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Pacific Northern Gas (N.E.) Ltd.

Application for a Certificate of Public Convenience and Necessity to Acquire and Operate the North Pine Fuel Gas Pipeline

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Decision
and Order G-136-18

July 20, 2018

Before:

W. M. Everett, QC, Panel Chair
H. G. Harowitz, Commissioner
B. A. Magnan, Commissioner

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1.0 Introduction

1.1 Proceeding at a glance

Date of application	December 4, 2017
Approvals sought	• Pacific Northern Gas (Northeast) Ltd. (PNG[NE])seeks approval from the British Columbia Utilities Commission's for a Certificate of Public Convenience and Necessity, pursuant to section 45 of the *Utilities Commission Act*, to acquire ownership of and to operate a fuel gas pipeline to provide service to the AltaGas Northwest Processing Limited Partnership at its North Pine Facility.
British Columbia Utilities Commission Panel	• William Everett, QC (Chair) • Howard Harowitz • Bernard Magnan
Registered interveners	• British Columbia Old Age Pensioners' Organization *et al.* (BCOAPO)
Regulatory process	• One round of Information Requests • PNG(NE) Written Final Argument and Reply Arguments • Intervener's Final Argument
Date of Decision	July 20, 2018

1.2 Background

Pacific Northern Gas (Northeast) Ltd. (PNG(NE)) is a public utility under the *Utilities Commission Act* (UCA) that owns and operates a natural gas transportation system and distributes gas to over 21,000 residential, commercial and industrial customers in the British Columbia municipalities of Fort St. John, Dawson Creek and Tumbler Ridge, Doe River, Pouce Coupe, Rolla, Tomslake, the District Taylor and Pink Mountain.[1]

PNG(NE) filed an application for approval from the British Columbia Utilities Commission (BCUC) for a Certificate of Public Convenience and Necessity (CPCN) to acquire ownership of and to operate (Acquire, Acquisition) a fuel gas pipeline to provide service to AltaGas Northwest Processing Limited Partnership's (AltaGas NPLP) North Pine Facility (Application).[2]

The proposed transaction is between two related parties: PNG(NE) and AltaGas NPLP are both wholly owned subsidiaries of AltaGas Ltd. (AltaGas).[3]

AltaGas NPLP recently completed the construction of the first phase of its North Pine Facility, a 20,000 Bbls/day natural gas liquids separation and handling facility located approximately 40 kilometers northwest of Fort St. John, British Columbia (the North Pine Facility). The facility was commissioned and became operational on November 9, 2017.[4]

[1] Exhibit B-1, p. 3.
[2] Exhibit B-1, Application, p. 3.
[3] Exhibit B-1, p. 3, p.5.
[4] PNG(NE) Final Argument, p. 3.

The North Pine Facility is serviced by three pipelines: two pipelines to transport the condensate and natural gas liquid (NGL) feedstock products for the facility (the Liquids Supply Pipelines); and a fuel gas pipeline to supply an estimated 280,000 GJ per year for phase one, doubling to 560,000 GJ per year with the completion of phase two of this project (the Fuel Gas Pipeline).[5] The Liquids Supply Pipelines and the Fuel Gas Pipeline were constructed by AltaGas NPLP, using the same pipeline right of way.[6]

Currently, AltaGas NPLP owns and is operating the North Pine Facility, the Liquid Supply Pipelines and the Fuel Gas Pipeline.[7]

PNG(NE) was approached by AltaGas NPLP, offering PNG(NE) the opportunity to acquire the Fuel Gas Pipeline and provide transportation service to the North Pine Facility.[8] If the Acquisition is approved, PNG(NE) intends to provide transportation service to AltaGas NPLP under a transportation service agreement (TSA) with AltaGas NPLP for an initial period of 20 years, including the following terms:

- The rate will be the Small Industrial Service Rate (RS10) for the contract demand; and
- A firm annual contract demand of 280,000 GJ and a monthly take-or-pay commitment based on equivalent of 240,000 GJ per year.[9]

In the event that AltaGas NPLP completes Phase 2 of the North Pine Facility, fuel requirements are expected to double to 560,000 GJ per year and the contract for service with PNG(NE) could be subject to a renewal term of up to 20 years.[10]

PNG(NE) and AltaGas NPLP have entered into a Cost Reimbursement Agreement (CRA) which establishes the assets to be acquired and sets the maximum purchase price at $1.8 million.[11] The final purchase price is estimated to be $1.712 million.[12]

2.0 Statutory and regulatory framework

Pursuant to section 45(1) of the UCA, "a person must not begin the construction or operation of a public utility plant or system, or an extension of either, without first obtaining from the Commission a certificate that public convenience and necessity require or will require the construction or operation."

