



March 10, 2021

Sent By E-mail

British Columbia Utilities Commission
6th Floor - 900 Howe Street
Vancouver, BC V6Z 2V3

Attention: Patrick Wruck, Commission Secretary

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Your reference	Our reference
Project No. 159898	1000385944

Dear Mr. Wruck:

Kinder Morgan (Jet Fuel) Inc. ("PKMJF") 2019 Tariff Filing – Vancouver Airport Fuel Facilities Corporation ("VAFFC") – Public (Redacted) Responses to BCUC IR No. 1

We are counsel for VAFFC in this matter and write to enclose a public (redacted) version of VAFFC's responses to BCUC Information Request No. 1.

If you have any questions, please contact the writer.

Yours very truly,

A handwritten signature in black ink, appearing to read "m. keen".

for Matthew D. Keen
Partner

MDK/roe

CAN_DMS: \138276439\1

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**Vancouver Airport Fuel Facilities Corporation (VAFFC) Response to British Columbia Utilities
Commission (BCUC) Information Request No. 1 - PUBLIC**

A. THE JET FUEL SYSTEM

**1.0 Reference: THE JET FUEL SYSTEM
Exhibit C2-36-2, VAFFC Direct Evidence, p. 5; InterGroup Report, p. 8;
Exhibit B-13, VAFFC IR 6.1
Forecast Volumes**

On page 5 of Exhibit C2-36-1, the Vancouver Airport Fuel Facilities Corporation's (VAFFC) Direct Evidence, VAFFC states:

Over the past 30 days, in light of the effects of the pandemic on air travel and hence aircraft fuel demand, YVR has averaged about 20 daily fuel tanker truck deliveries. Nominations on PKMJF's [PKM Canada (Jet Fuel) Inc.'s] system are approximately 20% of pre-pandemic levels. VAFFC and its members expect that air travel and fuel demand at YVR will ultimately return to pre-pandemic levels, but the pace and timing of that return is uncertain.

On page 8 of the InterGroup Report of Exhibit C2-36-1s, VAFFC further states that "PKMJF should be expected to work with its shippers to develop sound prospective forecasts of volumes, and to set tolls accordingly, to permit customers to plan their operations based on fixed unit costing for the shipping service."

In response to VAFFC Information Request (IR) 6.1, PKMJF indicates that a total of 703,386 cubic meters (m³) of jet fuel was shipped from the Westridge Marine Terminal in 2018 and that it "...expects the 2018 volumes and allocation between the shippers to continue until the VAFD [Vancouver Airport Fuel Delivery] project is in-service..."

1.1 Please discuss whether PKMJF has requested input from VAFFC regarding forecast shipping volumes over the test period and, if so, describe any input VAFFC provided.

Response:

No. PKMJF did not request input regarding shipping volumes for the test years from VAFFC or, to VAFFC's knowledge, from any VAFFC members, before PKMJF filed its Application.

Note that VAFFC itself does not ship on the JFL. Rather, it is VAFFC members that ship on the JFL. Air Canada is a VAFFC member and for some time, has been the only VAFFC member to ship on the JFL, but JFL tolls and conditions of service are important to all VAFFC members.

VAFFC understands that shippers, including Air Canada, provide PKMJF with regular operational forecasts of volumes requiring to be shipped from the Westridge Marine Terminal, including over the test period. These forecasts are typically for a period of 1-3 months.

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Please also see VAFFC's response to BCUC IR 1.1.1.

- 1.1.1 Please describe how VAFFC prepares its volume forecasts and how often these forecasts are updated.

Response:

Volume forecasts are prepared by member airlines of the VAFFC consortium based on their projected flight activity at YVR. Typically, airline members provide their jet fuel suppliers with monthly volume forecasts for each month of the year, which are updated regularly.

- 1.2 Please provide the actual volumes VAFFC shipped on PKMJF's jet fuel system (the Jet Fuel Line or JFL) in 2018, 2019, and 2020 (where known) and VAFFC's forecast for shipping volumes in 2020/2021.

Response:

VAFFC members (i.e., Air Canada) shipped the following actual volumes on the Jet Fuel Line in 2018, 2019 and 2020, in litres:

2018: 1,181,429,701 L
2019: 1,113,218,924 L
2020: 391,348,055 L

VAFFC forecasts that its members will ship 580,000,000 L on the Jet Fuel Line in 2021.

To be clear, these volumes are those transported by barge to Vancouver and then shipped on the JFL. VAFFC members flying from YVR also *consume* jet fuel shipped by other parties on the JFL, as well as jet fuel transported to YVR by tanker truck from Washington State and by train / tanker truck from Alberta.

- 1.2.1 Absent the effects of COVID-19 on air travel, did PKMJF forecast 2020 volumes to be in line with recent historical actuals? Please discuss.

Response:

VAFFC assumes that the reference to "PKMJF" in BCUC IR 1.2.1 is intended to be a reference to "VAFFC", and responds to this IR accordingly.

Yes, absent the effects of COVID-19 on air travel, VAFFC expected 2020 volumes on the Jet Fuel Line to be in line with recent historical actuals.

In fact, prior to the onset of the COVID-19 pandemic, VAFFC forecasted increased jet fuel consumption by members during 2020 due to the growth in air traffic at YVR. VAFFC did not forecast increased JFL shipments commensurate with the anticipated increase in jet fuel consumption due to capacity constraints

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on the Jet Fuel Line.

- 1.2.2 If VAFFC's forecast for 2021 differs significantly from the actual volume shipped in 2018, please discuss the reason(s) for the difference.

Response:

VAFFC's forecast for 2021 is significantly lower than the actual volume shipped in 2018, due to the ongoing impacts of the COVID-19 pandemic, which have resulted in a substantial decrease in air travel out of YVR, across Canada and around the world.

- 1.3 Please explain why, over the 30-day period described above, Vancouver International Airport (YVR) received an average of 20 tanker truck deliveries of jet fuel per day while nominations on the JFL decreased to approximately 20 percent of pre-pandemic levels.

Response:

The distribution of the transportation of jet fuel between tanker truck deliveries and transportation on the JFL depends entirely upon which member airlines were active during that period, as each member airline contracts with different fuel suppliers, and each fuel supplier uses different modes of transportation. The COVID-19 pandemic has skewed the typical distribution among modes of transportation because typical airline activity has varied widely from the norm.

- 1.3.1 Please provide a comparison of the cost of trucking and the effective toll for shipping on the JFL on a dollars per barrel basis.

