Stargas Utilities Ltd.
Cost Summary
Presented with Notes
December 14, 2016 BCUC SRP

Commodity Costs			Notes	BCUC Status/Other Detail
Shell Energy North America (Canada) Inc.				*Commission staff have asked for further*
Cost of natural gas		$122,487	1	*details on our annual natural gas purchase*
Fortis BC				*plan and our response posted to their*
Basic & administartive	$ 7,980			*Website November 28, 2016*
Transport demand	60,328			
Transport	27,373	95,681	2	
Commodity costs		218,168		
Refund prior year overrecovery		(19,870)	3	
		198,298		
Forecast recovery to October 31				
Recovery to October 31, 2016 at $2.95	8,023.5	23,669	4	
Balance to be recovered		174,629		
Deliveries against which recovery projected	33,070.1	**$5.28**	5	**Approved October 28, 2016 Order G158-16**
Projected 2016 fiscal year deliveries	41,093.6			

Delivery Costs				
FortisBC Alternative Energy Services Inc.				
Variable monthly charge	$ 62,057			
Fixed monthly charge	58,444	$120,501	6	**Contract approved G93-09**
Adminstrative Costs				
Professional fees	$ 6,200		7	average cost - 3 years prior $5,922
Office and sundry	15,028		8	see clarification response -avg prior 3 -$15,978
Insurance	13,130		9	average cost - 3 years prior $15,013
Management fees	88,127	122,485	10	Rate applications - current estimate $14,000
				Hourly rate increase - as per precedent
				General - further submission to come
Revenue contributions				
Net meters and lines	(170)		11	average - 3 years prior $1,280 (new customers)
Basic charges	(62,990)		12	average - 3 years prior $60,553
Sundry revenue	(4,102)	(67,262)	13	average -3 years prior $3,760
Income tax		9,300	14	pro-forma calculation 3 prior years $8,647
Debt service				
Interest on operating facility	4,190		15	**Approved G 157-12**
Interest on shareholders' advance	2,400		16	approval sought in current application
Debt service in lieu of amortization	56,241	62,831	17	Please review attached notes
Investor's return				
Preferred share dividend	28,500		18	**Approved G80-02, G163-06**
Catch-up dividend arrears	6,794	35,294	19	**Approved G157-12**
		$283,149	20	
Projected 2016 fiscal year deliveries	41,093.6	**$6.89**		

Commodity rate of $5.28 approved, effective November 1, 2016, BCUC Order G-158-16; Delivery rate of $6.89 the subject of continuing review; if approved it a $.49 reduction for the current $7.38 per gj.

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Notes to Stargas Cost Summary

Introduction: We considered it useful to offer, in advance of the meeting, a summary of the various items under discussion as relates the approved Commodity price adjustment ($2.95 to $5.28 per gj) and the under consideration Delivery rate (proposed as $6.89, a reduction from $7.38).

Commodity Pricing:

1. Commodity: We are projecting the purchase of 41,604 gj's at an average cost of $2.94 per gj; our estimate included actual purchases June through September at $2.19 per gj and purchases October through May 2017 at an average price $3.06 per gj per forecast pricing as of October 19th, 2016. We have seen some early fall off in prices that if continued, will contribute to a gas cost over recovery that will be refunded to customers as a reduction of costs to be recovered in fiscal 2018. While past performance not a guarantee of that in the future, our fiscal 2016 purchases were achieved at an average cost of $1.70 per gj; had we sourced the commodity from Fortis (as a residential customer) our average cost through that year would have been $3.12. Had we purchased our winter delivery's as a commercial Rate 5 customer (Fortis the supplier of natural gas) we would have incurred a cost approximating $58,600; our purchases for that period had a cost of $49,637.
2. Fortis BC – Rate 25: Under our rate classification (that based on volume purchased) included as elements within our commodity costs, we pay a basic and administration fee of $665 monthly, a transport charge to bring the gas to the resort boundary as well as a demand transport charge designed to compensate Fortis for fluctuations in throughput volumes. We forecast that that charge (based upon the highest volume month in the previous calendar year), currently $4,818 month, will increase to $5,320 monthly January 1st, 2017. Note that were Stargas ratepayers to consume natural gas equally in each of the twelve months of the year, this charge would be eliminated – it identified here, to provide context to the consequence of the load factors applied to our highly seasonal deliveries.
3. Operation of the Gas Cost Variance Account: Stargas neither earns a profit nor is exposed to a loss in the commodity; any loss/profit is recovered/refunded to ratepayers by an adjustment to the costs to be recovered in the following years commodity rate. In the current calculation we are refunding $19,870 to ratepayers reducing the costs to be recovered to $198,298.
4. Recovery of costs: We will, through June to October 31, 2016 recover commodity costs at the rate of $2.95 per gj so that, recovery of the $198,298 is based on delivery volumes projected for the period from November 1st to May 31, 2017. We project fiscal year deliveries will aggregate 41,093.6 gj's and of those, 8,023.5 gj's will have been delivered at the $2.95 price.
5. Commodity price effective November 1, 2016: we expect to recover the $174,629 remaining to be captured by charging $5.28 per gj through the balance of our fiscal year; if and to the extent our volume estimates and or price estimates vary, as inevitably they will, whatever the over or under recovery, will (on the pass through basis upon which we operate) be reflected in the following years costs**. The $5.28 commodity rate, encompassing all of the above, was approved October 27, 2016 by BCUC Order G-158-16.**