Section 45(8) stipulates that "[t]he commission must not give its approval unless it determines that the privilege, concession or franchise proposed is necessary for the public convenience and properly conserves the public interest."

Panel discussion

It is important to note that the proposed Acquisition of the Fuel Gas Pipeline not only contemplates a change in ownership of an already existing/operating asset, but also a change in the status of that asset, from non-regulated to regulated. More specifically, since the Fuel Gas Pipeline is currently owned and operated by AltaGas NPLP solely for the purpose of providing fuel gas to its own operation, the facility does not currently

[5] Exhibit B-1, p. 1.
[6] Exhibit B-1, p. 8.
[7] Exhibit B-3, BCUC IR 2.1.2.
[8] Exhibit B-1, pp. 5–6.
[9] PNG(NE) Final Argument, p. 1
[10] Exhibit B-1, p. 13.
[11] Exhibit B-1, p. 9.
[12] PNG(NE) Final Argument, p. 5.

come under the purview of the UCA. It is solely as a result of the proposed Acquisition that the Fuel Gas Pipeline would become a regulated asset.

An assessment of the public convenience and necessity therefore must include an examination from the perspective of whether the public interest is served by bringing a non-regulated asset into the regulatory regime.

In examining this aspect of the public interest, the Panel is guided by a principle of regulation that the BCUC has set out and relied upon in a number of prior decisions. In its report on alternative energy solutions, the BCUC stated that regulation is "only appropriate where required and is driven by the inability of competitive forces to operate with greater efficiency and effectiveness than a sole service provider."[13] In the same report, the BCUC also has stated that where a regulated utility seeks to participate in an activity where there are no monopoly characteristics, it must demonstrate that its participation is necessary and in the public interest, to the exclusion of other forms of enterprise.[14]

Within this context, the Panel has identified two aspects to the question of public convenience and necessity that should be examined:

- The necessity to Acquire the Fuel Gas Pipeline pursuant to the CRA; and
- The expected benefits from Acquisition of the Fuel Gas Pipeline.

3.0 Necessity to acquire ownership of and operate the Fuel Gas Pipeline

PNG(NE) states that the Fuel Gas Pipeline project is needed because AltaGas NPLP has requested that PNG(NE) provide natural gas transportation service to its North Pine Facility. In order to provide this service and to transport fuel gas from the CNRL West Stoddard Gas Plant to the North Pine Facility, the construction of a natural gas pipeline was essential.[15]

AltaGas NPLP will continue to own and operate the two Liquids Supply Pipelines which connect the Townsend Truck Terminal to the North Pine Facility. PNG(NE) does not propose to acquire or operate the Liquids Supply Pipeline as "PNG(NE) does not own or operate any NGL pipelines and hence does not have the core competency to own and operate NGL pipelines."[16]

In the Application, PNG(NE) states the Fuel Gas Pipeline is necessary to provide service to a single new customer.[17] PNG(NE) further states that there were no alternatives to constructing the new pipeline "other than to burn the products of the North Pine Facility which would have resulted in increased operating costs and greenhouse gas emissions for the facility.[18]"

AltaGas NPLP considered owning and operating the Fuel Gas Pipeline. However, since the operation and maintenance of fuel gas pipelines is not core to the AltaGas NPLP North Pine Facility business, PNG(NE) was approached to Acquire the Fuel Gas Pipeline. PNG(NE) states that "factors influencing this decision are not dissimilar to that of other industrial customers served by PNG(NE), including reduced project capital and

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[13] BCUC FortisBC Energy Inc. Inquiry into the Offering of Products and Services in Alternative Energy Solutions and Other New Initiatives Report (AES Report) p. 14.
[14] AES Report, p. 22.
[15] Exhibit B-1, p. 11.
[16] Exhibit B-3, BCUC IR 1.5.
[17] Exhibit B-1, p. 11.
[18] Exhibit B-3, BCUC IR 3.1.

operating and maintenance costs related to fuel gas supply."[19] PNG(NE) indicates that there are no known regulatory impediments to AltaGas NPLP owning and operating the Fuel Gas Pipeline.[20]

Position of the parties

BCOAPO did not question or oppose PNG(NE)'s need to Acquire the Fuel Gas Pipeline[21].

