CANADA

National Energy Board

Reasons for Decision

Westcoast Energy Inc.

RH-5-94

June 1995

Tolls

National Energy Board

Reasons for Decision

In the Matter of

Westcoast Energy Inc.

Application dated 21 October 1994,
as amended, for new tolls effective
1 January 1995

RH-5-94

June 1995

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Abbreviations

ACAP	Attrition Capacity Allocation Program
Act	*National Energy Board Act*
AFUDC	allowance for funds used during construction
BC Gas	BC Gas Utility Ltd.
Bcf	billion cubic feet
Board	National Energy Board
CAPP	Canadian Association of Petroleum Producers
COFI	Council of Forest Industries of British Columbia, Methanex Corporation and Cominco Ltd.
Company	Westcoast Energy Inc.
ESDP	Expansion Service Delivery Policy
EUG	Export Users Group
GST	Goods and Services Tax
GPIS	gas plant in service
NrG	NrG electronic bulletin board
NEB	National Energy Board
NPIS	net plant in service
O&M	operating and maintenance
QP&AC	Queuing Procedures and Access Criteria
TTTF	Toll and Tariff Task Force
Westcoast	Westcoast Energy Inc.

Definitions

(Explanation for certain terms used in these Reasons which appear infrequently in Board reports or which may be applicable to Westcoast only are provided for the reader's convenience)

attrition capacity	Firm service that becomes available for any reason other than the construction of additional facilities.
compa-ratio	Comparison of actual salaries paid to Westcoast employees to salary grade reference point set by the market.
DEALS	A process to transact business on the Westcoast system based on software that allows shippers to create their own buying and selling arrangements each day and to transmit them electronically to Westcoast for processing.
RH-2-87	Hearing Order in respect of Westcoast's application for new tolls effective 1 January 1987 and 1 January 1988.
RH-3-91	Hearing Order in respect of an application by Trans Mountain Pipe Line Company Ltd. for new tolls effective 1 January 1992.
RH-1-92	Hearing Order in respect of Westcoast's application for new tolls effective 1 January 1992.
RH-2-93	Hearing Order in respect of Westcoast's application for new tolls effective 1 January 1994.
RH-2-94	Multi-Pipeline Cost of Capital Hearing.
SHARE program	A program previously used by Westcoast to improve processes.
swing gas	Gas used by Westcoast to deal with gas imbalances on its system. When linepack is too low, so that additional gas is required, Westcoast will either borrow swing gas at a fee and later return it to the borrower, or purchase swing gas and later resell it.
TGI-2-94	Order which established interim tolls for Westcoast effective 1 January 1995.

Recital and Appearances

IN THE MATTER OF the *National Energy Board Act* and the Regulations made thereunder; and

IN THE MATTER of an application by Westcoast Energy Inc. for certain orders respecting interim and final 1995 tolls pursuant to subsection 19(2) and Part IV of the Act; and

IN THE MATTER OF the National Energy Board Hearing Order No. RH-5-94.

HEARD at Vancouver, British Columbia on 24, 25, 26, 27, 28 April and 1 and 2 May 1995.

BEFORE:

R. Illing	Presiding Member
R.L. Andrew	Member
J.A. Snider	Member

APPEARANCES:

J.W. Lutes R.M. Sirett	Westcoast Energy Inc.
M. Coppock	British Columbia and Yukon Territory Building and Construction Trades Council
H.R. Ward	Canadian Association of Petroleum Producers
D. Bursey	Council of Forest Industries, Methanex Corporation, and Cominco Ltd.
A.K. Fung D. G. Cowper	BC Gas Utility Ltd.
R.B. Beattie	CanWest Gas Supply Inc.
M.M. Moseley F.J. Weisberg	Export Users Group
R.R. Moore	Imperial Oil Resources Limited
C.B. Woods	Mobil Oil Canada
C. Worthy	Norcen Energy Resources Limited
N. Mills	NOVA Gas Transmission Ltd.

C. Hart	PanCanadian Petroleum Limited
S.R. Miller R. Cameron	Petro-Canada
D.R. Sutton	Shell Canada Limited
F.C. Basham	Talisman Energy Inc.
D. Green	British Columbia Ministry of Energy, Mines and Petroleum Resources

Overview

(Note: This overview is provided for the convenience of the reader and does not constitute part of these Reasons for Decision. For details the reader is referred to the relevant sections of the Reasons for Decision)

Tolls and Revenue Requirement for 1995

The Board estimated that final tolls for a typical export service movement for 1995 will be approximately 5.6% higher than the 1994 tolls.

The Board also estimated that the approved revenue requirement for 1995 will be approximately $448.1 million, or $10.3 million less than the applied-for amount of $458.4 million.

Rate Base

The Board approved a rate base estimated at $1,805.4 million for the test year.

Rate of Return

In the RH-2-94 Decision, the Board approved a rate of return on common equity of 12.25% for Westcoast for 1995. This represents an increase of 75 basis points over the previously approved rate of 11.50% for 1994.

Operating Costs

For 1995, the Board approved global O&M expenses of $135.2 million, or $3.4 million less than the applied-for amount of $138.6 million.

The Board found the Corporate Centre fee of $4.4 million to be reasonable.

Toll Design and Tariff Matters

The Board approved the proposed modifications to the General Terms & Conditions for contract demand credits.

The Board also approved Westcoast's request to replace its existing Queuing Procedures & Access Criteria with its proposed Expansion Service Delivery Policy, and to amend the General Terms & Conditions by adding the Attrition Capacity Allocation Program.

Chapter 1

Background and Application

By application dated 21 October 1994, Westcoast Energy Inc. ("Westcoast" or "the Company") applied to the National Energy Board ("NEB" or "Board") under subsection 19(2) and Part IV of the *National Energy Board Act* ("Act") for an order or orders respecting interim and final tolls for 1995. On 21 November 1994, the Board issued Hearing Order RH-5-94 which set down Westcoast's application for a hearing commencing 13 March 1995 and established the Directions on Procedure and the list of issues.

On 9 December 1994, the Board issued Order TGI-2-94 authorizing Westcoast to charge, on an interim basis effective 1 January 1995, tolls that would yield an increase in a typical service movement from Zone 1 to the export point of Zone 4 of 5% over the 1994 approved tolls. Order TGI-2-94 remained in effect until the Board rendered its final decision on Westcoast's application for 1995 tolls.

On 16 January 1995, Westcoast requested that the Board adjourn the commencement of the RH-5-94 proceeding until the latter part of April and make such consequent amendments to the hearing timetable as may be appropriate. After considering comments from interested parties, the Board decided to issue Order AO-1-RH-5-94 adjourning the commencement of the RH-5-94 proceeding until 24 April 1995 and amending the other filing deadlines for the proceeding.

The RH-5-94 proceeding was held in Vancouver, British Columbia and lasted seven days, from 24 April 1995 to 2 May 1995.

Chapter 2

Revenue Requirement for 1995

The net revenue requirement authorized by the Board for the 1995 test year is $448,102,000. This amount is subject to final determinations as indicated in Chapter 9. A summary of the approved revenue requirement together with the Board's adjustments is shown in Table 2-1.

Table 2-1
Revenue Requirement for the 1995 Test Year
($000)

	Application	NEB Adjustments	Approved by NEB (Estimated)
Operating and Maintenance	138,552	(3,394)	135,158
Regulatory Costs	2,405	-	2,405
Depreciation	55,808	(288)	55,520
Amortization	320	-	320
Taxes Other Than Income Taxes	65,763	-	65,763
Miscellaneous Operating Revenue	(825)	-	(825)
Insurance Deductibles	459	-	459
Foreign Exchange on Debt	1,366	-	1,366
Gas Substitution Costs	2,300	-	2,300
Gas Used in Operations	1	-	1
Income Tax Expense	5,406	-	5,406
Return on Rate Base	201,641	(6,656)	194,985
Gross Revenue Requirement	473,196	(10,338)	462,858
Deferrals	(14,756)	-	(14,756)
Net Revenue Requirement	**458,440**	**(10,338)**	**448,102**

Chapter 3

Rate Base

A summary of the 1995 applied-for and 1995 approved (as estimated by the Board) rate bases is shown in Table 3-1. The Board has made adjustments to certain 1995 rate base items as discussed in this chapter, resulting in an estimated 1995 rate base of $1,805,412,000.

3.1 Gas Plant in Service

3.1.1 Plant Additions Transferred to Gas Plant in Service

In respect of plant additions during the test year, Westcoast provided a list of construction projects that it expected to complete in 1995 and also forecast amounts of completed plant costs transferred each month to gas plant in service ("GPIS"). As of the date of the application for 1995 tolls, some of the listed projects had not been approved by the Board under Part III of the Act and, in some cases, the application had not yet been filed.

Views of the Board

The Board is of the view that, for the purposes of determining plant additions to GPIS during the test year, it should use the most current information available. Accordingly, the Board is prepared to accept for inclusion in forecast plant additions, only those projects which have been approved under Part III of the Act at the time that the Board rendered its decision in this proceeding.

Decision

The Board directs Westcoast to remove from the applied-for GPIS the forecast amounts for projects which, as of 14 June 1995, have been denied or have not been approved by the Board under Part III of the NEB Act.

3.1.2 Net Plant in Service Adjustment

Westcoast applied for a change in the methodology for calculating the net plant in service ("NPIS") adjustment. Under the existing methodology, approved in the RH-2-87 Decision, a five-year average error factor is calculated from the variances between the forecast and actual net plant in service and then applied to the forecast net plant in service. The Company proposed that the error factor be calculated from the variances between the authorized net plant in service and actual net plant in service.

Westcoast contended that the rate base on which it earns return reflects the authorized and not the forecast net plant in service; therefore, it is appropriate that the error factor be calculated with reference to the authorized net plant in service.

Westcoast was asked to comment on whether it would be appropriate to adjust its test-year forecast of plant additions based on the forecasting error experienced in the previous three years, prior to the proposed NPIS adjustment. The Company stated that a second adjustment is unnecessary. The evidence showed that during the past three years the actual transfers to GPIS have exceeded the forecast plant additions by 26%. BC Gas Utility Ltd. ("BC Gas") questioned why the forecasting error was so high. Westcoast explained that the approved forecast of plant additions for a test year did not include projects, such as those filed pursuant to section 58 of the Act, that were approved subsequent to the Board's decision and were completed during the test year.

None of the interested parties expressed concern with Westcoast's proposal.

Views of the Board

The Board accepts Westcoast's contention that, because it earns return on the authorized and not the forecast net plant in service, the NPIS adjustment should be determined from the variances between the authorized and actual net plant in service. Accordingly, the Board finds the applied-for methodology for calculating the NPIS adjustment to be reasonable.

Decision

The Board approves the applied-for methodology for calculating the NPIS adjustment.

Table 3-1
Average Rate Base for the 1995 Test Year
($000)

	Application	NEB Adjustments	Approved by NEB (Estimated)
Gas Plant in Service	2,614,951	(16,784)	2,598,167
Accumulated Depreciation	(764,472)	35	(764,437)
Net Plant in Service Adjustment	1,642	(16)	1,626
Net Plant in Service	1,852,121	(16,765)	1,835,356
Contributions in Aid of Construction	(4,182)	-	(4,182)
Plant Investment	1,847,938	(16,765)	1,831,174
Materials and Supplies	36,250	-	36,250
Line Pack Gas	4,076	-	4,076
Prepaid Expenses	4,255	(981)	3,274
Deferrals	(7,378)	-	(7,378)
Deferred Income Tax	(66,406)	-	(66,406)
Average Rate Base Exclusive of Cash Working Capital	1,818,735	(17,745)	1,800,990
Cash Working Capital	4,422	-	4,422
Average Rate Base[1]	**1,823,156**	**(17,745)**	**1,805,412**

1 Net of Alberta (Zone 5) Facilities

Totals may not add due to rounding

3.1.3 Section 58 Application Process

In any year, Westcoast files a number of separate section 58 applications for large projects and an annual application for minor projects. The Council of Forest Industries, Methanex Corporation, and Cominco Ltd. ("COFI") was concerned that, often, the annual application makes no reference to the large projects. As a result, COFI submitted that, from an interested party’s point of view, it is difficult to track the information as it changes.