Response:

The cost of trucking can vary, as it depends on several variables, including the source of the jet fuel that is being transported by truck. VAFFC also cautions that a comparison between the cost of trucking and the effective toll for shipping on the Jet Fuel Line has the potential to be misleading, since trucks are a less reliable form of transportation for jet fuel than pipelines, and VAFFC would never be able to replace all of the jet fuel currently being supplied by the Jet Fuel Line with truck deliveries.

Notwithstanding the foregoing, VAFFC considers that the estimate provided by PKMJF in its response to BCUC IR 2.2¹ for the cost to transport jet fuel by truck from the Parkland Refinery to YVR (\$1.110/Bbl) is lower than the typical trucking rates that VAFFC's member airlines have encountered in the past, which are generally closer to \$1.270/Bbl.

¹ Exhibit B-11.

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- 2.0** **Reference: THE JET FUEL SYSTEM
Exhibit C2-36-2, VAFFC Direct Evidence, pp. 9–10; InterGroup Report,
Appendix C, p. C-11
Forecast Volumes – Throughput Volumes Following Completion of the
VAFD Project**

On page 10 VAFFC's Direct Evidence, VAFFC states:

Once the VAFD becomes operational, VAFFC does not expect its members to cease all shipments of jet fuel on the Jet Fuel Line. Rather, VAFFC expects members will ship on the Jet Fuel Line opportunistically, when it makes economic sense to do so, taking into account different jet fuel source prices and overall transportation cost options.

- 2.1 Please describe the specific circumstances under which VAFFC envisions its members electing to ship on the JFL following completion of the VAFD project.

Response:

Please see VAFFC's response to Parkland IRs 1.1 and 1.2.

- 2.2 Please provide VAFFC's expectations for the frequency of shipments and forecast annual volumes on the JFL by its members following completion of the VAFD project.

Response:

Please see VAFFC's response to PKMJF IRs 1.7, 1.8.1 and 1.8.2.

- 2.2.1 How does VAFFC's expectation for future throughput volumes on the JFL compare to the volumes VAFFC shipped in 2018?

Response:

VAFFC expects that throughput volumes on the Jet Fuel Line in 2021 will be significantly lower than the volume VAFFC shipped in 2018, due to the ongoing impacts of the COVID-19 pandemic, which have resulted in a substantial decrease in air travel out of YVR, across Canada and around the world.

VAFFC does not have a JFL forecast beyond 2021 because the COVID-19 pandemic has created significant uncertainty about members' fuel requirements.

Please see also VAFFC's response to BCUC IR 1.2.2. 2.5.1 and PKMJF IRs 1.7, 1.8.1 and 1.8.2.

- 2.3 Please describe the process VAFFC envisions being in place that would allow its members to ship opportunistically on the JFL following completion of the VAFD project. In your response, please discuss how VAFFC members would nominate volumes and how VAFFC expects tolls would be calculated.

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Response:

VAFFC expects a standard nomination process consistent with current practices. Tolls would be on a per barrel basis and calculated as many if not most other liquid pipelines in Canada do for uncommitted shippers (PKMJF has considerable flexibility, and could, as most liquids pipeline operators in Canada do, establish committed and uncommitted classes of shipper).

VAFFC does not control the procurement or shipping decisions of its members. VAFFC expects that shipping decisions and nominations will occur as they do at present, but with far more opportunity to ship via pipeline rather than by truck.

VAFFC expects that, as in the past, tolls on the Jet Fuel Line could be set either by negotiation between the shippers and PKMJF, or by the Commission after an application by PKMJF.

Please see also VAFFC's response to BCUC IR 6.10.

- 2.4 Please explain how PKMJF would be compensated under the "opportunistic" shipping scenario.

Response:

Please see VAFFC's response to BCUC IR 2.3.

- 2.4.1 Does VAFFC believe operations of the JFL would remain economical under such a scenario? Please explain why or why not.

Response:

Yes. PKMJF would have to investigate, dialogue with, and understand its customer bases and propose tolls that are both attractive to customers and allow the JFL to remain economical. PKMJF is a sophisticated pipeline operator and the BCUC should expect PKMJF to take those core business steps (it has not).

To be clear, under the "opportunistic" shipping scenario PKMJF would be:

- shipping: (i) Parkland jet fuel production and (ii) jet fuel volumes currently delivered into the Lower Mainland from Alberta refineries via the Trans Mountain pipeline.
- trying to attract jet fuel volumes that: (i) are presently transported to YVR by truck (from Washington and Alberta); (ii) might be opportunistically barged to the JFL by VAFFC members or their third party fuel suppliers because of circumstances such as newly available tank capacity attached to the JFL, full tank capacity at the VAFD, or a transportation constraint (any of marine or rail or truck); or (iii) are sufficiently attractively priced as a commodity to overcome a higher transportation cost and result in an opportunistic purchase (i.e., discounted fuel from Parkland or the Trans

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Mountain line or the rail-connected Imperial Oil, Suncor, and Shell terminals).

For an established, partially depreciated pipeline with a long remaining life, connected from a refinery directly to a mature, enduring and in fact growing airport, the concept that a market competitive toll could not be developed is at best highly suspect.

- 2.5 Please describe any regulatory obligations governing PKMJF's activities as a common carrier that would necessitate continued operation of the JFL by PKMJF under the "opportunistic" shipping scenario described.

Response:

PKMJF would require leave of the BCUC to cease operations.²

If PKMJF made such an application after the VAFD had commenced operations then the BCUC would be required, at that time, to consider what the impact of stopping service would be on the BC public interest:

- The BCUC would notably have to consider whether the VAFD had fully displaced JFL shipments and truck deliveries – VAFFC does not believe that either is likely – and, if not, what effect closing a major supply channel for YVR would have on the airport's operation as one of the largest airports in Canada, and the larger BC economy. Ceasing operations could imply a return to significant truck traffic. Reducing tanker truck traffic is a goal of YVR and the JFL would provide redundancy and reliability of supply to YVR.
- The BCUC would also have to consider whether Parkland would be able to evacuate jet fuel from its site absent the JFL and, if not, whether full, standard refinery operations could continue. Parkland is the major but not exclusive source of motor fuel in the Lower Mainland.

- 2.5.1 In addition to any regulatory obligations, please discuss any economic rationale for PKMJF to continue operating the JFL under the "opportunistic" shipping scenario.

Response:

Please see VAFFC's response to BCUC 2.4.1. In addition to the favourable market position that will continue for PKMJF as an incumbent pipeline connecting a refinery and marine fuel terminal to an airport (albeit not quite as favourable as in the past), PKMJF would have an economic incentive to keep operating to defer the need to finance and expend abandonment costs. Payment of abandonment costs in the future rather than in the near-term has a clear economic deferral

² PKMJF acknowledges this at para. 47 of its Amended Application, Exhibit B-14, pdf p. 26: "KMJF recognizes that prior to discontinuing service and commencing abandonment of the Jet Fuel System, it will be required to apply to the BCUC to cease providing service and to the BC Oil and Gas Commission ("**BCOGC**") for leave to physically abandon the system".