Panel discussion

The Panel is satisfied that there is a need for the Fuel Gas Pipeline. The Application adequately examines and dismisses alternatives such as burning the products of the North Pine Facility and alternate routing of the pipeline.

However, the Panel draws a distinction between demonstrating the need for the pipeline and demonstrating the need for the Acquisition by PNG(NE). On the question of a demonstrated need to Acquire the Fuel Gas Pipeline the Panel notes the following:

From the perspective of the customer (AltaGas NPLP)

- AltaGas NPLP is currently operating the integrated system without any involvement of PNG(NE).
- While acknowledging that AltaGas NPLP may be motivated by considerations of "reduced project capital and operating and maintenance costs related to fuel gas supply", the Panel has no evidence to suggest that the plant's ongoing viability is in any way jeopardized in the absence of the transfer of ownership/operation of the Fuel Gas Pipeline.

For these reasons, the Panel finds that the necessity to Acquire the Fuel Gas Pipeline has not been established from the perspective of the customer.

From the perspective of PNG(NE) and its customers

- The pipeline is not connected to any portion of PNG(NE)'s other infrastructure. Further, the Panel notes that the Application is not based on any stated need in terms of the existing system infrastructure (e.g. need for additional capacity, safety issues, reliability of service).
- Demand for the service is limited to one (new) customer who is already being adequately served. While the possibility exists that other customers may come along some time in the future, none have been identified at present.

For these reasons, the Panel finds that the necessity to Acquire the Fuel Gas Pipeline has not been established from the perspective of PNG(NE) or its customers.

From the perspective of the regulatory framework

- As noted, this Application requires analysis of whether there is a need to bring an otherwise non-regulated asset into the regulatory sphere. The Panel is guided by the BCUC's articulated principle that regulation should be exercised if/when regulation is the only alternative, to the exclusion of other forms of enterprise. Clearly, given that AltaGas NPLP is currently operating the facility and receiving fuel from its wholly owned pipeline, another form of enterprise has not only been identified, but proven to be effective.

[19] Exhibit B-3, BCUC IR 3.2.
[20] Exhibit B-2, BCOAPO IR 3.0.
[21] BCOAPO Final Argument, p. 4.

For this reason, the Panel finds that the necessity to Acquire the Fuel Gas Pipeline has not been established from the perspective of general regulatory principles.

The Panel therefore finds that the Application does not establish a demonstrated public need, as required by section 45(1) of the UCA.

4.0 Expected benefits from the Acquisition of the Fuel Gas Pipeline

In its Application, PNG(NE) states that there are two primary benefits associated with Acquisition of the Fuel Gas Pipeline project: financial benefits and development opportunities.[22]

4.1 Financial benefit

PNG(NE) describes the financial benefit of the Fuel Gas Pipeline to other customers in the Fort St. John/Dawson Creek service area as being achieved "...in the form of the positive rate impacts of the incremental margin realized from providing service to AltaGas NPLP."[23]

PNG(NE) presents the results of a net present value (NPV) analysis under two different volume scenarios: volumes at the minimum take-or-pay volume of 240,000 GJ per year, and at the contracted firm demand of 280,000 GJ per year.

Table 1: NPV of Incremental Margin Over 20 Years – Standard Depreciation[24]

	240,000 GJ / Year (minimum take-or-pay volume)	280,000 GJ / Year (contracted firm demand)
Incremental Margin over 20 years	$976,859	$1,502,819
NPV of Incremental Margin	$523,266	$838,220

The above results are based upon a yearly depreciation rate of 1.94 percent for the Fuel Gas Pipeline assets, which is the depreciation rate for PNG(NE)'s distribution assets. PNG(NE) states that applying this depreciation rate to the $1.8 million capital cost will result in an undepreciated balance of $1,119,600 at the end of the initial twenty year TSA term.[25] Further, in the event that the assets are no longer used and useful at the end of the twenty year term, PNG(NE) states that it expects the asset to be "deactivated and retired for regulatory accounting purposes."[26] This would result in the sum of the undepreciated balance plus deactivation costs being recorded in the plant gains/losses deferral account and amortized over five years (resulting in an estimated annual revenue deficiency of approximately $285,000 for five years).[27]

PNG(NE) provides estimates of the average bill impact for two scenarios, as follows:

- Under a scenario where the customer takes 280,000 GJ / Year for the contract term, followed by a further renewal for twenty years at the same volumes, the average residential customer in the Fort St. John/Dawson Creek service area would see a $2.34 reduction in their annual bill.