COFI requested that Westcoast be required to file a tracking status report that would show: the projects that had been applied for and their status; any changes made to the forecast; and the effects of those projects in the different zones. COFI suggested that this report could be co-ordinated with the production of the five-year system outlook.

Westcoast stated that there would be a cost to preparing such a report. Further, Westcoast stated that it could not comment on the value of such a report, since the request was only raised in argument, and Westcoast had not considered it.

Views of the Board

As COFI raised its request only in argument, the Board finds it difficult to assess the merits of such a request.

Decision

The Board denies COFI's request for a status report for section 58 applications.

3.2 Materials and Supplies

Westcoast applied for a provision for materials and supplies of $36,250,000 for 1995, compared to the 1994 approved amount of $29,953,000. COFI was concerned by the 20% increase in this item and disputed Westcoast's position that significant rate base growth had led to growth in materials and supplies. COFI stated that the levels of capital spending for 1994 and 1995 were comparable and that Westcoast had not justified why there would be a significant increase in the use of materials and supplies. COFI recommended that there be no increase over the 1994 approved amount of $29,953,000.

Westcoast stated that COFI's position ignores the following factors: GPIS will increase by $450,000,000 in 1995; Westcoast is now recording consumable items as part of inventory in materials and supplies; two additional compressors were added in the Southern District; the Pine River Plant is now operating; and between 1990 and 1994 Westcoast had improved the turnover rate of its materials and supplies.

Views of the Board

Considering the increase in GPIS in 1995 and the other factors mentioned by Westcoast, the Board finds the applied-for amount for materials and supplies to be reasonable.

Decision

The Board approves the applied-for amount for materials and supplies.

3.3 Prepaid Expenses

As noted in subsection 5.1.4, Westcoast included the unamortized portion of its strategic planning costs within Rate Base as part of Prepaid Expenses. The unamortized portion of the costs represents approximately $981,000.

Views of the Board

For the reasons given in section 5.1, the Board is of the view that the unamortized portion of Westcoast's strategic planning costs should be removed from the prepaid expenses portion of rate base.

Decision

The Board directs Westcoast to remove the unamortized portion of its strategic planning costs from rate base.

3.4 Cash Working Capital

Westcoast estimated its cash working capital requirement for the 1995 test year, with one exception, according to the methodology approved in the RH-2-93 Decision. At variance with the approved methodology, the Company proposed that the cash working capital calculation should reflect the Goods and Services Tax ("GST") related only to operating and maintenance ("O&M") expenses. Further, the Company proposed that the GST related to capital expenditures should be excluded from the cash working capital calculation and be treated as an item which attracts a carrying charge, similar to the allowance for funds used during construction ("AFUDC"), and which should therefore be capitalized. The Company's latter proposal is dealt with in section 3.5.

Using the approved methodology, Westcoast calculated components of cash working capital in respect of payroll expenses, other O&M expenses, employee payroll deductions and gas purchases. For the component of cash working capital attributed to the GST related to pipeline operations, the Company calculated a negative cash working capital and accordingly adjusted its cash working capital requirement.

In its calculation, Westcoast took into account: the amount of GST paid on the goods and services purchased as O&M expenses; the amount of GST collected from the shippers through tolls each month; and the respective lead/lag days with reference to the GST return day. The GST return day is the last day of the following month when the Company files its GST return with Revenue Canada. Because the amount of 7% GST paid on O&M expenses is much smaller than the amount of 7% GST collected on tolls, the Company remits the balance to Revenue Canada with its GST return. However, the balance is available for the Company's use until it is remitted to Revenue Canada. The negative cash working capital reflects that the weighted dollar-days amount associated with the GST payments is lower than the dollar-days amount associated with the GST collections, and implies that the GST provides a source of funds and reduces the cash working capital requirement.

None of the intervenors expressed concern with the Company's calculation of the cash working capital related to O&M expenses.

Views of the Board

The Board notes that the Company's calculation of cash working capital in respect of O&M expenses is consistent with the methodology approved in the RH-2-93 Decision. The Board also notes that the Company's estimate of a negative cash working capital related to the GST appropriately takes into account the GST paid on operating expenses, and the GST collected on tolls and associated lead/lag days. Accordingly, the Board finds the Company's calculation of its cash working capital requirement to be reasonable.

Decision

The Board approves the applied-for methodology for estimating the cash working capital.

3.5 GST related to Capital Projects

Westcoast proposed that the GST paid on goods and services related to capital projects should be treated as an item which attracts a carrying charge, similar to AFUDC, and should become part of the project cost included in the rate base. The Company would recover the capitalized AFUDC through depreciation over the life of the project while earning a return on the undepreciated amount reflected in the rate base.

To calculate the amount of GST payable each month, the Company used the forecast amounts of capital additions for each month in the test year, added 50% of the overhead during construction and applied the 7% GST rate to the total. Assuming that it would be reimbursed by Revenue Canada 60 days later for the GST paid in any one month, Westcoast computed the outstanding balance for each month in the test year. The Company used an AFUDC rate of 11.06%, which is equal to the rate of return on rate base, and calculated an AFUDC amount of $713,000 on GST receivables related to capital projects.

The Company indicated that a GST return is required to be filed for a reporting month on the last day of the following month showing the amounts of GST paid and collected. The Company is required to remit any balance to Revenue Canada with its GST return, or it may claim a refund which is paid by Revenue Canada 25 days after the filing. However, in its calculations of the carrying charges, the Company assumed that the GST receivable balances remain outstanding for 60 days.

The evidence showed that, had the Company included the GST on capital projects in the calculation of cash working capital pursuant to the approved methodology, its cash working capital would have been $5,318,000 higher; therefore, its return on rate base would have been $588,000 higher. In other words, under the approved methodology, the $588,000 amount would have been included in the test-year revenue requirement and collected through tolls during the test year. Under the proposed methodology, the AFUDC amount of $713,000 would be capitalized and recovered through depreciation. As estimated by the Company, the impact on the test-year revenue requirement, including depreciation and return, would be $94,000. The Company acknowledged that with the proposed change in methodology the benefit accruing to the Company would amount to a present value of $116,000.

None of the intervenors opposed Westcoast's proposal to capitalize the AFUDC carrying charge related to the GST on capital projects. However, COFI expressed concerns with the calculation of the AFUDC. COFI recommended that Westcoast's AFUDC calculation should be changed to reflect the actual practice that Westcoast uses; that is, it only pays net GST after it offsets the GST credits to which it is entitled. In COFI's estimate the AFUDC would need to be reduced by more than $500,000.

In reply argument, Westcoast refuted COFI's suggestion and noted that the GST collected on revenues was already credited in the calculation of cash working capital. Therefore, using the credit again on the AFUDC calculation would be unreasonable.

Views of the Board

The Board finds Westcoast's proposal to capitalize, as part of the project cost, the carrying charges on the GST receivables related to capital projects, to be reasonable. The Board notes that the Company has appropriately reflected the average GST receivables in the total capitalization and calculation of the rate of return on rate base. Therefore, the Board accepts the calculation of the carrying charges using the rate of return on rate base.

The Board rejects COFI's suggestion that Westcoast's AFUDC calculation should be reduced by $500,000 to reflect the GST on revenues. As mentioned in section 3.4, the Company has appropriately taken into account the GST on revenues in the calculation of the cash working capital.

The Board notes, however, that with the proposed change in the treatment of the GST on capital projects, a benefit of $116,000 may accrue to the Company. It appears to the Board that this arises because of Westcoast's assumption that GST receivable balances remain outstanding for 60 days rather than for 55 days.

Decision

The Board approves the proposed treatment of the GST on capital projects.

3.6 Facilities Planning

During cross-examination, the Export Users Group ("EUG") questioned Westcoast on its facilities planning processes and documents, particularly the five-year system outlooks. In argument, EUG stated that, while Westcoast had taken some initiatives to improve its planning activities, there was still room for improvement. EUG advised the Board that its members were willing to work with Westcoast to improve Westcoast's planning processes and planning documents. Also, EUG stated that its members were prepared to discuss with Westcoast the kind of facilities that should be built by the regulated utility as opposed to some other entity. EUG requested that the Board comment on the importance of Westcoast's planning activities and on the desirability of having these kinds of discussions so as to develop the necessary improvements.

Views of the Board

The Board continues to believe that, in planning for facilities, Westcoast should take into account the requirements and views of the suppliers and shippers of gas as well as those of the distributors and other marketers of gas. The Board encourages the participation of the various stakeholders in the facilities planning process. However, the Board refrains from specifying the manner and the degree of such participation, by EUG or any other party, that may be considered desirable or necessary.

Chapter 4

Capital Structure and Cost of Capital

In the RH-2-94 proceeding, held between 24 October and 20 December 1994, the Board examined cost of capital issues for a number of pipelines that it regulates, including Westcoast. Only the relevant decisions from that proceeding, which were released on 11 April 1995, have been brought forward and incorporated in these Reasons. Details on the Board's views on these items can be found in the Board's Reasons for Decision for the RH-2-94 proceeding.

Westcoast applied for a rate of return on rate base of 11.06% for the 1995 test year, based on a deemed common equity component of 35%. Details of the applied-for capital structure and requested rates of return are shown in Table 4-1.

Table 4-1
Applied-for Deemed Average Capital Structure and Rates of Return for the 1995 Test Year

	Amount ($000)	**Capital Structure** (%)	**Cost Rate** (%)	**Cost Component** (%)
Debt - Funded	1,155,939	55.42	10.15	5.62
- Unfunded	164,841	7.90	9.60	0.76
Total Debt Capital	1,320,780	63.32		6.38
Preferred Share Capital	34,960	1.68	7.91	0.13
Common Equity	730,014	35.00	13.00	4.55
Total Capitalization	**2,085,753**	**100.00**		
Rate of Return on Rate Base				**11.06**

4.1 Funded Debt

Westcoast applied for a rate of 10.15% on a forecast funded debt balance of $1,155,939,000 for 1995. The dollar amount of funded debt and the associated cost rate were determined using the net proceeds methodology approved by the Board in the RH-1-90 Reasons for Decision. No intervenor objected to the applied-for amount of funded debt and the associated cost rate.

Decision

The Board approves the applied-for funded debt amount of $1,155,939,000 at a cost rate of 10.15% for the 1995 test year.

4.2 Unfunded Debt Rate

Westcoast applied for a cost rate of 9.60% for unfunded debt, on a balance of $164,841,000 for the 1995 test year. Westcoast used the blended rate methodology approved by the Board in the RH-2-93 Reasons for Decision where the unfunded rate reflects financing by both long- and short-term instruments.

Westcoast stated that it determined the applied-for short-term debt interest rate of 8.15% based on its forecast of a rate of 7.7% on 91-day Treasury Bills, plus a spread of 45 basis points. In forecasting the Treasury Bill rate, Westcoast relied on quarterly forecasts prepared by large Canadian brokerage houses and banks. On the other hand, the 45 basis point spread represents the average differential of 15 basis points over the period 1990 to 1994 between 91-day Treasury Bills and 30-day commercial papers, and a 30 basis point spread reflecting Westcoast's issue costs. Westcoast added, however, that the actual point spread related to issue costs was 28 basis points.