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value. Plus, as the airport is a growing load, the opportunities for PKMJF cannot only be viewed as being represented by the situation in the first or second year of the VAFD – over the next 25 years there remains a clear market opportunity for PKMJF if the asset is properly managed.

On page C-11 of the InterGroup Report, VAFFC states:

VAFFC filed an application for an Environmental Assessment Certificate (EAC) with the BC Environmental Assessment Office (EAO) in February 2011 wherein it stated the need for the VAFD Project (Project) and expectations that PKMJF would abandon the JFL facilities soon after the Project became operational. The EAC was issued in 2013. Thus, it was clearly evident in 2009 and certainly by 2011 and 2013, at the latest, that VAFFC had made more than a tentative decision to proceed with the VAFD Project.

- 2.6 Please discuss whether VAFFC's 2011 application for an EAC for the VAFD project and/or the 2013 issuance of the EAC was publicly available information.

Response:

Yes, both VAFFC's 2011 application for an EAC for the VAFD Project and the 2013 issuance of the EAC were publicly available.

Further, as noted at paragraph 33 of VAFFC's evidence, VAFFC undertook extensive public consultations as part of the environmental assessment process, and launched a dedicated project website in February 2009:³

In January 2009, as toll negotiations with PKMJF were continuing, VAFFC submitted its Project Description ("PD") for the VAFD Project to the BC Environmental Assessment Office ("EAO"). The PD reflected VAFFC stakeholder consultation efforts since 2007, including the City of Richmond, the Vancouver Airport Authority, and the Greater Vancouver Regional District, among others. VAFFC launched its dedicated project website in February 2009. It continued and expanded upon these efforts over the following years, engaging in consultation with numerous individuals and organizations. By 2012, VAFFC had held seven public open houses in the City of Richmond, in addition to two open houses hosted by the BC EAO as part of the environmental review process.

- 2.6.1 Please explain why it is or is not reasonable to expect that PKMJF would have been aware of VAFFC's EAC application and/or the subsequent EAC issuance.

Response:

PKMJF was aware of VAFFC's EAC application and the subsequent EAC issuance.

³ Exhibit C2-36-2.

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As noted in VAFFC's response to BCUC IR 2.8, PKMJF and VAFFC have been in regular communication regarding the VAFD Project, from the early days of the planning for the VAFD Project to the present day. PKMJF has been aware of the progress of the VAFD Project from early on.

Representatives of VAFFC and its members made PKMJF representatives aware that VAFFC was proceeding with the VAFD project in early 2009 as part of discussions concerning post-2009 JFL tolls. VAFFC was concerned that PKMJF not oppose the EAC application for the VAFD.

PKMJF was also likely aware of the project from VAFFC's extensive public engagement and consultation efforts, including multiple open houses, newspaper advertising, and social media channels, and routine business interactions with VAFFC and its members. For example, in 2011 PKMJF requested and provided corrections to some of the information concerning the JFL presented in a VAFFC report on the EAO website.

It is reasonable to expect PKMJF, as a common carrier pipeline, to be aware of the development and progress of a competitor. Put differently, it would be a profoundly unreasonable business practice for PKMJF to remain unaware of the issuance of an EAC.

- 2.7 Please list any permits or approvals required for construction and operation of the VAFD project that were outstanding at the time the EAC was issued in 2013.

Response:

Please see VAFFC's response to PKMJF IR 2.1.6.

- 2.7.1 For each permit/approval identified please indicate (i) when VAFFC applied for the permit/approval, and (ii) when VAFFC received the permit/approval.

Response:

Please see VAFFC's response to PKMJF IR 2.1.6.

On page 9 VAFFC's Direct Evidence, VAFFC states:

In January 2009, as toll negotiations with PKMJF were continuing, VAFFC submitted its Project Description ("PD") for the VAFD Project to the BC Environmental Assessment Office ("EAO"). The PD reflected VAFFC stakeholder consultation efforts since 2007, including the City of Richmond, the Vancouver Airport Authority, and the Greater Vancouver Regional District, among others. VAFFC launched its dedicated project website in February 2009. It continued and expanded upon these efforts over the following years, engaging in consultation with numerous individuals and organizations. By 2012, VAFFC had held seven public open houses in the City of Richmond, in addition to two open houses hosted by the BC EAO as part of the environmental review process. [footnotes

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omitted]

- 2.8 Was PKMJF included in VAFFC's consultation process for the VAFD project? Please discuss.

Response:

PKMJF and VAFFC have been in regular communication regarding the VAFD Project, from the early days of the planning for the VAFD Project to the present day. Illustrative examples of such communications are provided below;

- a) See VAFFC's tracking table from 2012 outlining its consultation for the VAFD Project, available on the Environmental Assessment Office webpage for the VAFD Project.⁴ The tracking table indicates, at p. 14 (pdf p. 19), that "[d]uring the early planning for this project, the Proponent [VAFFC] consulted with TMJ [PKMJF] about options for the expansion of the existing pipeline [the Jet Fuel Line]", but that "TMJ expressed no interest in expansion and, in fact, advised VAFFC and the shippers that it was no longer interested in operating the aviation fuel pipeline". The tracking table further indicates that:

[...] In 2007, TMJ applied to the BC Utilities Commission to increase its rates. The application was unusual because TMJ was seeking to almost double its rates so it could recover its invested capital in the system and abandonment costs over a 5-year time frame, which it believed was the remaining economic life of its pipeline system. TMJ filed this application because it believed the VAFFC Fuel Delivery Project would be built within this time frame and it represented a superior project from several perspectives, including economics and access to fuel sources.

[Underlining added]

- b) VAFFC met with representatives of Kinder Morgan (then the parent company of PKMJF) in 2012 to discuss Kinder Morgan's concerns regarding the proposed VAFD Project and, in particular, the accuracy of certain aspects of the report prepared for VAFFC by Golder Associates and Ausenco-Sandwell in 2011.⁵

- 2.8.1 If yes, please describe the nature of the information VAFFC provided to PKMJF and the date(s) when this information was shared. Please provide copies of any relevant correspondence between VAFFC and PKMJF in your response.