Delivery Costs:

6. Fortis Alternate: Costs incurred pursuant to a service contract running to November 30th, 2019 (the contract reviewed and approved by the **BCUC, Order G93-09** stipulated that costs incurred thereunder be a component of cost of service). The variable charge covers Fortis activity in servicing the physical aspects of the operation and maintenance of the Stargas delivery system; the rate is adjusted to reflect a proportionate share of the increases in deliveries over the base year such that the applicable rate in the test year $1.51; it $1.62 per gj in the base year. Administrative services are covered by a fixed monthly charge subject to CPI adjustment (it $4,000 in the base year and $4,187 currently) plus $15 per customer added over those in place when the contract signed.
7. Professional fees: We pay KPMG for their annual review of our financial statements and preparation of tax returns as well as modest amounts to our company legal counsel in sustaining our corporate registration.
8. Office and sundry: Our financial model includes an estimate of these costs based on revenues (accounting for the increment from $14,989 to $15,028). We refer to the clarification to the SSPOA follow up filed with Commission as addressing the underlying costs represented in this account classification.
9. Insurance: We provide coverages as required by the resort and as prudent with respect to directors and officers liability of a natural gas utility.
10. Management fees: Our application contemplates an aggregate management fee of $88,127; included in that estimate was $8,044 in respect of the preparation of the BCUC applications and in responding to interrogatories, with the balance $80,023 a representation of those amounts to incurred on an annual basis.
    a. Application costs: we reported, in our response to IR#1 that we'd incurred 83 hours to the date of its filing at a cost of $11,973 and will expend further hours preparing for the December 14th meeting (and additional hours will be required thereafter). Commission staff has raised the prospect of deferring a portion of these costs, writing off 50% in the current year and the balance in the fiscal year ending 2018; we are amenable, should that be their determination and would, given the expected frequency of applications addressing delivery rates, accept inclusion of 1/3 of the estimated cost ($14,000) in the current year with the remaining balance charged to income over the following two fiscal years.
    b. Hourly rates: The BCUC granted a rate increase in our 2012 full rate application based upon increases in the provinces Consumer Price Index and we, following that precedent, are seeking approval to adjust Okanagan Funding rates accordingly (they've be unchanged from 2014 through to May 31, 2016).
    c. Annual costs: The hours tabulated and paid to Okanagan Funding are the hours incurred; we intend to file additional detail in advance of the meeting on the nature of and time required to maintain and efficiently administrate Stargas. Included within that information, will be detailed accounts of the time charged Stargas by Okanagan Funding in completing its November reports – while in the past I've accepted the hours incurred

with only peripheral narrative as to variances from the norm, both of the accountant and administrator were instructed to provide complete detail on hours incurred in producing November reports.

11. Meters and lines: We levy, as approved by the BCUC, a 10% administration charge for new installations at the resort – only one of which was forecast in the test year.
12. Stargas Basic Revenue: Our tariff provides for a monthly fixed fee per customer at one of three levels - $15 residential, $25 small commercial and $100 large commercial and was structured, originally, to recover the fixed fees included in the Fortis Alternate contract. In negotiating the current Fortis service contract we were able to exact a modest increment in this account as a contribution to the balance of our operating costs.
13. Sundry revenue: we generate income from customers not satisfying their accounts on schedule and earn commissions on the collection and remittance of provincial sales tax. The former item has a corresponding cost in the interest incurred on our operating facility.
14. Income tax: the amount here, based, on a pro-forma calculation of the tax liability as estimated on test year forecast results.
15. Interest on operating facility: The seasonal nature of our deliveries results in uneven cash flows through the year; accordingly, we rely on an operating line provided by our bank to meet obligations as due, and have BCUC approval (**BCUC Order G157-12**) to include same in the determination of cost of service.
16. Interest on shareholder's advance: We are seeking approval to include this cost in cost of service, as we assert it analogous to financing costs incurred on the operating line. If allowed, we are agreed to reduce the amount included based on an interest rate at 1% over that paid on our operating line. The $2,400 reflected in the attached would be reduced to $1,800.
17. **Debt Service in lieu of amortization**: Our application presented on the basis that a change in the cost of service calculation, to include term debt principal and interest costs would accomplish two complimentary objectives; the first provide a delivery rate reduction to ratepayers and the second, allow CMI98 to earn both a return on and <u>of</u> its investment in preferred shares. Stargas notes here, the following as raised in Commission IR#1; "Given that amortization/depreciation provides a "regulated enterprise the opportunity to recover its capital investment" and the following from BCUC Order 157-12 – in referring to the dividends contemplated on its preferred shares the comment made that "Stargas has not included any additional return on equity, <u>nor have they included a long-term debt return"</u>, in their revenue requirement" (emphasis added).