In responses to information requests, Westcoast stated that its actual borrowing rates for the first three months of 1995 were, respectively, 6.5%, 7.69% and 8.33%. It also provided data for 1993 and 1994 that showed that its actual borrowing rates in several months, particularly in 1994, were lower than the equivalent monthly average 91-day Treasury Bill rates.

COFI opposed Westcoast's approach. It filed an exhibit which demonstrated that Westcoast's actual results over the years 1993 and 1994 are almost consistently below Westcoast's proposed rate of Treasury Bills rate plus 45 basis points. COFI recommended that the best data to use as proxy for 1995 are that of 1994, where Westcoast's actual short-term borrowing rate averaged the forecast rate for Treasury Bills minus approximately 10 basis points. COFI thus recommended that, based on Westcoast's forecast rate of 7.7% for 91-day Treasury Bills, the Board approve a short-term interest rate of 7.6% for the 1995 test year.

Views of the Board

While Westcoast used the same methodology in forecasting the short-term debt interest rates as in the RH-2-93 hearing, the methodology tends to over-estimate actual rates at which Westcoast accesses funds. The Board particularly notes that the Company's average actual borrowing rates for the first three months of 1995 stood at 7.51%, which is not only lower than the applied-for rate of 8.15% but is also lower than the average Treasury Bill rate of 7.89% forecast by financial institutions for the first quarter of 1995. The Board also notes evidence to the effect that the Company's actual borrowing rates in certain months of 1994 were lower than the corresponding average 91-day Treasury Bill rates for these months.

The Board further notes that the adjustment for commercial paper borrowing seems to rely on the market as a whole, without specific reference to Westcoast borrowing power, and that the adjustment for issue costs seems to be based on the Company's past experience. The Board finds that Westcoast's analysis in both areas could be improved.

Considering the above comments and that the forecast relies on a number of estimates, the Board finds that Westcoast's short-term debt interest costs should be reduced to the rate of 8.0%. The effect of this change is to reduce the unfunded debt rate from 9.60% to 9.58%.

Decision

The Board approves an unfunded debt cost rate of 9.58% for the 1995 test year.

4.3 Preferred Shares

Westcoast continued to allocate the full amount of 7.68% preferred shares to its utility operations regulated by the Board. Using the modified net proceeds methodology approved in the RH-2-89 Reasons for Decision, Westcoast applied for a cost rate of 7.91% on a preferred share balance of $34,960,000 for the 1995 test year.

No intervenor objected to the applied-for amount of preferred share capital and the associated cost rate.

Decision

The Board approves the applied-for preferred share capital amount of $34,960,000 at a cost rate of 7.91% for the 1995 test year.

4.4 Common Equity Ratio

Westcoast applied for a deemed common equity ratio of 35% for the 1995 test year. In the RH-2-94 Decision, the Board approved the continuation of that ratio for Westcoast.

4.5 Rate of Return on Common Equity

Westcoast applied for a rate of return on common equity of 13.0% for the 1995 test year. In the RH-2-94 Decision, the Board approved the lower rate of 12.25% for Westcoast.

4.6 Rate of Return on Rate Base

Decision

Based on the decisions contained in these Reasons for Decision, the Board has estimated a rate of return on rate base of 10.80% for Westcoast for the 1995 test year. The capital structure and overall rate of return as estimated by the Board are shown in Table 4-2.

Table 4-2
Approved Deemed Average Capital Structure and Rates of Return for the 1995 Test Year

	Amount ($000)	Capital Structure (%)	Cost Rate (%)	Cost Component (%)
Debt - Funded	1,155,939	55.90	10.15	5.67
- Unfunded	153,306	7.41	9.58	0.71
Total Debt Capital	1,309,245	63.31		6.38
Preferred Share Capital	34,960	1.69	7.91	0.13
Common Equity	723,803	35.00	12.25	4.29
Total Capitalization	**2,068,008**	**100.00**		
Rate of Return on Rate Base				**10.80**

4.7 Income Tax Expense

4.7.1 Charitable Donations

In its provision for Income Tax Expense, Westcoast included amounts for both the Base Year and the Test Year of $430,000 and $455,000, respectively, for charitable donations.

Since 1993 Westcoast has recorded a Utility Taxable Income of zero, primarily due to the availability of substantial Capital Cost Allowance deductions associated with acquisition of new facilities. Charitable donations are added back to arrive at net income for tax purposes, and their deductibility is then limited under the *Income Tax Act* to 20% of that net income for tax purposes. In any year that net income for tax purposes is zero, it is not possible for Westcoast to avail itself of the tax deductibility of charitable donations. The deductions, however, may be deferred and accumulated to be deducted in the following five years if there is sufficient net income for tax purposes to do so. This is what Westcoast proposed to do, although the Company did admit that neither the utility, nor Westcoast Energy Inc., is likely to have sufficient net income for tax purposes within the next five years to use charitable donations as a deduction.

Views of the Board

The proposed method for recording charitable donations is in keeping with the flow-through basis of calculating the provision for income taxes, as approved by the Board for Westcoast. It is desirable that the Company prepare, and file with future toll applications, a schedule of "Charitable Donations - Deferred", covering the period from the time of the first deferral until the time that the carry-forward is eliminated.

Decision

Considering that Westcoast has a zero net income for tax purposes, the Board finds the proposed method for recording charitable donations acceptable. The Board requires Westcoast to maintain a schedule of "Charitable Donations - Deferred" covering the period from the first deferral until the carry-forward is eliminated. This schedule is to be included in future toll applications.

4.7.2 Flow-through Tax Calculation

In its provision for income tax calculated on a flow-through basis, Westcoast excluded the B.C. Corporation Capital Tax, as the classification of this tax as Income Tax Expense has been delayed to 1 January 1996. It has instead been grouped with Taxes Other than Income Taxes.

Decision

The Board has adjusted Westcoast's 1995 income tax provision on a flow-through basis (see Table 4-3) to reflect the decisions contained in these Reasons for Decision.

Table 4-3
Utility Income Tax Allowance for the 1995 Test Year
($000)

	Application	**NEB Adjustments**	**Approved (Estimated)**
Return Related to Equity	85,324	(5,525)	79,799
Prior Year Deferral Carrying Charges	(1,082)	-	(1,082)
AFUDC - Interest Portion	(15,869)	3,923	(11,946)
Charitable Donations	455	-	455
Depreciation	55,808	(288)	55,520
Amortization	320	-	320
Amortization of Issue Costs	1,480	-	1,480
Financing Expenses	(2,346)	-	(2,346)
Capital Cost Allowance	(117,703)	1,890	(115,813)
Overhead During Construction	(13,120)	-	(13,120)
Cumulative Eligible Capital	(61)	-	(61)
Foreign Exchange Loss - Debt Redemption	1,193	-	1,193
Disallowable Expenses	750	-	750
Rate Case Expense Payments	(555)	-	(555)
Large Corporation Tax	5,406	-	5,406
Utility Taxable Income	**-**	**-**	**-**
Income Taxes	-	-	-
Add: Large Corporation Tax	5,406	-	5,406
Utility Income Tax Provision	**5,406**	**-**	**5,406**

Chapter 5

Operating Costs

5.1 Operating and Maintenance

Westcoast estimated its test-year O&M expenses to be $138,552,000 for the 1995 test year, representing an increase of $12,552,000 or 10% over the 1994 approved amount of $126,000,000.

5.1.1 1994 Actual O&M Costs

In determining O&M expenses for the 1995 test year, Westcoast showed a 1994 base year amount of $130,400,000, approximately $4,400,000 more than the amount of $126,000,000 that the Board approved in the RH-2-93 Decision. In its evidence, Westcoast described several reasons for the higher base year amount.

During argument, Westcoast stated that in order to appropriately compare actual 1994 O&M to approved O&M, a number of adjustments should be made. The Company stated that an amount of $911,000 should be added to the $126,000,000 to account for Insurance Deductibles. A second amount of $721,000 should also be added for the deferral of some costs associated with the B Train turnaround at Pine River. A third amount of $750,000 is required because of the deferral of costs associated with some vessel inspections and repairs.

A fourth and final adjustment is due to a change in accounting for "Consumable materials and supplies" from being an expense item to a rate base item. Westcoast elaborated that the $130,400,000 amount includes $1,100,000 for unused inventory which was expensed to accommodate the transfer to rate base for 1995. The 1995 cost of service is credited by the $1,100,000 and therefore Westcoast's 1994 O&M should reflect this amount. With these adjustments, Westcoast stated that the variance was actually around $900,000.

All parties and the Board cross-examined Westcoast with respect to its effort to reduce costs in 1994. Westcoast was also questioned on how it addressed achievement of the target amount determined under the Board's global approach in the RH-2-93 Decision. Although there was a decision to reduce salary increases by 0.5% for a total of $483,000 after the release of RH-2-93, there were no other specific items targeted for reduction. Through cross-examination, Westcoast stated that no formal priority listing of O&M items had been made, at least at the Vancouver Departments, and no specific written instructions regarding cost reduction had been issued to managers.

5.1.2 NrG

Westcoast included a provision of $1,240,000 in the 1995 O&M for the Company's portion of costs related to the NrG electronic bulletin board ("NrG"). NrG acts as a "front end" to the pipeline's internal gas management system and provides customers with information required to conduct their daily business in a timely manner. Services offered include on-line bulletins and reports on various subjects as well as tariffs, maps of facilities, want or available ads, nominations, and current and historical operational information.

Westcoast stated that it does not use the nomination function provided with Release 1.0 of NrG in April 1995. Instead, the Company continues to provide shippers with DEALS, its own nomination service, as it is currently superior to the NrG service. DEALS will eventually be integrated with NrG in a future release.

Westcoast has a 33.3% non-utility ownership in NrG Information Services Inc., a company set up to develop NrG. During the hearing, Westcoast stated that its actual 1995 cost for the NrG service would be $1,270,000 based on nine months of service for 310 users representing all shippers on Westcoast. The cost is based on a three-year fixed, posted fee of $475 per ID per month for the first 200 users and $425 for any user ID above 200. Westcoast estimated that it will require 310 user IDs for 1995 and stated that it has signed on 30 users in the first three weeks of operation of the service starting on 1 April 1995.

When asked about the possibility of setting a separate user fee for its shippers, Westcoast stated that NrG is a part of the Company's overall service to shippers and therefore is charged and costed accordingly.

Westcoast stated that no O&M cost reductions have been forecast with the implementation of the service and the addition of one staff position is necessary for the management of the system.

Intervenors questioned the benefits that NrG would bring to shippers when services such as nominations were not being utilized. BC Gas suggested that InfoTap, an electronic brochure that describes the Westcoast pipeline system and services offered, at a total cost of $110,000 over 3 years, provides some of the same information as NrG.

Westcoast include a provision of $450,000 in the 1994 cost of service for NrG. Westcoast stated that these costs were not incurred as a result of the delay in implementation until 1995. The Canadian Association of Petroleum Producers ("CAPP") asked that an equivalent amount be removed from the 1995 budgeted amount on the basis that 1994 tolls were designed to recover these costs which were not incurred. COFI recommended that the full amount related to NrG be removed as well as the associated cost for the additional staff position. BC Gas agreed with COFI and also recommended the removal of $150,000 from rate base related to the cost of an interface required to run NrG.