Response:

Please see VAFFC's response to BCUC IR 2.8 for illustrative examples of the types of communications that have occurred between VAFFC and PKMJF (or its

⁴ Available here:

<https://projects.eao.gov.bc.ca/api/public/document/5887e31aad20ac134d91626f/download/Appendix%20%20-%20Working%20Group%20Tracking%20Table%20%28including%20First%20Nations%29.pdf>

⁵ Please see VAFFC's response to PKMJF IR 1.10 for further details on this report.

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parent companies) regarding the VAFD Project over the years.

It would be unduly onerous for VAFFC to compile routine correspondence between VAFFC and PKMJF regarding the VAFD Project, given that PKMJF was clearly aware of the environmental assessment process and associated publicly available documents on the EAO website throughout.

2.8.2 If not, why not?

Response:

Not applicable.

3.0

**Reference: THE JET FUEL SYSTEM
Exhibit C2-36-2, InterGroup Report, p. 8
Throughput Volumes – Use of 2018 Throughput Volumes**

On page 8 of the InterGroup Report VAFFC states that “For the purposes of setting tolls for the Test Years, the respective 2019, 2020 and 2021 Revenue Requirements should be divided by this 2018 Throughout Volume to derive tolls, which are then applied to the actual volumes shipped by the respective shippers.”

3.1 Please confirm, or otherwise explain, that “2018 Throughout Volume” refers to actual volumes shipped in 2018.

Response:

Confirmed. The intent is to have a measurable benchmark of reasonable throughput volumes that are not affected by the pandemic. The effects of the pandemic are the culmination of a risk that there is no reason for shippers to bear. The 2018 volumes also predate the test years, which are meant to have tariffs set prospectively. An alternative option would be to use a 3-year average (i.e., 2016-2018), but 2018 is as reasonable as any other measure – and, indeed, what PKMJF selected for its purposes.

3.2 Please explain why use of the 2018 throughput volume – rather than 2019 and/or 2020 actual throughput volumes – is reasonable and appropriate for setting tolls for the Test Years.

Response:

Please see VAFFC’s response to BCUC IR 3.1. To the extent possible, rates for a forward test year should be set using prospective data, with an eye to those variables on which the service provider, versus the customers, should bear risk of variance. In the case of regulated utilities, it is understood that customers often bear many of the risks (e.g., through deferral accounts), and as a result, updating for known actuals is a means to get more representative tariffs and minimize the balances in deferral accounts. Consider, for example, BC Hydro’s 2020-2021 Revenue Requirement Application in which an Evidentiary Update took into account test year loads for the months where actuals were available, and other variables such as trade income were updated pursuant

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to the Panel's decision. These items otherwise would have only served to build up excessive balances in deferral accounts, if not updated for actuals.

In the case of a common carrier, particularly one where there is no reason for the owner to have protection from variances in shipped volumes, updating for actuals only serves to transfer risk properly borne by the owner to the shippers, which is inappropriate. Please also see VAFFC's responses to BCUC IR 6.1, 6.2, and 6.9.

- 3.2.1 Please provide the effective toll for each of the Test Years based on: (i) the methodology proposed; (ii) 2019 actuals; and (iii) 2020 actuals (if available).

Response:

To ensure the most accurate information is available to the Commission, it is recommended that PKMJF perform these calculations. In the event a high-level overview will suffice, we note that the PKMJF nominations are approximately 20% of pre-pandemic levels, which would equate to approximately a factor of 5 in terms of unit tolls (i.e., at benchmark volume levels, the tolls would equate to those noted in the PKMJF filing, but at pandemic volumes they would be 5 times higher).

4.0

Reference: THE JET FUEL SYSTEM
Exhibit C2-36-2, VAFFC Direct Evidence, p. 5; VAFFC Fuel Delivery Project
Website – Project Overview
VAFD Project

On VAFFC's VAFD project website¹, VAFFC states that "Construction of the new system is currently underway. The system is currently scheduled to be fully operational by mid-2022."

On page 5 of VAFFC's Direct Evidence, VAFFC states that "VAFFC has continued to proceed with the construction of the VAFD pipeline throughout 2020. It now expects the project to be operational in 2023."

- 4.1 Please explain the discrepancy between the anticipated in-service dates reported on VAFFC's project website and in VAFFC's Direct Evidence.

Response:

The discrepancy is due to construction delays associated with COVID-19, as well as an expanded scope of work that was required at the marine terminal for the VAFD Project.

- 4.2 Please provide any project schedules or other documentation supporting VAFFC's anticipated in-service date for the VAFD project.

Response:

¹ <https://www.vancouverairportfuel.ca/projectOverview>.

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Please see VAFFC's response to PKMJF IR 2.1.5.

- 4.3 Please discuss the likelihood of the VAFD project being operational in advance of or later than 2023.

Response:

VAFFC has no reason to believe the schedule for the completion of the VAFD Project will change at this time.

- 4.4 Will VAFFC be a "common carrier" as defined in the *Utilities Commission Act* following completion of the VAFD project? Please explain why or why not.

Response:

No. VAFFC intends to operate the VAFD Project on a not-for-profit basis for the purpose of providing jet fuel transportation services to its members, and does not plan to seek to have the VAFD Project regulated by the BCUC as a common carrier.

Please see also VAFFC's response to PKMJF IRs 1.4 and 1.15.

B. COST OF SERVICE

5.0

**Reference: COST OF SERVICE
Exhibit B-11, BCUC IR 4.1; Exhibit C2-36-2, InterGroup Report, Appendix A, Section 5.0, p. A-32; Appendix C, Section 4.0, p. C-14; RH-2-2008 Reasons for Decision, LMCi Stream 3, Pipeline Abandonment – Financial Issues, Technical Conference, Revisions to Preliminary Base Case Assumptions, dated March 4, 2010, Section 2, p. 4
Annual Escalation Factor**

On page A-32 of the InterGroup Report, VAFFC states:

Reject Escalation: No escalator of any type should be used to calculate tolls in 2020 and 2021, as proposed by PKMJF. The proper approach would have been a fully tested revenue requirement for each test year, with supporting justification. However, at this late date, and with the limited information provided by PKMJF regarding 2020 and 2021, such a review is not possible. Instead, it should be recognized that only a portion of PKMJF's costs are affected by inflation, and others ought to be offset by appropriate productivity factors. Depreciation, for example, does not increase each year, and Rate Base would decline over time along with associated returns. For this reason, the only practical approach to balance some potentially increasing categories with others that decrease is to approve a flat revenue requirement, maintaining the same 2019 revenue requirement across 2020 and 2021.

In response to British Columbia Utility Commission (BCUC) Information Request (IR) 4.1,

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PKMJF states:

The 2.00% annual escalation factor is an estimate of overall cost increases. It is not intended to suggest that each individual revenue requirement component will increase precisely by 2.00% annually, but rather, that the total revenue requirement will increase by approximately 2.00% annually.