[22] Exhibit B-1, p. 11.
[23] ibid., p. 11.
[24] Ibid., p. 12.
[25] Exhibit B-3, BCUC IR 6.2.
[26] Exhibit B-3, BCUC IR 6.2.1.
[27] Exhibit B-3, BCUC IR 6.2.1.

- Under a scenario where the customer takes only the minimum take-or-pay volume for the contract term and does not renew, the average residential customer will see a positive bill impact over the first twenty years, followed by a negative bill impact in the five years following (due to the write-off of the asset). Aggregating the two opposing impacts, PNG(NE) estimates an averaged negative impact to residential customers, in terms of a $0.35 bill increase per year for the twenty five years.[28]

PNG(NE) presents a second set of NPV calculations based on an accelerated depreciation schedule that amortizes the asset over the twenty year life of the TSA (at a flat rate of 5% per year).

Table 2: NPV of Incremental Margin Over 20 Years – Accelerated Depreciation[29]

	240,000 GJ / Year (minimum take-or-pay volume)	280,000 GJ / Year (contracted firm demand)
Incremental Margin over 20 years	$242,089	$768,048
NPV of Incremental Margin	$6,243	$321,198

In response to BCOAPO IR1.2, PNG provides an estimate of a simple averaged bill impact based on the $242,089 Incremental Margin value (see Table 2, column 1) for an average residential customer as a reduction of $0.38 in their annual bill.[30]

In its Reply Argument, PNG(NE) states that during the course of the proceeding, the following changes occurred that have a positive impact on the NPV analyses: interim approval of RS10 change effective January 1, 2018 increasing from $0.6602 used in the NPV analyses to $0.7273/GJ; and final capital cost decreasing from $1.8 million used in the NPV analyses to $1.712 million.[31]

PNG(NE) submits that there are "negligible"[32] financial and operational risks associated with the service provided to AltaGas NPLP under the TSA, as any risks have been mitigated through contractual arrangements.[33] Specifically, PNG(NE) states that the CRA includes a price cap of $1.8 million and the final capital costs are lower than this amount at $1.712 million. Further, PNG(NE) states that all capital and operating costs will be recovered through the RS10 tariff to be paid by AltaGas NPLP under the terms of the TSA. Finally, PNG(NE) highlights that, in the event that the TSA is terminated before the end of the 20 year primary term, PNG(NE)will be entitled to "…the net present value of the Firm Demand Charge for the Contract Demand for the remainder of the Primary Term."[34]

Position of the parties

In its Final Argument, BCOAPO states that following "a thorough examination of the costs, benefits, and risks of this project, BCOAPO has no objection to the Utility's application for approval of the North Pine Fuel Pipeline CPCN."[35]

[28] Exhibit B-2, BCOAPO IR 9.2.
[29] Exhibit B-1, p. 12.
[30] Exhibit B-2, BCOAPO IR 1.2.
[31] PNG(NE) Reply Argument, pp.1-2 .
[32] Exhibit B-1, p. 13-14.
[33] Exhibit B-1, p. 13.
[34] PNG(NE) Final Argument, p. 6.
[35] BCOAPO Final Argument, p. 4.

Panel discussion

Based on PNG(NE)'s estimates, the expected benefit to existing ratepayers will fall between a bill increase of $0.35 and a bill decrease of $2.34 per year (between plus three and minus twenty cents per month). The Panel does not consider this benefit to be sufficiently attractive to support on its own the approval of acquiring the asset.

The Panel also reviewed PNG(NE)'s confidential filing containing updated financial projections that reflect the recent rate increase (RS10) and lower capital costs. While the numbers change somewhat, the Panel considers the magnitude of the changes in expected bill impacts to be immaterial in the context of our findings.