5.1.3 Other Information System Issues

COFI referred to continuous overruns incurred by Westcoast on new information system projects and the lack of good selection criteria for new systems such as SAP for the Company's new financial reporting system. As a result, COFI recommended that, for the 1995 test year, the 1994 actual amount of $2,200,000 be approved instead of the applied-for $2,900,000, for a reduction of $700,000.

5.1.4 Strategic Planning

In 1994, Westcoast carried out a strategic planning study at a total cost of $1,401,192, where approximately $1,100,000 was spent on consulting fees, including $923,000 for one consultant. While the costs were primarily incurred in 1994, the Company proposed to amortize the cost in equal yearly amounts of $280,000 over the five-year period 1994 to 1998 and to carry the unamortized portion in rate base as a prepaid expense.

Westcoast stated that the study addressed a number of strategic objectives, including customer satisfaction, competitiveness, identification and understanding of public stakeholders, safety and environment, shareholder value, and the development of a high performance organization.

At the hearing, Westcoast was questioned, in some detail, on the benefits derived from the study and the consulting fees paid to the one consultant. Westcoast asserted that the expert help provided was invaluable to the Company and that it was not able to devote sufficient time to strategic planning because its management group was busily engaged in managing the operations of the pipeline. Westcoast also stated that similar planning had been done before as evidenced by the SHARE program.

CAPP found that Westcoast was vague in explaining specific efficiency results from the strategic planning exercise, whereas COFI and BC Gas thought that the output was simplistic for such an expensive initiative. Both the latter intervenors recommended that all costs associated with the plan be disallowed.

5.1.5 Benchmarking Studies

At the hearing, reference was made to five benchmarking studies in which Westcoast participated. CAPP argued that the studies should be made available because they would provide a means of gauging Westcoast's efficiency and performance and because the tollpayers had paid for the studies through the tolls. Westcoast replied however that, by agreement with the other participants, it could not make the studies available. CAPP added that the Board should nevertheless consider directing Westcoast to produce the studies, or make them available for Board review. COFI submitted that a summary document should be prepared and provided to tollpayers to allow them to gauge how Westcoast ranked against the benchmarks.

5.1.6 1995 US Legal Fees

For the 1994 base year, Westcoast incurred US legal fees of $195,000, whereas for the 1995 test year, it estimated an amount of $200,000. At the hearing, Westcoast explained that the 1994 actual fees were incurred for the monitoring of certain US regulatory proceedings. It also asserted that the fees were justified considering the level of expertise obtained. For 1995, Westcoast stated that the estimate reflects a sharing of costs with Union Gas Limited.

Intervenors questioned whether less expensive means of monitoring US activities could be used such as relying on regulatory reporting services or having Westcoast's own personnel attend the proceedings. Intervenors also questioned the type of proceedings being monitored and their relevancy to the Westcoast pipeline.

Westcoast stated that, if it were to send its own personnel to monitor US proceedings, it would incur the associated travel and accommodation costs.

5.1.7 1995 Association Dues, Charitable Donations and Conferences

Westcoast applied for association dues of $647,000, charitable donations of $500,000, and conference expenses of $413,000 for the 1995 test year.

CAPP suggested that Westcoast could particularly exercise cost restraint in the areas of association dues and conferences. CAPP also pointed out that Westcoast would not be able to benefit from the income tax deduction associated with its charitable donations because the Company will not be in a taxable position for the next five years.

COFI recommended that charitable donations be shared equally between the Corporate Centre and the utility, for a disallowance of $250,000.

5.1.8 Costs Associated with the Cost of Capital Hearing

Westcoast included costs of $443,000 in its 1995 revenue requirement for its intervention in the RH-2-94 Cost of Capital Hearing. CAPP questioned whether the total amount should be allowed since, in CAPP's view, the costs relate entirely to Westcoast's shareholders' interests. CAPP also stated that it was concerned with Westcoast's apparent lack of restraint in respect of these costs, particularly since no estimated costs were requested and no budget was established.

5.1.9 1995 Compensation Program for Employees

For the 1995 test year, Westcoast applied for an increase of 2% for both salary and wages. Westcoast based the salary increase on its assessment of a number of industry salary surveys. Westcoast added that it had already awarded its employee salary increases for 1995 and that an additional amount of $132,000 is budgeted for 1995 for the Company to achieve compa-ratio and pay equity targets.

Westcoast also stated that it is developing a new performance-based compensation program, referred to as the Success Sharing Program, to link achievement of strategic business objectives with incentive pay. Westcoast expects the new program to be finalized in the third quarter of 1995 and to be implemented in 1996, and to provide for lump-sum payments that would be considered as bonuses for all non-management employees.

In the interim, Westcoast paid amounts of $500 in 1994 to all field employees pursuant to negotiated settlements for wage earners that provided for automatic provision for lump-sum payments in 1994 and 1995. For 1995, Westcoast budgeted for additional payments of $750 to all pipeline employees as part of Westcoast's regular compensation package, mainly in consideration of parity between compensation to unionized wage earners and salaried employees. For all employees, the $750 payments made for 1995 amount to $777,000, equivalent to 1.1% of budgeted salaries.

Intervenors questioned the applicability of the $750 lump-sum payments proposed for all employees in 1995 with regard to cost restraint. COFI was of the view that the lump-sum payments were voluntary and unjustified, and recommended that they be disallowed.

5.1.10 Executive and Management Bonuses

Westcoast included a total amount of $625,000 in its 1995 application for Executive and Management bonuses. Westcoast stated that it increased its executive bonus targets for 1995 from 15% to 20% of salary, for its nine executives. The Company also increased the bonus targets for its 31 managers from 10% to 15% of salary. Westcoast pointed out that these levels are considered to be at the 50th percentile for gas and pipeline companies.

Westcoast stated that it awards executive and management bonuses not only for achieving the O&M budget but also for other performance factors, including system reliability, throughput levels and minimum outages. It added that no bonuses are included in the Corporate Centre fee to the pipeline.

Intervenors questioned the awarding of management bonuses for seemingly normal performance and noted that Westcoast's forecasts for target bonuses have consistently been distributed each year. COFI recommended that management bonuses be shared equally between the Utility and the shareholders since the shareholders receive the benefit of management's efforts.

5.1.11 CAPP's Proposal on O&M Performance Indicators

CAPP proposed an alternative methodology to determine the reasonableness of Westcoast's 1995 O&M budget, where the total amount would be determined based on performance indicators. CAPP asserted that such an approach would provide meaningful results, would reflect cost causality and would be responsive to the level of activity undertaken by Westcoast in a given year. Based on its analysis, CAPP proposed that Westcoast's O&M budget should be set at approximately $132,800,000 for 1995.

CAPP added that the currently approved methodology results in O&M levels higher than would be consistent with Westcoast's operating environment and provides little incentive for Westcoast to reach settlements at reasonable levels. Further, CAPP was of the view that a broad approach is needed because, in setting approved O&M levels, the Board has generally not accepted the intervenors' specific line item recommendations.

Westcoast did not accept CAPP's methodology. Westcoast found that the methodology had no theoretical or logical foundation and that it simply appeared to be an attempt to arrive at a desired result.

5.1.12 EUG's Comments

In argument, EUG submitted that the traditional cost of service method of regulation was not producing the desired results and that a better method was required. EUG requested that the Board encourage Westcoast and concerned parties to explore various alternatives.

Views of the Board

In this proceeding, the Board has been given the opportunity to review the global approach to determining the appropriate O&M amount for Westcoast. The Board introduced the approach in the RH-2-93 Decision to recognize the dynamic market place in which Westcoast operates where flexibility to adapt to changing circumstances is required. The Board also expected the approach to stimulate management initiative, encourage Westcoast to strive for more efficient operations, and challenge it to "find ways to do more with less". The Board is of the view that it should again approve a global amount for 1995 O&M expenses, allowing Westcoast to determine how and where its O&M budget is to be spent to operate its system in an efficient and effective manner.

CAPP's Proposal

The Board was not persuaded to adopt CAPP's proposed use of performance indicators to determine the global O&M amount. The Board is of the view that CAPP's proposal is insufficiently developed at this time because it does not adequately address such factors as productivity improvement, inflation, growth and uncontrollable costs.

At the same time, the Board appreciates the effort made by CAPP in challenging the current regime and providing an alternative approach, and encourages CAPP, EUG and other interested parties to continue presenting innovative and sound proposals in future toll proceedings. The Board also appreciates CAPP's comments on the evolution of incentive regulation.

1994 Actual O&M Costs

While the Board notes Westcoast's position that adjustments to the 1994 O&M variance would bring it to less than $1,000,000, the Board is still of the view that the effort and the approach taken by Westcoast to achieve the cost reductions in its ongoing activities could have been more serious and aggressive. The Board, in making this statement, notes the apparent lack of expenditure prioritization essential for effective cost reduction. The Board believes that, had the Company exerted the effort required for a more rigorous budget review, it would not have incurred certain discretionary and other costs and the Company would have been able to demonstrate that it had paid due regard to the Board's directional emphasis on cost reduction.

To provide guidance for future hearings and clearly indicate, but not limit, areas where Westcoast could, in the Board's opinion, concentrate its efforts with respect to effectiveness and efficiency, the Board has specifically addressed those items that give it particular concern.

NrG

The Board acknowledges that systems, like NrG, conform with current information and communication trends. However, the Board is concerned with the non-arm's length relationship between Westcoast Energy Inc. and NrG Information Services Inc. Under this relationship, NrG Information Services Inc. profits from any upside, yet leaves to the shippers the cost and much of the risk. For example, the evidence indicated that the system was expected to be operational in the fourth quarter of 1994, later revised to the first quarter of 1995, and finally started operations in April 1995. The costs, however, did not reflect this non-performance and in fact increased for 1995 in spite of the delay.

For these reasons, the Board does not accept the $1,240,000, plus associated costs for additional staff, in its determination of an appropriate O&M amount for 1995 and believes that Westcoast should recover the costs directly from the shippers that use the service. In the future, if Westcoast can demonstrate that shippers support the system and the associated costs, the Board will reconsider the eligibility of the NrG costs as part of cost of service. The Board will also have to be satisfied that the non-arm's length relationship has been made completely transparent as to its cost effects.

Strategic Planning

The Board was not convinced by the evidence adduced in this proceeding that the strategic planning initiative taken by Westcoast has produced sufficient new and worthwhile organizational goals and initiatives to justify its costs. Also, the Board is concerned with the very high costs incurred for consultants. In light of the synergy that should have resulted for Westcoast from Union Gas's previous efforts in the strategic planning area, including utilization of some of the same consultants, and also considering the fact that less formal strategic planning had been evolving at the management level over the past several years, the Board is not convinced that the Company exhibited adequate cost-benefit evaluation of its expenditures in this area. Therefore, the Board has decided to reduce the 1995 O&M amount by $280,000. Further, the Board directs Westcoast to remove the unamortized amount for strategic planning from prepaid expenses in rate base (see section 3.3). This will reduce the return on rate base for 1995 by approximately $106,000.

Benchmarking Studies

The Board has decided that it will review the benchmarking studies as part of its audit activities.

Hearing Costs

With respect to the recovery of costs associated with the Cost of Capital Hearing, the Board considers that the costs are a legitimate part of Westcoast's cost of doing business in a regulated environment. Westcoast may therefore recover the costs in tolls as the Board is satisfied that the amount is reasonable.