- 5.1 Please explain which cost categories should be subject to inflation. In your response, please provide the proposed inflation rate, the rationale and external source for the proposed inflation rate.

Response:

Broadly, the categories that may be subject to inflationary escalation are the operating costs (specifically Field Expenses, A&G Allocation, and potentially Integrity Costs if not already included in Field Expenses). For these categories, an inflationary rate equal to 1-2% is not unreasonable, as being within the range of the Bank of Canada's Consumer Price Index ("CPI") target and reasonably representative of CPI measured in recent years. However, the inflationary rate should be offset to some degree by an expectation of productivity gains by PKMJF, particularly given the change of ownership and synergies that would reasonably be expected.

Notwithstanding the above comments, the appropriate approach to setting tariffs for test years after the first is through proper budgets and justification of spending for all O&M, Integrity spending and A&G allocations in each test year.

- 5.2 Please discuss why an inflationary increase is not a reasonable approach when inflation is a general measure of the increase in the level of prices of goods and services, including replacement parts for the JFL, to which PKMJF is exposed.

Response:

An inflationary increase is not a reasonable approach when the base amount recovered is disputed and overstates the actual costs to operate the JFL.

Also, inflationary pressures are expected to be experienced on many items, but not all, and not all of the components of pipeline tolls. There is no inflationary increase in depreciation, for example, based on straight-line methods. There is also no inflationary increase appropriate for amortized costs (e.g., rate case), interest costs, and returns on equity – these items have costs in future years tied to the decreasing level of net unrecovered investment.

- 5.3 Please clarify the "productivity factors" that should offset an inflationary increase.

Response:

Productivity factors should be adopted to reflect continuous improvement and expectations that the pipeline operator will work to minimize costs imposed on customers over time. This is a normal part of rate setting where future years are being set based on an inflationary pressure (e.g., in a long-term PBR regime).

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In a letter dated March 4, 2010, the National Energy Board (NEB, now the Canadian Energy Regulator, CER) the NEB clarified specific items established RH-2-2008 Reasons for Decision with respect to the base case assumptions to facilitate the filing of preliminary estimates of future abandonment costs, including the application of inflation. The NEB stated:

In the Board's view, there may be a role for two types of inflation assumptions: an industry-specific inflation for cost escalation and a general economy-wide inflation. However, at this time, the same value can be used for each type of inflation.

The Board currently sees value in relying on the Bank of Canada's inflation target to establish the long-term inflation to be used in the Base Case. To the extent that the Bank of Canada inflation target continues to meet the Board's needs as an external benchmark, the Board will continue to give considerable weight to it in setting the inflation component of the Base Case. The Board will revise the inflation estimate when warranted, as discussed later in this report.

For the Base Case, the Board has determined that the current inflation target set by the Bank of Canada of two per cent per year for expected long-term, inflation is appropriate. The Board notes that actual inflation may fall below or rise above two per cent in the short-term, but would be expected to trend towards two per cent over the long-term.

- 5.4 Please comment on the reasonableness of applying the Bank of Canada inflation target to each of the components for PKMJF's revenue requirement (i.e., operating expenses, integrity costs, plant depreciation and amortization, rate base, etc.).

Response:

Please see VAFFC's responses to BCUC IR 5.1 and 5.2. Note that the issue is not the Bank of Canada benchmark, it is (1) PKMJF failing to produce proper test year forecasts (the above reference is for long-term inflation assumptions for costs forecast long into the future) and (2) the issue of applying inflation to items that do not increase over time, like depreciation on specific assets (straight-line) or return on rate base (declining).

The reference is also not in regard to rate setting for a test year, and items in revenue requirement, but instead to dealing with the measurement of future liabilities.

- 5.5 From VAFFC's perspective, please discuss whether an industry-specific inflation rate would be appropriate for PKMJF's revenue requirement. If so, please indicate: (i) the components of the revenue requirement an industry-specific rate should apply to; (ii) an applicable rate for each component; and (iii) the basis for VAFFC's proposed rate. If not, please explain why not.

Response:

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Please see VAFFC's responses to BCUC IRs 5.1, 5.2 and 5.4.

On page C-14 of the InterGroup Report, in reference to the economic life of the JFL it states, "[i]t is conceivable that Parkland and some other shippers (airline and non-airline) may use the JFL even if it had higher tolls."

- 5.6 Considering it is conceivable the JFL may continue operating for an indefinite period, and capital additions may occur, please explain why depreciation would "not increase each year" and rate base would "decline over time".

Response:

As the question suggests, absent capital additions, rate base declines over time as invested capital is recovered / the main asset is paid down (the very principle behind the accelerated depreciation PKMJF negotiated in 2009) and, under the straight-line basis PKMJF uses, depreciation expense remains constant for each individual asset until fully disposed of. Significant capital additions would be required to offset the flat depreciation expense / declining return on rate base trends described, which is unrealistic and, in any event, for the test years 2020 and 2021 should be able to be properly forecast and not assumed as part of a coarse inflationary concept.

- 5.7 In a scenario where the JFL continues operation for an indefinite period, please comment on whether there is a potential risk of intergenerational inequities by not accounting for inflation.

Response:

The premise of the question is incorrect. VAFFC/InterGroup do not propose to ignore inflation. They propose to rely on reasonable estimates of actual costs. There are no intergenerational inequities by setting each test year revenue requirement based on a properly prepared forecast of the costs and investments (e.g., capital spending, rate base) related to that period.

- 6.0 **Reference: COST OF SERVICE
Exhibit C2-36-2, Section III (a) (iii), p. 9; InterGroup Report, Section 3.0, p. 8;
Appendix B, Section 2.0, p. B-11, B-12; Application by Trans Mountain (Jet Fuel) Inc. for Approval of 2010 Tariff Filing and Toll Setting Agreement for the term 2010 - 2018, dated December 7, 2009 (2010 Tariff Filing), Section IV, p. 2; Order P-5-09;
Change in Risk Profile**

On pages B-11 and B-12 to the InterGroup Report, VAFFC states:

From 1998 to 2008 the Commission's decision with respect to the Jet Fuel pipeline set final tolls on a dollar per cubic metre basis. Starting in 2009 (retroactively) to 2018, the negotiated settlement applied a total revenue requirement, with tolls back calculated from actual load. This *fundamentally*

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changed the risk profile such that tollpayer charges no longer varied based on volume. Instead shippers paid a pre-calculated amount, consistent month over month, increasing on average 2.5% each year from 2010 – 2018. At the same time, the utility no longer bore any risk to revenues as a result of volume fluctuations.