The Panel recognizes that these estimates do not include the possible added benefits that might arise from such events as: AltaGas NPLP extending the contract for years beyond the current twenty years, at either current volumes or the expanded volumes if phase 2 moves ahead; and/or the addition of other customers being served on this line. That said, the Panel considers these positive impacts are in the realm of possibility, but not yet established as probable.

In counterpoint to the possible upside benefits (noted in the immediately preceding paragraph), the Panel does not agree with PNG(NE)'s assertion that the financial and operational risks are "negligible". Possible risks from the Acquisition include (but are not limited to): unforeseen pipeline failure and/or maintenance costs, the customer going out of business and or bankrupt, reliance on a single customer on a sole-purpose pipeline, the parent defaulting on its commitment, and non-renewal of the contract. The Panel does not view the risks as extraordinary, but we do assume them to be commensurate with the general risk of running a utility, which are not generally regarded as "negligible". To that point, if the risks of operating a utility were negligible, the Cost of Capital determinations that establish target rates of return for utilities would not include any meaningful risk premium.

Everything considered, existing ratepayers are expected to realize a very small benefit from Acquisition under the base case. And while the possibility exists that ratepayers may realize additional benefits under one set of outcomes, the possibility also exists that they may incur the additional costs of adverse events that could arise from Acquisition of the new asset.

Having considered the above, **the Panel finds that the potential benefit to ratepayers is not sufficient or certain to establish the public convenience and necessity required to justify Acquisition of the asset on the basis of financial benefits.**

4.2 Development opportunities

PNG(NE) submits that the Acquisition of the Fuel Gas Pipeline provides an opportunity "to provide a platform to attract and serve additional customers in the area."[36] The Fuel Gas Pipeline's proximity to the Montney gas exploration region would enable PNG(NE) to attract and provide service to new industrial customers that may choose to locate in the vicinity of the Fuel Gas Pipeline.[37]

PNG(NE) further states that:

> [T]he Fuel Gas Pipeline is situated in the central part of the Montney shale formation which has significant industrial activity related to natural gas extraction. Further, the Fuel Gas Pipeline was designed with a riser located at the Beatton River road crossing for the purpose of future

[36] Exhibit B-1, p. 13.
[37] Exhibit B-1, p. 13.

expansion north to the area around Buick and south to areas in and around Shepherds Bush, providing the capability for future fuel gas deliveries to production facilities in these areas.[38]

PNG(NE) states that at present there are currently no additional customer requests for service that could be served by the Fuel Gas Pipeline, however the location of the pipeline positions PNG(NE) to capitalize on opportunities when economic activity increases.

Panel discussion

As PNG(NE) states, there are no current prospects for new customers requesting service. While the Panel does not rule out the possibility of customer growth, the case has not been made that this is anything more than a possibility.

The Panel therefore finds that the new customer opportunities are not sufficiently quantified or certain to establish the public convenience and necessity to justify Acquisition of the asset on the basis of development opportunities.

5.0 CPCN determination

The Panel finds that, pursuant to section 45(8) of the UCA, the public interest is not served by granting the CPCN because neither need nor benefit have been sufficiently established. More specifically as set out in Sections 3 and 4 of this Decision:

- the Panel finds that the Application does not establish a demonstrated public need, whether viewed from the perspective of the new customer for the service, PNG(NE)'s customers, or general regulatory principles;
- the Panel finds that the potential benefit to ratepayers is not sufficient or certain to establish the public convenience and necessity required to justify Acquisition of the asset on the basis of financial benefits; and
- the Panel finds that the new customer opportunities are not sufficiently quantified or certain to establish the public convenience and necessity to justify Acquisition of the asset on the basis of development opportunities.

For the reasons above, **PNG(NE)'s Application pursuant to section 45 of the UCA, for a CPCN to acquire ownership of and to operate the Fuel Gas Pipeline to provide service to AltaGas Northwest Processing Limited Partnership at its North Pine Facility is denied.**

[38] Exhibit B-3, BCUC IR 9.2.

Dated at the City of Vancouver, in the Province of British Columbia, this 20th day of July 2018.

Original signed by ____________________________________
W. M. Everett, QC
Panel Chair / Commissioner

Original signed by ____________________________________
H. G. Harowitz
Commissioner

Original signed by ____________________________________
B. A. Magnan
Commissioner