Other Items

In looking at ways to reduce costs, Westcoast may wish to reconsider the 1995 budgeted amounts for certain items that tend to be discretionary. Examples of such items may be: conferences; consultant fees; charitable donations; US legal fees; and association dues. Further, it appears to the Board that efficiencies can be realized in the area of salaries, wages and benefits considering that this item alone encompasses approximately one-half of the O&M budget for 1995. The Board expects Westcoast to make every effort to identify all areas across its system where expenditures can be reduced without affecting the reliability and safety of the pipeline. In addition, the Board encourages Westcoast to set organizational component targets and to take full advantage of the creativity of all its personnel in meeting the global target established by the Board.

Such an approach would have the added advantage of providing a fuller, more objective basis for evaluating managerial and other employee performance and the awarding of compensation and bonus payments. In that regard, the Board questions whether distribution of all the budgeted management bonus money in 1994 could be objectively justified.

General Observations

Comments by intervenors on NrG and Strategic Planning were, in the Board's view, pertinent and valid. However, as a general observation, the Board is disappointed with the narrow scope of cross-examination by intervenors. In "chasing", in detail, items such as Westcoast's US legal fees, conferences, association dues, and charitable donations, the Board found intervenors to be largely subjective in their approach. While the Board recognizes that these expense items are largely discretionary costs, it also found that examination by intervenors did not leave the Board in a position to determine specific budgetary reductions.

The Board is also disappointed that intervenors chose not to question Westcoast's field operating costs, given that these costs account for approximately 80% of the Pipeline Division's costs. Considering that most intervenors in the Westcoast toll hearing represent large corporations with industrial operations, some of whom also operate gathering lines, processing plants and pipelines, the Board would expect intervenors to take a more macro approach in their cross-examination to test the proposed O&M budget. This would include analysis of Westcoast's field operations.

The Board feels that pursuit of specific discretionary items does not recognize the thrust of the global target approach. The Board encourages intervenors to examine, more actively, Westcoast's operations and management practices that will contribute to fulfillment of the global target strategy and to setting of corporate efficiency targets for Westcoast.

Concluding Remarks

The Board is aware that during 1994 and 1995 Westcoast has faced a number of challenges. These have included re-organization of Westcoast's corporate structure, creation of the Pipeline Division and re-assignment of senior personnel. Westcoast has also continued to be challenged by the need to expand its system and is currently challenged, as are producers and shippers, by the Board's GH-5-94 Decision dated May 1995 on jurisdiction. Nonetheless, the Board finds that Westcoast has been innovative in presenting new proposals, such as those for the Expansion Service Delivery Policy, the Attrition Capacity Allocation Program and Contract Demand Credits. The Board commends Westcoast for these initiatives and for the way it has dealt and is dealing with its organizational challenges.

During this proceeding, however, the Board observed that there has been a lack of focus by Westcoast in addressing some key O&M items, particularly NrG and strategic planning, and the cost reduction targets set by the RH-2-93 Decision.

The Board is of the view that Westcoast must focus its management approach and tangibly demonstrate that it is aiming for a "least-cost" system. The Board recognizes that, until Westcoast further orients its corporate goals to achieve that target, no one, including Westcoast, will know what efficiencies can be achieved. However, it is the Board's view that efficiencies can be gained across the Westcoast system particularly if its management and staff are motivated towards meeting that objective. In the Board's view, this will be stimulated by Westcoast setting appropriate efficiency gain targets across its system, as is done in many other companies, and as would be to the employees and shareholders' advantage under an incentive regulatory scheme.

Considering all the above and the fact that over one-half the 1995 test year has passed, the Board has determined that an appropriate O&M amount for 1995 would be $135,158,000, which is a reduction of $3,394,000 from the applied-for amount. The Board has every confidence that the energies of Westcoast's staff can be effectively harnessed by management to achieve the target the Board has established. The key, though, will be how management focuses on and presents this challenge to the organization, while also dealing with other corporate challenges.

In future applications, the Board expects Westcoast to file information in the same format as in this proceeding. In addition to substantiating applied-for amounts in their entirety and providing variance analysis for costs incurred, the Board also expects Westcoast to be prepared to produce evidence of concrete steps the Company took in assessing its priority expense items and reviewing its budgets for cost reduction.

Decision

The Board approves O&M expenses in the amount of $135,158,000 for the 1995 test year.

5.2 Swing Gas Costs

For the 1995 test year, Westcoast forecast a total amount of $900,000 for swing gas costs, where $800,000 is for events that occurred in the last quarter of 1994 but where the associated costs will be incurred and recovered in 1995, and $100,000 is for events expected to occur in 1995.

Westcoast explained that the $800,000 amount is not expected to recur every year as it is largely due to the one-time implementation of a daily gas balancing policy on 1 September 1994. By the policy, shippers must maintain their deliveries and takes on Westcoast's system within set tolerances on a daily basis. Westcoast stated that it can apply the policy only through cooperative efforts because no penalties are provided in cases of non-compliance.

Westcoast explained that, when it instituted the policy, there was a significant imbalance on the system resulting from a number of factors, including: insufficient recovery of fuel from shippers due to high levels of takes at the time; shippers reporting higher volumes than actually delivered to the system; and a total imbalance in shippers' accounts in the order of 1 Bcf (28,300 thousand cubic metres).

While Westcoast worked with shippers to gradually bring accounts in balance, the Company had to purchase a total of approximately 1.5 Bcf (42,500 thousand cubic metres) of gas on 21 October and 5 December 1994, at a cost of $3,300,000. However, Westcoast expects to be able to dispose of that gas at only half this cost, for a loss of $1,600,000 expected to be realized during the 1995 test year.

Based on its analysis of whether swing gas events resulted from either plant outages or unacceptable levels of linepack, Westcoast determined that the forecast loss should be spread in equal amounts of $800,000 each to zone 2 as mitigating costs and to zones 3 and 4 as swing gas costs. Westcoast also stated that it does not expect to recover much of the zones 3 and 4 swing gas costs because it doubts that it will be able to assign all of the costs to specific shippers.

Regarding the forecast amount of $100,000 for swing gas events expected in 1995, Westcoast explained that it determined the amount based on its expectations of swing gas events over the test year and on its experience over the past few years. The Company also stated that, in the first quarter of 1995, it incurred swing gas costs of $53,000, as well as swing gas costs of $10,300 in 1994 and $79,000 in 1993.

CAPP commented indirectly on the matter when it questioned whether the Gas Management System of Westcoast as a whole provide benefits to tollpayers when Westcoast experiences a gas imbalance in shippers' accounts as large as 1 Bcf (28,300 thousand cubic metres).

COFI recommended that the forecast $800,000 loss for swing gas events that occurred in 1994 should not be considered as a loss in 1995 but rather be deferred until such time as the loss is realized. It also suggested that deferral treatment should allow examination of whether Westcoast's actions have been prudent, and noted that the policy does not provide for penalties for non-compliance.

Views of the Board

While the Board considers that Westcoast was prudent in introducing a daily balancing policy, it is also surprised that, when it introduced the policy, the system imbalance was as large as Westcoast described it and that the loss to Westcoast is forecast to be so high. The Board gave consideration, however, to Westcoast's explanations that it was forced to buy the swing gas when the system was utilized at high levels, which could explain how imbalances could have quickly reached high proportions and how Westcoast would have had to pay a premium for the gas.

COFI recommended that the loss be deferred until such time as it is realized; it added that deferral treatment would allow examination of whether Westcoast's actions have been prudent. However, no evidence was adduced at the hearing which would suggest that Westcoast would not dispose of the gas in the current test year. In addition, in the opinion of the Board, no intervenor challenged the reasonableness of the various decisions taken by the Company in bringing its system back in balance.

Regarding the reasonableness of the $100,000 amount forecast for swing gas events expected to occur in 1995, it appears to the Board that the amount is acceptable, particularly when considering the difficulty of forecasting swing gas events and the recent experience of Westcoast at incurring swing gas costs.

Decision

The Board has decided to deny COFI's request for deferral of the loss that Westcoast expects from events that resulted from the introduction of the daily balancing policy in 1994 and to accept Westcoast's estimate of $900,000 for swing gas costs for the 1995 test year.

5.3 Cost Allocation

5.3.1 Corporate Centre Fee Charged to the Pipeline Division

During 1994, Westcoast undertook a major reorganization of its Vancouver Head Office departments by creating a separate Pipeline Division comprising of the Company's NEB-regulated activities and a separate Corporate Centre which provides shared services to a number of operating entities within the Westcoast group of companies, including the Pipeline Division. Commencing 1 January 1995, the Corporate Centre has been providing specific services to the Pipeline Division for an annual fee, which was set at $4,359,000 for 1995.

Westcoast stated that the Corporate Centre allocated its annual budget to various entities using the cost driver approach and thereby determined the annual fee charged to the Pipeline Division. The Pipeline Division participated in this process of fee determination. It analyzed the specific functions provided by the Corporate Centre, the related costs and the cost drivers used. It also compared the 1995 administrative costs, including the Corporate Centre fee, with those for 1994. The Pipeline Division was satisfied that the charge allocated to it by the Corporate Centre is reasonable.

The Company estimated that the Pipeline Division's administrative costs for 1995, inclusive of the Corporate Centre fee, would be $39,891,000. This amount is about $420,000 lower than the 1994 administrative costs prior to the formation of the Corporate Centre, as adjusted and normalized to reflect the 1995 situation. In Westcoast's view, this comparison fully supports the reasonableness of the Corporate Centre fee. Westcoast noted that this comparison does not reflect the fact the Pipeline Division would recover approximately $800,000 from the Corporate Centre for the accounting services it provides. The Company argued that when these recoveries are included in the comparison, the 1995 cost of service would be approximately $1,200,000 lower than what it would have been if the Corporate Centre did not exist.

Westcoast stated that of the total budget of $14,994,000 for the Corporate Centre, 29% is being charged to the Pipeline Division, 35% to other regulated entities and 36% to non-regulated and corporate activities. Westcoast noted that, unlike Union Gas Limited or Centra Gas Ontario Inc., the Pipeline Division has no Board of Directors, does not raise its own debt, and has no annual report and shareholders meeting of its own. For those reasons, a relatively higher percentage of Corporate Directors' costs was charged to the Pipeline Division.

Intervenors focussed their examination on the appropriateness of the cost drivers used by Westcoast and on the reasonableness of the allocated costs. In argument, CAPP and COFI noted that in the absence of a breakdown of the Corporate Centre costs by departments, and the relative size of allocation bases for other entities, the reasonableness of the costs allocated to the Pipeline Division cannot be assessed. In their view, the process of cost allocation remains opaque, contrary to Westcoast's claim that with the formation of Corporate Centre and use of cost drivers the process is now transparent. COFI recommended that the Corporate Centre fee should be reduced to $3,500,000.

Westcoast argued that with the formation of the Corporate Centre a transparency has been created in that every person in the Pipeline Division works 99.3% of the time for the pipeline.

Views of the Board

The Board notes that the general description of the cost driver methodology used for allocating the Corporate Centre costs to the Pipeline Division, as provided by Westcoast, was adequate. Given that 1995 is the first year of operation following the creation of the Corporate Centre, the Board agrees with CAPP and COFI that the allocation could have been more transparent.

The Board was not convinced by COFI's suggestion that the Corporate Centre fee should be adjusted downward to $3,500,000 because COFI failed to justify its recommendation. Based on Westcoast's comparative analysis of the Pipeline Division's administrative costs for 1995, including the Corporate Centre fee, and 1994 administrative costs prior to the creation of the Corporate Centre as adjusted to reflect the 1995 situation, the Board finds that the Corporate Centre fee of $4,359,000 for 1995 is reasonable.

Decision

The Board approves the Corporate Centre fee of $4,359,000 for the 1995 test year.