6.1 Please elaborate on the toll methodology(ies) that was(were) applied to shippers from 1998 to 2008 and provide the formula(s) used to calculate the toll(s), as applicable.

6.1.1 For each methodology, please comment on the allocation of risks between the owner and shippers.

Response to BCUC IR 6.1 and 6.1.1:

As background, it appears that prior to 1993, the tolling mechanism was usually a unit value toll largely only reviewed on complaints-based system (e.g., P-2-88, P-2-89, P-3-90, P-5-90, P-7-90, P-3-91, P-6-91, P-3-92), eventually moving towards more active regulation including a Return on Equity trigger for overearning (e.g., see P-4-94). It appears tolls were set based on a forecast of throughput. Tolls for 1996 reference only forecast throughput values (P-1-96 and P-5-96).

By 1997, it appears the parties entered into a complicated and contentious period with many rate changes and regulatory interventions (P-1-97, P-2-97, P-5-97, P-7-97, P-8-97), which led to a new system being implemented for 1998.

Order P-3-98 implemented a negotiated framework for 1998-2002 which was consented to by shippers. It appears this approach led to volume risk being carried by shippers, at least in part, by way of deferral account adjustments. Toll adjustments over this period were agreed to by shippers in P-2-99, P-2-00, P-2-01, and P-1-02.

For 2003, interim tolls were in place for January per P-4-02 and (after a period of negotiation) finalized at the same level in P-1-04 and be continued into 2004 as interim. The 2004 tolls were later finalized at the same level (P-2-05), and carried forward as 2005 interim tolls (see P-1-06). The 2005 tolls were requested to be increased as part of finalization due to lower actual throughput, but this was rejected (P-1-06). The Commission specifically explained that the pipeline retained throughput risk, as part of IRs in this proceeding (Question 1.3, as described in P-1-06 Reasons for Decision).

For 2006 tolls, a negotiation occurred that received approval in P-2-06. The net result appears to be final 2006 tolls and collection of a shortfall related to 2005 and 2006, which may or may not reflect collection of the net financial impacts of a lower actual throughput.

Tolls for 2007 and 2008 were set prospectively based on a litigated proceeding (P-3-08).

In short, it appears volumetric risk resided primarily, if not entirely, with the owner

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for all periods prior to 1998, but volumetric risk between 1998-2002 resided with shippers pursuant to an agreement (where shippers presumably received offsetting consideration that merited them taking on this risk). From 2003 to 2005, the risk resided first and foremost with the owner (and the concept of risk residing with shippers was rejected by the BCUC for 2005) but a later negotiation process led to shippers potentially accepting volume risk retroactively for 2005 and 2006. The risk resided with the owner for 2007 and 2008. Since 2009, the risk has resided with shippers. In short, it appears shippers only carried this risk in 1998-2002, potentially 2005 and 2006, and 2009 to 2018, in each case pursuant to explicit agreement as part of a negotiation. It does not appear after-the-fact volume risk was foisted upon shippers through any regulatory process, without their explicit approval, at any time.

- 6.2 Please elaborate on how the risk profile changed for shippers commencing in 2009 as a result of the change in toll methodology.

Response:

The risk profile changed in that shippers bore the risks tied to volume from 2009-2018. If volumes declined on an actual basis, shippers made up the difference through a higher average effective unit charge for shipping.

- 6.3 Please clarify, from VAFFC's perspective, the risks PKMJF bore before and after the change in toll methodology.

Response:

Please see VAFFC's response to BCUC IR 6.2.

- 6.4 Please explain whether any concessions were made by PKMJF as a result of the change in toll methodology.

Response:

Please see VAFFC's response to BCUC IR 16.4.3. VAFFC and members have limited direct knowledge and only partial records from the negotiation period. There is no written agreement and some records may be subject to solicitor/client and/or settlement privilege. Airline shippers were motivated to avoid Kinder Morgan opposing the VAFD Project and had commercial motivations to agree to toll levels that exceeded the cost of service, i.e., exceeded those accepted in December of 2008.

Page 2 of Trans Mountain (Jet Fuel) Inc. (TJM) 2010 Tariff Filing states:

Throughout 2009, TMJ has been in discussions with a shipper to set fixed annual revenue amounts for use of the pipeline that span the tolling periods commencing 2009 through to the end of 2018. Such discussions have resulted in an agreement for the annual revenues to be shared monthly on a volumetric basis by all shippers.

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6.5 Please explain why VAFFC was satisfied with the modifications to the risk profile and assuming volume risk at the time of the 2009 discussions.

Response:

Please see VAFFC's response to BCUC IR 16.4.3, 16.5 and 16.6.

By Order P-5-09 the BCUC approved Trans Mountain (Jet Fuel) Inc. Turbine Fuel Tariff No. 39 which calculates the annual revenues and gather line fee using the same methodology proposed by PKMJF in its current application. Directives 2 and 3 of Order P-5-09 state:

2. The approved tolls are permanent and subject to review by the Commission in the event of a complaint by one or more Shippers on the pipeline within 60 days of this Order. If a complaint is received by the Commission after 60 days of this Order, any adjustments in tolls will be on a prospective basis.
3. TMJ is to provide all Shippers on the pipeline with a copy of this Order along with confirmation to the Commission.

[Emphasis added]

6.6 Please confirm that VAFFC received a copy of Order P-5-09.

Response:

Confirmed.

6.7 Please explain whether VAFFC registered any complaints with the BCUC with respect to the tolls approved by Order P-5-09.

Response:

To VAFFC's knowledge, no shipper made any such complaints.

6.7.1 If yes, please provide the date(s) and nature of the complaint(s), as well as the BCUC's response.

Response:

Not applicable – see VAFFC's response to BCUC IR 6.7.

6.7.2 If not, please explain why concerns with respect to the risk profile were not raised between 2009 and 2018 (the negotiated settlement period).

Response:

Please see VAFFC's response to BCUC IR 16.4.3.

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With respect to the tolls established for the 2009-2018 period, on page 9 of VAFFC's Direct Evidence, VAFFC indicates that, pursuant to a negotiated settlement, "...rates were guaranteed to generate certain annual revenues, rather than being specified in terms of dollars per unit shipped. This placed all the throughput forecasting risk on the shippers..."

- 6.8 Please explain why during the negotiated settlement period, VAFFC considered it to be acceptable for shippers to bear risks associated with throughput variance and why VAFFC does not consider such an arrangement to be appropriate for the test period.

Response:

Please see VAFFC's response to BCUC IR 6.1 and 16.4.3 and 16.5.