    We recognize then that the decision before the Commission on the proposed change to cost of service, the subject of yet further consideration and offer the following discussion of an alternative* to that contemplated in the application:

    a. Commission approves inclusion of debt service in lieu of amortization, as requested; in each of the test and two following years, amortization expense of $54,804 is replaced by debt service of $56,241 (assumes June 1, 2016 drawdown in the test year) while dividends on preferred shares reduced from $38,000 to $28,500 – an $8,063 annual

reduction in cost of service accounting for an approximate $.20 reduction in our delivery rate.

b. Commission directs Stargas to continue the inclusion of amortization in its cost of service through the test and two following fiscal years, debt service excluded, so that the reduction in cost of service only that of the preferred share dividend reduction of $9,500 accounting for an approximate $.23 reduction in our delivery rate.

*each of the alternatives presupposes Commission approval of the drawdown of the proposed replacement term loan.

Under either scenario, Stargas undertakes, hereby, to file an application with respect to its cost of service calculation during the course of its fiscal year ending May 31, 2019 so that, effective with and in its fiscal year ending May 31, 2020, there agreement as to those elements then to be included/excluded in the calculation – we note that amortization will have been reduced to $16,076 and suggest that at that time, we'd propose inclusion of interest on term debt within the calculation (thereby, generating in our delivery rate cash flows requisite to servicing term financing).

18. Preferred share dividends: If the proposed refinancing approved, Stargas will redeem $100,000 of the outstanding preferred shares and, on an annual basis thereafter, pay an annual dividend at the benchmark return plus 75 basis points (currently 9.5%). Note that in the fiscal year ended May 31, 2017, the dividends recorded and paid will be determined by the date on which the redemption is approved (if approved). Stargas has included in its test year summary, the annual dividend as if the redemption were to have occurred on June 1, 2016; while electing to do so will understate the allowed cost of service for the current year, including an estimate of the actual amount to be paid in the fiscal year would result in an overstatement of that element in subsequent years.
On August 15, 2002, Stargas applied to the Commission for approval to issue cumulative preferred shares. Commission **Order G-80-02** approved the issuance of $400,000 of cumulative preferred shares with a dividend rate equal to the Commission's annual benchmark return on equity plus 75 basis points. From fiscal 2002 through fiscal 2006, accumulated unpaid dividends amounted to $135,887 and no return on equity was included in the revenue requirement. In order to provide a return to Stargas' shareholders, Commission Order **G-163-06** directed the Company to pay an annual dividend on its outstanding preferred shares. Stargas has declared and paid dividends annually in accordance with Order G-163-06 between fiscal 2007 and fiscal 2016.

19. Considering that no return on equity was included in the revenue requirement from fiscal 2002 through fiscal 2006, the Commission considered it appropriate that the accumulated unpaid dividends be declared and paid to the shareholder if declared and paid in the same fiscal year. The Commission approved Stargas' request to amortize the accumulated unpaid dividends in the revenue requirement over a period of twenty years and directed Stargas to declare and

pay $6,794 in cumulative preferred share dividends in each fiscal year (**G157-12**). $108,711 remains to be paid in sixteen annual payments of $6,794.

20. Projected rate (assumes amortization remains an inclusion in cost of service)

Cost of service, as filed		$ 283,149
Adjustments:		
Reduction in interest rate on shareholder's advance		(600)
Return to inclusion of amortization	$ 54,804	
and exclusion of debt service	(56,241)	(1,437)
Estimated Application and Refinancing costs	$ 14,000	
Amount to be deferred (2/3)	9,333	
To be included in test year cost of service	4,667	
Included in management fee estimate	8,044	(3,377)
Revised cost of service		$ 277,735
Projected deliveries (GJ's)	41,093.6	**$6.76**

If the foregoing accepted by the Commission our delivery rate would be reduced from $7.38 per GJ to $6.76 per GJ.