5.3.2 Allocation of Costs Between Utility and Non-Utility Activities

In compliance with a Board directive in the RH-1-92 Decision, Westcoast hired Arthur Andersen & Co. to review and recommend on the allocation of costs between its utility and non-utility operations. In the report entitled "Study of Cost Allocation Between the Utility and Unregulated Activities" dated May 1993, Arthur Andersen recommended that Westcoast should allocate costs using cost drivers, that is, based on a measurable volume or activity level. Under the existing methodology, Westcoast allocated costs based primarily on time sheets supplemented with an overhead load to account for indirect costs.

Since Westcoast's reorganization, the majority of the non-utility work is now done at the Corporate Centre. The Pipeline Division continues to provide certain services to the non-utility including the Corporate Centre. However, the level of the non-utility work within the Pipeline Division is now relatively small and therefore, in Westcoast's view, the concerns regarding the utility and non-utility allocation are no longer the same.

Westcoast indicated that, other than Vancouver departments, the operating personnel in four cost centres spend time on capital and non-utility activities. In those cost centres, Westcoast allocated costs to capital and non-utility based on time sheets which, in Westcoast's view, are the appropriate cost drivers.

In respect of Vancouver departments, the Company identified: the activities performed by each department; the cost driver used to allocate the cost of each activity; and whether the individual activity cost is allocated to O&M, utility capital, non-utility or a combination thereof. The Company also provided a list of non-utility activities undertaken by each department. Westcoast stated that the choice of the various cost drivers was determined on the basis of the particular activities performed by each department. In certain departments, such as legal and process administration, time estimates continue to be the most appropriate cost driver having regard to the nature of the activities performed.

During cross-examination, Westcoast stated that it identified each activity within a department, calculated the cost of each activity, chose an appropriate cost driver and calculated the allocation based on either a time sheet, a voucher count, a head count or some similar type of hard and fast cost driver. However, Westcoast did not provide the activity costs or the percentages of such costs allocated to capital or non-utility.

Intervenors did not comment on Westcoast's choice of cost drivers or on the reasonableness of the allocated costs. COFI noted that whereas the Pipeline Division identified the activities of the various divisions and the cost drivers used for allocating costs, it did not provide the amounts or the percentages of costs and, therefore, it was difficult for COFI to comment on the cost allocation methodology. In COFI's view, more studying is required.

Views of the Board

The Board finds Westcoast's qualitative description of the cost allocation methodology used for 1995 to be reasonable. However, the Board agrees with COFI that intervenors require quantitative analysis in order to be able to comment on the reasonableness of the allocated costs. The Board believes that Westcoast should attempt to satisfy intervenors' concerns in this area in future applications.

However, given that 1995 is the first year that Westcoast has used new cost drivers, in addition to time sheets, the Board is prepared to accept the applied-for amounts allocated to capital and to non-utility.

Decision

The Board approves the allocation of the Pipeline Division costs to non-utility and capital for the 1995 test year.

5.3.3 Capitalization of Salaries and Overhead

As in the previous proceedings, CAPP and COFI were concerned with the issue of capitalized versus expensed salaries and overhead. CAPP analyzed Westcoast's 1994 salaries expense and noted that, in Northern District, the actual capitalized salaries exceeded the approved forecast. Westcoast explained this was due to an extremely high level of capital activity in the North. While CAPP accepted this, it noted that the sum of the approved O&M salaries recovered in current year's tolls and the actual capitalized salaries, recoverable in future years' tolls, exceeded the actual total salaries expense for the Northern District in 1994. CAPP adduced evidence which showed that the situation was similar at the Pine River Plant. CAPP inferred that certain salaries included in the 1994 cost of service, and already recovered through tolls, were being capitalized and recovered a second time through depreciation of the rate base. Westcoast acknowledged that, while this appears to be so for the Northern District and Pine River Plant, it was not the case in other cost centres.

CAPP expressed its continuing concern with Westcoast's capitalization procedures and urged the Board to continue to monitor the situation very closely. For an appropriate Board action, CAPP referred to the Board Decision in RH-3-91 where, in a similar situation, Trans Mountain Pipe Line Company Ltd. was directed to reduce its gross plant in service by the amount of salaries found to have been provided for in the cost of service and as well charged to capital. COFI recommended that approximately $2,000,000 of capitalized overhead should not be allowed into rate base since this was already recovered as an O&M expense. As well, COFI urged that an NEB audit should focus in this area.

Views of the Board

The Board notes that the evidence on record in this proceeding concerning this matter lacks data for carrying out a conclusive analysis. Based on the available data, the Board accepts Westcoast's evidence that salaries recovered through the 1994 tolls have not been capitalized. Accordingly, the Board rejects COFI's recommendation of disallowing $2,000,000 from the rate base. The Board also notes that in 1994 and prior years Westcoast's forecast of capitalized salaries was based on a predetermined allocation factor. Therefore an NEB audit of 1994 records may not be useful for initiating a Board action in this matter.

As mentioned in subsection 5.3.2, Westcoast has implemented a new cost allocation methodology for the 1995 test year and the forecasts of salaries and overhead charged to capital are based on an analysis of capital activities to be undertaken during the test year and on the use of appropriate cost drivers, including time sheets. The Board recognizes that there will be some variances between the actual and forecast capitalized salaries and overhead but the Board is not overly concerned with reasonable and small variances. The Board believes that, with the new cost allocation procedures, actual capitalized salaries and overhead will be closer to forecast amounts.

The Board is of the view that from 1995 onwards, when variances between forecast and actual capitalized salaries are large and remain unexplained, an adjustment to the cost allocation factors may be considered for the prospective test year. Alternatively, an adjustment to the gross plant in service may be appropriate.

Westcoast is advised to take note of the concerns expressed by intervenors to this proceeding. Given the extent of recent expenditures related to computing facilities, the Board expects Westcoast to maintain and be able to provide the necessary data for carrying out the required analysis.

5.3.4 Deferral of Maintenance Work

Westcoast sometimes defers budgeted maintenance work to allow its employees to work either on more urgent unbudgeted maintenance projects or on capital projects requiring additional resources. For 1994, Westcoast stated that the extremely high level of capital activity did not necessarily result in O&M projects being deferred, although this may have been the case in a few circumstances.

When asked to provide information regarding the number of projects deferred in 1994 as well as the breakdown of 1995 O&M projects as being either new or routine projects or deferred projects from a previous year, Westcoast answered that it did not maintain records in a form which would enable it to readily provide the requested information. Westcoast acknowledged that a deferred O&M project may be rescheduled in a subsequent year with the corresponding dollar amount included in that year's budget.

Views of the Board

The Board is not questioning the flexibility Westcoast should have in determining whether or not discretionary maintenance work can be deferred in order to take advantage of the most effective use of its resources. The Board is not even able to assess whether this flexibility is being reasonably exercised by Westcoast due to the limited information made available by Westcoast in this proceeding. However, the Board would like to be able to determine this reasonableness in future proceedings. In considering the recent expenditures for information systems to better organize cost centre data, the Board expects Westcoast, in the future, to be prepared to provide information regarding deferral of O&M work similar to what was requested in this proceeding.

Chapter 6

Toll Design and Tariff Matters

6.1 Throughput Forecast

For cost allocation and toll design purposes, Westcoast submitted a forecast throughput for each zone. At the hearing, no intervenor questioned the forecast.

Decision

The Board finds Westcoast's 1995 test year throughput forecasts for each zone to be reasonable for cost allocation and toll design purposes.

6.2 Interruptible Throughput

Westcoast adopted a new method of forecasting the test year interruptible throughput by relying on a forecast of interruptible revenue instead of interruptible volumes. Westcoast submitted that the new approach is better because it allows for adjustments of interruptible charges for shippers' under-utilization of firm service and for raw gas deliveries of higher acid gas content than that stipulated in service agreements.

The forecast is based on a historical analysis of the relationships between actual and billed interruptible and firm revenues for each zone from January 1990 to July 1994 and non-linear, best-fit trend lines carried out to the year 1995. While Westcoast explained that it did not consult its shippers about the forecast because of the inherent uncertainty of predicting requirements for the service, it added that it tested its reasonableness in the light of its expectations of system usage and availability in the test year.

In recent years, interruptible throughput forecasts were too low for zones 1 and 2 and too high for zones 3 and 4. In total, for the 1994 test year, Westcoast had estimated interruptible revenues of approximately $5,300,000, while actual revenues amounted to $15,800,000. As a result, a total of $10,500,000 had to be recorded in the Interruptible Revenue deferral account. Using the proposed methodology, Westcoast has forecast interruptible revenues for 1995 of $13,200,000, or $2,500,000 less than that experienced in 1994. Westcoast noted that, for the first quarter of 1995, interruptible revenue stood at only 90% of the level experienced in the first quarter of 1994.

COFI suggested that the forecast should be increased from the level suggested by Westcoast so as to yield interruptible revenues of approximately 3.5% of total revenue. COFI explained that Westcoast has had a history of under-estimating interruptible revenues as evidenced by forecasts significantly below actuals for both the 1993 and 1994 test years. COFI added that its recommendation represents a compromise between Westcoast's current forecast and the actual experienced interruptible throughput for 1994.

BC Gas submitted that the 1995 interruptible revenue forecast should be set equal to at least the level experienced in 1994 as a percentage of total firm revenue. Among other things, contrary to Westcoast, BC Gas was of the view that the proportion of interruptible revenues should increase from 1994 to 1995 for zones 1 and 2. BC Gas also noted that Westcoast had not carried out further statistical analysis of the results obtained by its new methodology and suggested that, in applying it, Westcoast ignored changes in the marketplace and in the Westcoast system, and a recent trend towards higher proportions of interruptible volumes. Further, BC Gas stated its view that Westcoast prefers to under-estimate interruptible throughput so as not to find itself in a situation of having to seek further payments from shippers through a future period's tolls.

Views of the Board

The Board is of the view that Westcoast's new methodology should produce more reliable estimates of interruptible throughput because it addresses adjustments to interruptible charges due to under-utilization of firm service and raw gas deliveries of higher acid gas content than that stipulated in service agreements. Further, the new methodology considers each zone independently of other zones.

There is some doubt, however, that Westcoast carried out as sophisticated an analysis as it could have done. For example, it could have tested the new methodology by applying it to forecast the 1994 throughput for each zone and comparing the results with the actual throughput.

Further, while the forecasts for each zone can be defended statistically, Westcoast does not seem to have fully evaluated the best-fit character of each curve. It is not certain that the quasi-straight lines fitted to data for zones 1 and 2 and the higher order curves fitted to data for zones 3 and 4 are the best ones to forecast throughput for 1995.

In addition, the Board shares the concerns expressed by some intervenors that the forecasts of lower revenues in 1995 for zones 1 and 2 are at odds with the upward trend in actual data observed for the 1993 and 1994 test years. However, the Board also gives credence to the fact that the downward trend forecast by Westcoast might be justified when considering that the level of usage of interruptible service for the first quarter of 1995 is lower than that experienced for the same time period in 1994.

COFI and BC Gas both recommended that the forecast throughput be increased from the applied-for level. COFI made reference to the forecasting record of Westcoast for 1993 and 1994, whereas BC Gas highlighted weaknesses perceived with the proposed methodology. While the Board shares some of these concerns, it finds that these proposals are not sufficiently detailed to be considered as alternatives to Westcoast's proposal; further, the proposals were presented in argument, without the benefit of full examination at the hearing.

Considering all the evidence before it on this matter, the Board finds that Westcoast's new approach should be adopted for the 1995 test year as it should improve the accuracy of the interruptible volume forecast. However, the Board also finds that the approach could be enhanced if it were supported by further statistical analysis and further corroborating data as suggested by intervenors.