- 6.9 Please discuss why risks associated with throughput variance should be assumed by PKMJF.

Response:

As an entrepreneur who developed the pipeline on their own initiative, and as a common carrier who does not enjoy the protections appropriate for a regulated public utility, there is no reason to expect a service provider of any commercial service to secure a right to protection from volume risk unless they can so negotiate. At times, PKMJF has so negotiated, presumably by offering shippers other valuable offsetting concessions. However, PKMJF did not so negotiate for 2019-2021.

Just like any entrepreneurial business venture, PKMJF ought to be at risk of sales volume. This risk must reside somewhere, and there is simply no legislative, policy, regulatory or other legal or economic principle, guideline, or enactment that would presumptively force this risk on the airlines or other shippers. Public utilities have extensive duties owed to them because they are actively enticed to invest so as to take on aspects of the public interest – common carriers (particularly PKMJF) were not and are not intended to be so enticed.

- 6.10 Please discuss alternative toll methodologies VAFFC recommends, and the pros and cons of each alternative.

Response:

The evidence of InterGroup recommends that the Commission determine a reasonable revenue requirement for PKMJF for each test year, and then design a tariff for each year for both Gathering, and Shipment to YVR. This tariff should then be applied to the volumes each party actually ships (or shipped) to determine the amounts to be paid (with appropriate true-ups for periods where only interim tolls were in place).

- 6.11 Please separately explain how the entitlements and obligations for revenue requirements differ between a common carrier and a public utility.

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Response:

As discussed in InterGroup's evidence, Appendix A, sections 2.3 and 2.4, a public utility is entitled to the reasonable opportunity to earn a fair return on any investment (both annual revenue requirement and long-term recovery of rate base), within the standard of the prudent investment principle. This entitlement arises as a result of the special authority (e.g., exclusive franchise) it has been granted. The public utility is required to provide reliable service to all customers who request service, including expansions of its system as necessary and as ordered by policy makers. The concept of a right to the opportunity to earn a fair return means that any asset or investment added to rate base will almost assuredly have its full cost recovered from ratepayers. This is true even if the asset did not last as long as intended, or did not prove to be an enduring technology.

In contrast, a common carrier does not have the assurance of a fair return in the face of competition and, likewise, in such circumstances may set prices representative of reasonable market value, provided it does not discriminate in service availability or price as between customers. It operates under a more entrepreneurial concept of service.

As an illustrative example, start with the conceptual scenario where no infrastructure exists.

If there is a desired public utility due to a clear public interest such as bringing electricity to a region (whether initiated by the company or the government), a negotiation can occur for a franchise, which the government will grant despite this being a clear impediment to a future active vibrant competitive market. This franchise will include clear protections for the investor – such as arm's length regulation, an assured opportunity to earn a fair return (not a guaranteed return, but at least a fair opportunity), rights of appeal to higher courts, protections against expropriation, etc. Why would the government grant this bundle of exclusive rights? Because without the grant, the utility would not develop expensive infrastructure that cannot be relocated. This bundle of rights is very valuable to the public utility investor – indeed utilities go to great lengths to preserve, defend and expand their franchise rights and territory.

If there is no such overwhelming public interest, the government need not grant such favourable rights. As a result the common carrier will not possess the same degree of protections that exist for a public utility – but it offers the common carrier more entrepreneurial options.

As is the case with PKMJF, a common carrier can suffer from bad investments more than a public utility (including the possibility of not recovering its revenue requirement or investment), but can also negotiate more favourable tariffs than would be permitted for the public utility and have greater returns (as PKMJF did from 2009-2018 when it experienced extraordinary returns as a result of a negotiated settlement). The common carrier also has fewer obligations imposed on its business decisions – for example, PKMJF can elect to run its facility to obsolescence despite the capacity being undersized for the airport it serves, without regulator inquiry or intervention. Were PKMJF a public utility, it would not have this option – it would have been required to forecast and file service plans with the BCUC, leading the requisite expansion or twinning of its facilities many years ago to meet forecast customer demand. The option of installing a competing pipeline to YVR like the VAFD would not exist because any airport fuel supply franchise

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would likely prohibit competing supply.

Common carrier principles have been applied to airlines – but airlines cannot after-the-fact allocate the costs of unsold seats to the passengers who actually chose to fly. Taxis owe a common carrier duty to passengers, but do not charge more for months where less trips are taken, especially if this is only known after the fact. Sometimes air transport or ground vehicle services can negotiate “take or pay” contracts with customers that transfer the risks to the customer, but this right is not automatically granted to the operator – it is accepted on offer only in exchange for other characteristics that the counter party values. In this proceeding, where no negotiated settlement exists, the principle ought not to apply.

Regarding PKMJF’s current toll application, on page 8 of the InterGroup Report, VAFFC states that “...like basically any other purchased commodity or service, the entrepreneur who sells the service should be at risk for variances in the volumes consumed or demanded by the market”. VAFFC further states that “For the purposes of setting tolls for the Test Years, the respective 2019, 2020 and 2021 Revenue Requirements should be divided by this 2018 Throughout Volume to derive tolls, which are then applied to the actual volumes shipped by the respective shippers.”

- 6.12 Please discuss the pros and cons associated with relying on forecast throughput volumes for the purposes of establishing tolls in instances where actual throughput volumes are available.

Response:

Here InterGroup comments both generally on the pros and cons for common carriers, and on the specific circumstances of PKMJF.

First, this situation only arises where tariffs are set after-the-fact. This situation should be avoided to the extent possible. Please see VAFFC’s response to BCUC IR 3.2.

Second, the situation can only arise by the Commission unilaterally determining which party owns the risk of underutilization – the owner who possesses the facility, or the parties that actually used the facility. The BCUC cannot avoid foisting the risk upon one of the two – owners or shippers. If actual volumes are known, the temptation to consider this risk best residing with shippers may grow, even though the knowledge of actual loads makes the outcome no less ill-advised.

Third, adopting the principle that shippers bear this risk even though they did not explicitly negotiate or accept the risk gives rise to a major con – foisting the risk on the shippers means that the tariffs to be paid cannot be known until after the fact (for both the test years behind us – 2019 – as well as the years ahead – 2021). Cost certainty is a reasonable expectation of almost any service provided in the marketplace.

