. and North American Pipelines Inc.

REASONS FOR DECISION

INTRODUCTION

On March 12, 2009, the British Columbia Utilities Commission (Commission) granted FortisBC Energy Inc. (FEI) a Certificate of Public Convenience and Necessity (CPCN) by Order C-2-09 for two horizontal directional drilled (HDD) natural gas transmission pipeline crossings of the South Arm of the Fraser River between Delta and Richmond (Project). As part of its approval, FEI was required to file quarterly progress reports within 30 days of quarter end and a final report within six months of project completion. The Project encountered problems with the HDD of both pipelines which resulted in a project delay of 22 months and significant additional FEI and its contractors costs over the approved total project cost estimate of \$29.751 million. FEI submitted a final report (Final Report) to the Commission on April 30, 2012 reporting that during the fourth quarter of 2011 the prime contractor for the Project – North American Pipelines Inc. substantially completed the field construction of both pipeline crossing which were placed into service on October 22, 2011 (NPS 20) and December 3, 2011 (NPS 24). The Final Report also reported that FEI and North American had reached a Settlement Agreement relating to disputes arising from the problems encountered with the HDD and requested that the Commission approve the final Project costs of \$34 million for the Fraser River South Arm Upgrade Project including a Settlement Agreement of \$2.475 million payable by FEI to North American (Application).

REGULATORY PROCESS

In reviewing of the Final Report and Application, the Commission sought comments from Registered Interveners of the 2012-2013 FortisBC Energy Utilities (FEU) Revenue Requirements proceeding.

The British Columbia Old Age Pensioners' Organization (BCOAPO) intervened, requesting a written hearing process and agreed to enter into an undertaking of confidentiality to have access to the confidential filings and proceeding. By Order G-93-12, the Commission established the Regulatory Timetable which was amended by Order G-95-12 and is attached as Appendix B to this Order.

PROCEEDING ISSUES

The final project cost of \$33.946 million inclusive of the settlement agreement represents a variance of \$4.195 million or 14.1 percent over the P(50) cost estimate approved by the CPCN of \$29.751 million. The final project cost represents a \$1.467 million or 4.5 percent variance over the P(90) cost estimate.

| Cdn \$(000) | Control Budget at (Jul 30/09) | Spent to Date | Total at Completion | Variance from Control Budget |
|------------------------------|-------------------------------|---------------|---------------------|------------------------------|
| Pre CPCN Expenditures | \$ 450 | \$ 450 | \$ 450 | - |
| Performance Measure Baseline | \$29,581 | \$ 30,231 | \$33,456 | (\$4,775) |
| Total Project Cost (TPC) | \$29,751 | \$ 30,676 | \$33,946 | (\$4,195) |
| | | | | |
| P(50) Cost | \$29,751 | | | |
| P(90) Cost | \$32,479 | | | |

(Table 4-1 from FEI Final Report)

The Project incurred 22 months of delay on the 12-month construction phase of the Project. The significant delay and additional costs over the estimate were substantially the result of two major problems experienced on the Project.

1. January, 2010, NPS 20 HDD Failure

Failure occurred during reaming process by sub-contractor which left 1 km of drill pipe abandoned, sub-contractor abandoned site, new NPS 20 path had to be designed.

2. July, 2010, NPS 24 HDD Failure

Failure occurred during the pull-back of the NPS24 pipeline which left the 1.35 km of pipe pull short with the end at a depth of 18 metres. (Exhibit B-16, p. 27) As a result of the NPS 24 Failure a coffer-dam excavation and extensive water management was needed to connect to the buried end and finalize the connection to the existing line.

FEI continued to evaluate project progress and project management activities closely during these issues and delays as documented in its quarterly reports to the Commission including ensuring that other stake-holders and land-owners impacted by the worksite were kept informed and inconvenienced as little as possible. In its first quarter 2010 report, FEI reported the first NPS 20 HDD failure and included a revised estimate for project completion of \$36.283 million.

The Final Report and evidence in the proceeding confirms that the two pipeline crossings were completed, put into service in December, 2011 and both pipelines meet the original design intent and specification as verified by independent engineering evaluation. (BCUC 1.1.1 & Attachment 1.1)

Several potential issues were raised in the written hearing process and final argument from BCOAPO (name changed to the British Columbia Pensioners' and Seniors' Organization [BCPSO]) with discussion below.