Decision

The Board has decided to accept Westcoast's new methodology for forecasting interruptible throughput. In addition, the Board directs Westcoast to file evidence in its future tolls applications that would support the reasonableness of the selected best-fit curve and the forecast for each zone. Reference should be made to, among other things: evolution of marketplaces; evolution of Westcoast's system; shippers' under-utilization of firm service; and data on raw gas deliveries of higher acid gas content than that stipulated in service agreements. Westcoast should also comment on the accuracy of the estimates for the previous year as evidenced by the amounts recorded for each zone in the Interruptible Revenue deferral account.

6.3 Contract Demand Credits

Following a recommendation from the Toll and Tariff Task Force ("TTTF"), Westcoast proposed to modify its General Terms and Conditions for contract demand credits in zones 3 and 4 so that it would be relieved from allowing credits when, during the summer shipping season, it delivers at least 90% of a shipper's contract demand or it restricts a shipper to no less than 90% of its contract demand.

Westcoast explained that during the summer months, from April to October, the physical capacity of the system is reduced to 93% of the contracted capacity because of higher ambient temperatures; the capacity is also reduced by an additional 3% because of interruptions due to maintenance and construction activities. Westcoast elaborated that, in the past, the reduced availability of capacity did not affect shippers because, in aggregate, summer nominations for firm service were well below the level of contracted firm service. Recently, however, summer loads have increased to the point where some shippers no longer have summer valleys in their delivery pattern.

By the proposed amendment, Westcoast would be liable to contract demand credits for zones 3 and 4 if, for operational reasons, it fails to deliver the quantity of gas requested by a shipper up to 100% of its contract demand in the winter and up to 90%, in the summer. In this case, the credit would be equal to the applicable daily demand charge, multiplied by the difference between the amount of service which would otherwise have been provided and the amount actually provided.

Westcoast would also be liable for credits if, for operational reasons, it restricts transportation service to a volume less than 100% or 90% of a shipper's contract demand during the winter and summer, respectively. In this case, the credit would be determined by reference to the average amount of service that was actually provided during the three days preceding the reason for the constraints.

Westcoast also proposed to capitalize contract demand credits due to capital additions as a cost of the facility addition and to review the above summer reliability level of 90% annually.

CAPP and COFI expressed their support for Westcoast's proposal; COFI added, however, that the threshold levels should be re-examined in the light of the experience in 1995.

Views of the Board

The Board finds Westcoast's proposed modifications reasonable. The Board also finds that the proposal to capitalize credits due to capital additions complies with the *Gas Pipeline Uniform Accounting Regulations*.

Decision

The Board approves the proposed modifications to the General Terms and Conditions for contract demand credits. In addition, the Board expects that, either in its future toll applications or through separate filings, Westcoast will justify the continued appropriateness of the applied-for summer reliability level of 90% or any changes to it.

6.4 Expansion Service Delivery Policy

Westcoast applied to delete its existing Queuing Procedures and Access Criteria ("QP & AC") set forth in Schedule A to its current General Terms and Conditions and to replace it with its proposed Expansion Service Delivery Policy ("ESDP"). In support of this requested change, Westcoast noted that its main rationale for replacing the existing QP & AC is to address the problem acknowledged by Westcoast's shippers that queues for service are no longer effective in meeting its customers' requirements, to the extent that queues contain requests for service that are stale-dated or, in some cases, speculative.

Specifically, the ESDP represents a fundamental change in Westcoast's facility access mechanism. Currently, as per the QP & AC, prospective shippers make written requests for service to Westcoast and are entered into the queue for that zone and, as facilities are expanded, shippers' requests are satisfied on a first-come, first-served basis. Under the proposed ESDP, prospective expansion shippers, instead, have 30 days to respond to Westcoast's electronic bulletin board posting of its intention to apply to the NEB for facility expansion approval, advising Westcoast of their desired firm service contract demand volumes. This posting will occur not less than 60 days prior to the date that Westcoast intends to forward Expansion Service Agreements to prospective expansion shippers.

Further, to the extent that the total desired contract demand volume is larger than the expansion capacity, under the proposed ESDP, prospective expansion shippers would follow a three-tiered pro-rationing mechanism which would proceed, sequentially, as follows:

a) resolution amongst the prospective expansion shippers themselves;
b) pro-rationing by Westcoast on the basis of contract demand volumes; or,
c) allocation by way of a lottery process, agreed upon by the prospective expansion shippers.

The proposed ESDP would also be a departure from the current practice of progressive rigour in Westcoast's supporting information requirement of prospective expansion shippers, approved by the Board in the RH-3-92 Reasons for Decision. That is, instead of a two-step filing requirement 18 months and 12 months prior to the service commencement date requested, there would be a one-time submission of supporting information to Westcoast, accompanying the executed Expansion Service Agreement. This one-time submission of supporting information, which is essentially equivalent to the existing second requirement just noted, would be filed with Westcoast within 21 days of the prospective expansion shippers' receipt of its Expansion Service Agreement from Westcoast and not more than 90 days before Westcoast files its application with the Board.

There is also a notable difference between the two policies with respect to the specific data required in the supporting information. Currently, in the case of zone 3 and 4 facility expansions, where the prospective shipper represents a firm gas supply/market, the shipper must provide satisfactory evidence that there exists supply/market for 10 years and that a firm market/supply exists for that supply/market for a minimum term of two years. Under the proposed ESDP, the supporting information required in relation to any facility expansion would be evidence of firm supply/markets for the length of the term of the Expansion Service Agreement and of firm markets/supply for a minimum term of one year. In other words, Westcoast proposed that the existing "10-10 & 2" requirement (10-year executed firm service agreement, evidence of a 10-year supply/market for a supply/market shipper and at least a two-year market/supply) be changed to a "10-10 & 1" requirement.

Although the validity of the proposed ESDP was not directly challenged by intervenors, three ancillary issues were raised. The first issue related to how the ESDP should be defined. Specifically, CAPP challenged the appropriateness of Westcoast's request to have the proposed ESDP filed with the Board as a Westcoast policy. CAPP submitted that greater certainty would exist with respect to equal access to Westcoast's facilities if the proposed ESDP were expressly included in Westcoast's General Terms and Conditions. Conversely, Westcoast indicated that it believes that the proposed ESDP would be overly restrictive to both Westcoast and its shippers if the entire ESDP document, or a portion thereof, were to be included within Westcoast's General Terms and Conditions. Consequently, Westcoast submitted that since the proposed ESDP relates to facilities to be constructed in the future and an intention to provide service rather than to the provision of service on existing facilities, it would not fall under the definition of "Tariff" in Part IV of the NEB Act and, consequently, need not be included in Westcoast's General Terms and Conditions unless the Board specifically instructs Westcoast to do so.

The second issue raised by intervenors pertained to the information requirement of prospective expansion shippers with respect to firm market and supply evidence. Specifically, CAPP and COFI proposed a "10-10" requirement of a prospective market/supply shipper, suggesting that it is unrealistic to require evidence of a corresponding one-year supply/market arrangement up to 26 months in advance of a delivery date. Additionally, these parties submitted that the "10-10" requirement, coupled with Westcoast's macro market and supply assessments, together make the provision of a corresponding one-year commitment unnecessary. On the other hand, BC Gas concurred with Westcoast that a "10-10 & 1" requirement is important to the extent that it enables Westcoast to identify and eliminate capacity requests which are made for speculative requirements.

The third issue raised with respect to the proposed ESDP was a wording concern regarding Westcoast's proposed "10-10 & 1" information requirement of a market shipper. COFI raised this issue suggesting that the one-year supply commitment required of a market shipper, section 3.(c)(v) of the proposed ESDP document, which requires the provision of "satisfactory evidence that the prospective shipper owns, controls, or has contracted for a firm gas supply to meet its firm supply requirements or sales obligations for a minimum of one year" is more stringent, in terms of how it might be interpreted by Westcoast, than the one-year market commitment required of a supply shipper, section 3.(b)(vii), which requires the provision of "satisfactory evidence that there exists a firm market for the prospective expansion shipper’s firm gas supply for a minimum of one year."

In response to COFI’s request, Westcoast prepared an adapted section 3.(c)(v) which, instead, requires the provision of "satisfactory evidence that there exists a firm gas supply for the prospective expansion shipper’s firm market or supply requirement for a minimum of one year." CAPP objected to the use of this latest version of section 3.(c)(v), citing that the wording softens the information requirements of market shippers relative to the information requirements of supply shippers.

Views of the Board

The Board acknowledges that the facility access mechanism contained within the existing Queuing Procedures and Access Criteria, as administered by Westcoast, results in queues which have not proven effective in meeting Westcoast customers’ requirements. Further, the Board is of the opinion that the facility access mechanism specified in the proposed Expansion Service Delivery Policy will eliminate the problems associated with queues. It will provide Westcoast with current contract demand information which will enhance its facilities planning processes while, concurrently, providing prospective expansion shippers greater assurance that service will be available on a timely basis. Accordingly, the Board will allow Westcoast to replace its existing Queuing Procedures and Access Criteria set forth in Schedule A to its current General Terms and Conditions with its proposed Expansion Service Delivery Policy.

The Board is of the view that, although the proposed ESDP may be captured by the definition of "Tariff" in Part IV of the NEB Act, it may be filed with the Board as a Westcoast policy rather than as part of its filed Tariff. The Board notes that the proposed ESDP is, nevertheless, subject to the jurisdiction of the Board with respect to any complaints that might be made by an aggrieved shipper against Westcoast in the matter of the administration of the proposed ESDP by Westcoast.

Additionally, the Board is of the view that a "10-10 & 1" information requirement of prospective expansion shippers with respect to evidence of firm supply/markets provides Westcoast with information essential to assess adequately whether service requests of prospective expansion shippers are legitimate and the facility expansions needed.

Finally, the Board has determined that Westcoast’s new definition of section 3.(c)(v) of the ESDP document ensures more equitable treatment of market and supply shippers in regard to the respective one year supply and market commitments required of them by Westcoast. Therefore, section 3.(c)(v) of the ESDP document should read as follows: "satisfactory evidence that there exists a firm gas supply for the prospective expansion shipper’s firm market or supply requirement for a minimum of one year."

Decision

The Board approves Westcoast's request to replace its existing Queuing Procedures and Access Criteria, set forth in Schedule A to its current General Terms and Conditions, with its proposed Expansion Service Delivery Policy as initially submitted, subject to the amendment of section 3.(c)(v). As well, the Board approves Westcoast's request to file with the Board the proposed Expansion Service Delivery Policy as a Westcoast policy.

6.5 Attrition Capacity Allocation Program

Westcoast applied to amend its General Terms and Conditions by adding a new Article 9: Attrition Capacity Allocation Program ("ACAP"). In support of the proposed ACAP, Westcoast submitted that there was general agreement within Westcoast's TTTF that any procedure designed to allocate attrition capacity had to reflect the notion that all shippers should have equal access to the capacity. To this end, the TTTF deemed the first-come, first-served concept to be inconsistent with this equal access notion, concluding that an open-season bid process should be adopted. Westcoast noted that the TTTF also agreed that, when Westcoast is in an expansion mode, attrition capacity should be used to reduce, to the extent possible, the design capacity of additional facilities that would otherwise be required.

The proposed program departs from the current attrition capacity allocation practice of using queues and satisfying shippers' requests for service on the basis of first-come, first-served, by instituting an open-season bid process which enables shippers to have equal access to attrition capacity. Specifically, with the proposed ACAP, Westcoast would post on its electronic bulletin board, all features of any firm service that becomes available for reasons other than the construction of additional facilities, including capacity associated with the failure of shippers to exercise their renewal rights. Prospective shippers would then post bids to take up the service at any time prior to 1600 hours on the tenth business day following the day the service was posted. All bids would be at the authorized posted toll and would specify the maximum and minimum contract demand, as well as define the scope of service required (e.g. receipt and delivery points, term).

While a bidder could withdraw its bid at any time prior to the end of the ten-day period specified above, it could not resubmit a bid with a lower economic value nor submit multiple bids having the same receipt points and delivery points. With the exception of the bidder's name, all posted bids would be open to public examination. A bidder to whom service is awarded would be bound to take the service unless the volume offered is less than the bidder's minimum specified contract demand.

Westcoast would award the available service to the bid with the highest economic value. This would be determined by calculating the net present value of the authorized monthly demand unit toll for the service specified, discounted at a rate equivalent to Westcoast's current approved rate of return on rate base, on a before-tax basis. In the event that two or more bids are equal, Westcoast would determine the winning bid using one or more of the following criteria: the bid with the earliest start date would be considered the winning bid; the bid with the longest term would be considered the winning bid; and, bids that are contingent on obtaining service in other zones would be given a lower priority. Westcoast indicated that all shippers who intend to bid would be made aware of the tie-breaker criteria well before the process began.

Intervenors did not raise concerns relating to the proposed ACAP.

Views of the Board

The Board affirms the appropriateness of instituting mechanisms which allow shippers equal access to attrition capacity and which award attrition capacity to the shippers who place the highest value upon it. Further, the Board believes that the proposed Attrition Capacity Allocation Program is consistent with these principles. Therefore, the Board has determined that attrition capacity should be allocated on the basis of the proposed Attrition Capacity Allocation Program, replacing Westcoast's current attrition capacity allocation practice of using queues and satisfying shippers' requests for service on the basis of first-come, first-served.

Decision

The Board approves Westcoast's request to amend its General Terms and Conditions by adding a new Article 9: Attrition Capacity Allocation Program.

Chapter 7

Deferral Accounts

7.1 Disposition of Existing Deferral Accounts

Westcoast provided the balances in the existing cost of service and revenue deferral accounts as at 31 December 1994 and proposed that such balances be amortized to the 1995 test year cost of service in the same manner as used in previous years.

For the disposition of the Demand Charge Credits deferral account balance, Westcoast proposed that the deferral balance, which was caused by construction of the Fort Nelson Mainline facilities in 1994, be capitalized as of 1 January 1995 as part of the project.

None of the intervenors objected to the proposed disposition of the deferral account balances.

Views of the Board

The Board finds that the disposition of the existing deferral account balances as at 31 December 1994 as proposed by Westcoast is reasonable.

Decision

The Board approves the proposed disposition of the deferral account balances.

7.2 Continuation of Existing Deferral Accounts for 1995

For the 1995 test year, Westcoast applied to maintain for accounting and toll-making purposes the following cost of service and revenue deferral accounts, each of which has been previously approved by the Board.

<u>Cost of Service Deferral Accounts</u>

- Property Taxes
- Taxes Related to Fuel Consumption
- Federal Surtaxes and Income Taxes
- Provincial Surtaxes and Income Taxes
- Corporation Capital Tax
- Foreign Exchange
- NEB Cost Recovery
- Zone 2 Demand Charge Credits
- Pressure Vessel Inspection and Repair
- Swing Gas

Revenue Deferral Accounts

- Contract Demand Volumes
- Interruptible Revenues
- Liquids Products Stabilization and Fractionation Service Revenue Variance

None of the intervenors commented on this matter.

Decision

The Board approves the continuation of the deferral accounts listed above for the 1995 test year.

7.3 Unfunded Debt Rate Deferral Account

Westcoast plans to raise a total of $375,000,000 during 1995 through three debt issues: one in June for $150,000,000, one in August for $125,000,000 and a final one in October for $100,000,000.

In final argument, COFI suggested that the Board approve a deferral account for unfunded debt to ensure that Westcoast does not reap substantial gains if it were to delay issuing long-term debt and rely on shorter term financing in the interim. COFI added that interest rates have been particularly volatile so far in 1995, which may cause Westcoast to alter the times at which it goes to market for long-term funds. COFI further stated that the Board had approved such an account previously where capital markets had been volatile.

Views of the Board

The Board finds that no new evidence was adduced in this proceeding that would warrant departing from its earlier decision in the RH-2-93 Reasons for Decision. At that time, the Board had denied a request for a deferral account for the unfunded debt rate because it found that the costs could reasonably be forecast and are subject to sufficient scrutiny that Westcoast should recover a cost rate that is fair and reasonable.

Decision

The Board has decided to deny COFI's request for a deferral account for the unfunded debt rate.

7.4 Swing Gas Cost Deferral Account

COFI recommended that the loss of $800,000 included in swing gas costs for 1995, due to swing gas events that occurred in 1994, should be deferred until such time as the loss is realized. This matter is discussed in section 5.2.

Chapter 8

Interim and Final Tolls

By Order TGI-2-94 dated 8 December 1994, the Board approved tolls that the Company may charge for services provided to customers on the Westcoast system on an interim basis effective 1 January 1995.

The Board continues to take the view that final tolls for 1995 should be uniform, in the sense of being charged at the same level throughout the year. The Board has estimated that final tolls for 1995 set in this manner would give rise to an increase of approximately 5.6% over the 1994 tolls for a typical export service movement. Westcoast will be required to refund to or, where applicable, recover from its customers the difference between the tolls resulting from these Reasons for Decision and those approved on an interim basis by Order TGI-2-94, together with carrying charges at the approved rate of return on rate base for 1995.

Decision

The Board intends to approve final tolls for 1995 which are uniform throughout the 1995 calendar year. Westcoast is directed to refund to its customers or, where applicable, recover from its customers, the difference between the tolls resulting from these Reasons for Decision and those approved on an interim basis by Order TGI-2-94, together with carrying charges at the rate of return on rate base approved for 1995.

Chapter 9

Further Filings by Westcoast

In these Reasons for Decision, the Board has estimated the impact of its decisions on the Company's 1995 cost of service and tolls on the basis of information available to it in this proceeding. The Board has not included a final approved rate base, rate of return on rate base, cost of service or tolls for the 1995 test year.

Accordingly, Westcoast is required to file for Board approval revised information on rate base and cost of service, together with supporting schedules, reflecting the Board's decisions in Chapters 3 to 8 inclusive. These revisions and the tolls and tariffs are to be filed with the Board forthwith and served on interested parties. Westcoast's filing should include detailed explanations and, where necessary, supporting tables or working papers.

Chapter 10

Disposition

The foregoing chapters, together with Order TG-5-95, constitute our Decision and Reasons for Decision on matters considered in the RH-5-94 proceeding.

R. Illing
Presiding Member

R.L. Andrew
Member

J.A. Snider
Member

Calgary, Alberta
June 1995

Appendix I

Order TG-5-95

IN THE MATTER OF the *National Energy Board Act* ("the Act") and the regulations made thereunder; and

IN THE MATTER OF and application by Westcoast Energy Inc. ("Westcoast") dated 21 October 1994, as amended, for approval of interim and final tolls pursuant to subsection 19(2) and Part IV of the Act and filed with the National Energy Board ("the Board") under File No. 4200-W005-8.

BEFORE the Board on 22 June 1995.

WHEREAS Westcoast, by application dated 21 October 1994, as amended, applied to the Board for an order or orders under subsection 19(2) and Part IV of the Act fixing just and reasonable tolls that Westcoast may charge, effective 1 January 1995, for raw gas transmission, processing and residue gas transportation services that it provides;

AND WHEREAS the Board, expecting that it would not render a final decision regarding Westcoast's tolls until sometime in the new year, issued Order TGI-2-94 which authorized Westcoast to charge, on an interim basis effective 1 January 1995, tolls that would yield an increase in a typical service movement from Zone 1 to the export point of Zone 4 of 5% over the 1994 approved tolls;

AND WHEREAS the Board held a public hearing pursuant to Hearing Order RH-5-94, as amended, in Vancouver, British Columbia during which time the Board heard the evidence and arguments presented by Westcoast and all interested parties;

AND WHEREAS the Board's decisions on Westcoast's application are set out in its RH-5-94 Reasons for Decision dated June 1995 and in this Order;

IT IS ORDERED THAT:

1. Westcoast shall calculate new tolls in accordance with the decisions set out in the RH-5-94 Reasons for Decision and with this Order and shall forthwith file with the Board for approval, and serve on all intervenors to the RH-5-94 proceeding, new tariffs implementing these new tolls;

2. Westcoast shall, for accounting, tollmaking and tariff purposes, implement procedures to conform with the Board's decisions outlined in the RH-5-94 Reasons for Decision;

3. Order TGI-2-94, which authorized tolls that Westcoast may charge on an interim basis pending a final decision on above-mentioned application, is revoked and the tolls that have been authorized thereunder are disallowed as of the end of the day on 31 July 1995;

4. Westcoast shall charge on a final basis, for service commencing 1 January 1995, tolls authorized by paragraph 1 of this Order;

5. Westcoast is directed to refund that part of the tolls charged by the Company under Order TGI-2-94 which is in excess of the tolls determined by the Board to be just and reasonable in this Order or, where applicable, to recover the amount by which the tolls contemplated in this Order exceed the tolls charged by the Company under Order TGI-2-94, together with carrying charges on the amount so refunded or recovered at the rate of return on rate base approved in the RH-5-94 Reasons for Decision;

6. The refund or recovery authorized by this Order shall be effected without delay;

7. Westcoast shall file with the Board forthwith, and serve on all interested parties to the RH-5-94 proceeding, new tariffs, including general terms and conditions, and tolls conforming with the decisions set out in the RH-5-94 Reasons for Decision dated June 1995 and with this Order; and

8. Those provisions of Westcoast's tolls and tariffs, or any portion thereof, that are contrary to any provision of the Act, to the Board's RH-5-94 Reasons for Decision dated June 1995 or to any Order of the Board including this Order, are hereby disallowed.

NATIONAL ENERGY BOARD

J.S. Richardson
Secretary

Appendix II

List of Issues

This list is intended to assist all parties in defining the key issues to be addressed at the hearing. This will not preclude the Board from dealing with other issues which are normally raised by virtue of the Board's mandate pursuant to Part IV of the Act.

At the hearing, the Board will consider, *inter alia*, the following issues:

1. The appropriate rate base, throughput and cost of service for the 1995 test year.

2. The appropriate cost for funded and unfunded debt.

3. Whether the person-year utilization and the salary and wage increases proposed for the 1995 test year are appropriate.

4. Whether the allocation of expenditures among utility operating and maintenance expense, utility capital and non-utility is appropriate for the 1995 test year.

Appendix III

List of Previously Distributed Documents

(a) National Energy Board Hearing Order RH-5-94

(b) Letter dated 9 December 1994 and Order TGI-2-94

(c) Letter dated 31 January 1995 and Order AO-1-RH-5-94

Copies of these documents are available on request from:

Regulatory Support Office
National Energy Board
311 Sixth Avenue S.W.
Calgary, Alberta
T2P 3H2
(403) 292-4800

Facsimile: (403) 292-5503

Appendix IV

Westcoast Energy Inc. System Map - Tolling Zones

Figure a4-1
Westcoast Energy Inc. System Map - Tolling Zones

Appendix IV

Westcoast Energy Inc. System Map - Tolling Zones