- 1) BCPSO was concerned with changes that were made to the primary contract resulting from North American, the primary contractor, requesting changes to accommodate the HDD sub-contractors about 100 days after the primary contract was executed and prior to the HDD sub-contractor agreement with the primary. BCPSO states that without independent expert evidence about HDD drilling, it is not in a position to comment on whether the changes to the contract, made about 100 days after it was signed and one month before the first HDD failure, amounts to imprudence. (BCPSO Final Argument, p. 2)
- 2) BCPSO also raised concerns that FEI did not enforce other elements of the contract relating to the design tender, allowing the sub-contractor to bypass the drilling of the intermediate 20" ream as originally required. The NPS 20 failure occurred during the reaming process where the sub-contractor proceeded with a 30" ream step. BCPSO argue that "logic suggests that concerns over changes to sub-surface conditions would warrant a more cautious approach to a technically advanced process, while bypassing an intermediate step would appear to be less cautious." BCPSO submits that the Commission should consider these factors and question FEI's presumed prudence in this matter. (BCPSO Final Argument, p. 2)

FEI, in its reply submission addressed the 'presumed prudence' raised by BCPSO by citing *Enbridge v. Ontario* that the burden to demonstrate 'reasonable grounds' to question the prudence of FEI's decisions is with BCPSO. FEI makes the following reply arguments specifically on the issues raised by BCPSO.

Changes to primary contract

FEI explains that when considering contracting for construction work, FEI reviews its options and determines the optimum balance between transfer of risks to the prime contractor, cost certainty and cost minimization. (FEI, Reply Submission, p. 2; footnote 3, BCPSO 1.1.4) When it amends a contract it follows the same principles. Additionally, as in the original contracting, FEI sought the advice of a leading external construction lawyer with respect the amendments. (FEI Reply Submission, p. 3; footnote 4, BCPSO 1.3.4) FEI further argues that the amendments made were to provide greater clarity with respect to the responsibility between FEI and the prime

contractor and that given the prime contractor did complete both crossings, the amendments did not have an effect on the final outcome of the project. (FEI Reply Submission, p. 3)

Intermediate 20" Reaming

FEI explains that its prime contractor, North American, is responsible for the detailed construction methodology used (FEI Reply Submission, p. 3; footnote 5, BCPSO 1.4.1) and that FEI relies on the experts in the field to review the drilling plan. FEI therefore submits that there is no reasonable ground to suggest that FEI acted imprudently with respect to the construction methodology chosen by the prime contractor. (FEI Reply Submission, p. 3)

COMMISSION DETERMINATION:

The Commission recognizes that FEI has completed the Fraser River South Arm Crossing Upgrade Project by installing two HDD pipelines that meet FEI and industry standards in order to provide a reliable major system upgrade to FEI's system as outlined in the original CPCN. The Commission accepts that FEI provided timely and fulsome quarterly updates and Final Report and demonstrated active and competent project management of a complex HDD project. In considering the Application to accept the settlement agreement and final costs of the project, the Commission has to first determine if there are reasonable grounds that FEI acted imprudently in its decisions and management of the Project.

The Commission determines that the evidence does not support a reasonable grounds proof that FEI acted imprudently in its decisions and management of the Project.

The Commission therefore accepts the Final Report and costs of \$34 million for the Fraser River South Arm Upgrade Project including a Settlement Agreement of \$2.475 million.

An Application by FortisBC Energy Inc.
to Recover Final Project Costs
in the Fraser River South Arm Crossing Upgrade Project

REVISED REGULATORY TIMETABLE

| ACTION | DATE (2012) |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------|
| FEI and BCOAPO execute a undertaking of Confidentiality and FEI provides Compliance Reports and Settlement Agreement to BCOAPO as Intervener | Friday, July 6 |
| FEI Workshop to present Project summary, Final Report and Settlement Agreement. Location: BCUC Hearing Room – 900 Howe St, 6 th Floor Time: 9:30 am to 11:30 am (to be confirmed with Participants) | Wednesday, July 11 (Revised) |
| Commission and Intervener Information Request No. 1 | Friday, July 20 |
| Response to Commission and Intervener Information Request No. 1 | Tuesday, August 7 (Revised) |
| FEI Final Submission | Monday, August 13 |
| Intervener Final Submission | Monday, August 20 |
| FEI Reply Submission | Monday, August 27 |