Fourth, if shippers bear the risk of under-usage, they bear it in relation to their actual usage. In short, if it is determined that the collective customers underused the system to their own detriment, it is the very parties who did not cause this situation (those who shipped relatively more) who will bear more of the cost for those who reduced their

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shipping. Indeed, it is as if a customer takes on an unknown and unknowable and potentially vast annual liability the minute they ship their first barrel in January, a concept that is antithetical to most rate design principles set out in the seminal Bonbright text which is well-known to the Commission²: it is not practical, understandable, feasible, free from controversy, stable, fairly apportioned to the broad group of customers who underpinned the investment, non-discriminatory, nor promoting of efficiency (including promoting all justified uses). It is just as much a fallacy to suggest that the party who reduces their usage at any given point in time is the “problem” as it is to suggest it is the party who retains the usage in the face of declining usage by others – both are incorrect and inappropriate judgment laden concepts in this situation.

Fifth, particularly in an entrepreneurial venture, the perpetual foisting of the risk for underusage on the shippers who do in fact ship product (and foisting none of the risk on the operator) removes incentive from the operator to grow loads, or preserve their duration. It also permits the potential for what might colloquially be known as a “death spiral”, with declining loads leading to higher prices and less usage, terminating in a collapse of the system.

The only “pro” to setting tolls based on known loads is to ensure protection for the facility owner for volumes, which stabilizes their income in the face of massive changes in the marketplace around them. This is a pro or privilege for the owner. It is not, however, a privilege that has been granted to the owner in this case.

7.0

**Reference: COST OF SERVICE
Exhibit B-25, VAFFC IR 22.1, pp. 2, 4, 6; Exhibit C2-36-2, InterGroup Report, Appendix B, Section 3.1.1, p. B-21; Section 3.1.2, pp. B-21, B-22, B-23, Table 8; Section 3.1.2, pp. B-24, B-29
Operating Costs – Direct Field Expenses**

Page B-21 of the InterGroup Report includes a breakdown of PKMJF’s direct field forecast expenditures compared to actuals.

Table 8: Direct Field Expenses (\$000s)³²

	2019 Forecast	2019 Actuals	Variance
Field Payroll	562	587	(25)
Field Non-Payroll			
Employee Expenses	93	180	(87)
Materials/Supplies/Parts/etc.	121	42	79
Outside Services	420	647	(227)
Vehicle Expenses	45	0	45
Rents	162	162	0
DOT Fees	7	8	(1)
Other	60	135	(75)
Field Major Maintenance	340	0	340
Tank Major Maintenance	15	0	15
Subtotal	1,263	1,174	89
Direct Field Expenses	1,825	1,761	64

² James C. Bonbright, Principles of Public Utility Rates, 1st ed. (New York: Columbia University Press, 1961)

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On page 2 of the further and better response to VAFFC IR 22.1, PKMJF states, “Regarding comparing year over year fluctuations in operating expenses, KMJF took into account that certain costs are often normalized over a longer period of time.”

- 7.1 Please discuss whether some of the variances between forecast and actual costs can be attributed to the fact that certain operating costs are normalized over a specific period of time (i.e., 3 years).

Response:

No. Table 8 lists PKMJF’s 2019 forecast Direct Field Expenses. InterGroup understands those expenses are **not** based on a normalization methodology and therefore the resulting variances would not be due to normalization. In contrast, the IR response quoted in this question’s preamble relates to Integrity Costs, which PKMJF separated **out** from Direct Field Expenses for its 2019 forecast and are not included in Table 8 above. PKMJF also applied a normalization methodology for Rate Case costs that are also not included in Table 8.

PKMJF provides more detail on its Direct Field Expenses forecast methods in Exhibit B-25 KMJF Supplemental Response to VAFFC IRs 22.1 and 23.1. PKMJF explains that its forecasts for many of the Direct Field Expense line items are based on annual and regularly occurring operating activities.

Further on page 2 of the further and better response to VAFFC IR 22.1, PKMJF states, “prior to September 2018, the previous operator of the Jet Fuel Line maintained accounting in a different manner than as is currently used by KMJF and as is reflected in the Application.”

- 7.2 Considering the difference in the manner in which the accounting was maintained by PKMJF’s predecessor, please discuss if a review of total direct field expenditures would be of greater value. If not, why not?

Response:

There were a number of difficulties in assessing PKMJF’s forecast and actual costs at a detailed level for reasonability. The 2018 accounting changes were part of this, reducing the transparency of year-over-year cost changes for Direct Field Expenses, but so was the JFL acquisition partway through 2019 (and in the middle of the IR phase), and the lack of history and past application forecasts because tolls were set based on a negotiated settlement for the past 10 years.

It is accepted that categorization can change within the Direct Field Expenses category. For this reason, InterGroup’s evidence also assesses the level of Direct Field Expense at the total level (Appendix B, Table 3, page B-14) and shows that the level of expense grew by 11.47%/year on average from 2008 to 2018, to \$1.454 million. PKMJF’s Application then bumps this up to \$1.825 million for 2019, a further growth of 25.5% in one year.

PKMJF has had ample opportunity within this proceeding to justify its 2019 Toll Application (including after the JFL acquisition, to refile any parts of the Application it saw fit) as this proceeding was based on standard regulatory process and has been

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expanded for better or more fulsome responses as well. There is also a good basis of actual costs which show substantially lower operating costs year-over-year than PKMJF has budgeted for in its 2019 Application. Based on these two factors, there is strong justification for the BCUC to make a determination to reduce Direct Field Expenses, and Revenue Requirement more broadly, based on the information on the record.

On pages B-22 and B-23 of the InterGroup Report, VAFFC states:

It is unclear why A&G Direct Staff costs significantly increased over the 10 year period 2009 – 2018. However, relative to prior year, 2018 A&G Direct Staff costs, the 2019 Field Payroll and Employee Expenses appear reasonable – as long as they are fully replacing A&G Direct Staff costs (i.e. resulting in direct cost efficiencies). While total A&G costs have been reduced for 2019 compared to past years, it is clear total A&G has not decreased by corresponding 2018 Direct Staff levels (approximately \$1 million).

Recommendation: For Field Payroll, actual expenditures of \$587,000 should be approved in the revenue requirement as long as the A&G cost allocations are reduced by the corresponding level of Direct staffing as a result. At present, it appears considerable overlap between these two cost components exists (as forecast A&G spending through shared allocations is increasing from previous year allocations). [*Emphasis retained*]

- 7.3 Considering the financial statements of PKMJF and its predecessor have been audited annually by an independent third party, and the revenue requirement for the test period is calculated based on prior year actuals, please provide the basis for asserting the existence of considerable overlap between field payroll and administrative and general costs. Please provide any evidence in support of VAFFC's position.

Response:

With respect, the premise of the question is incorrect. The revenue requirement for the test period is not calculated based on prior year actuals. Additionally, there has been a material reallocation of costs from A&G to Direct Field Expenses for the purposes of preparing the 2019 forecasts which is a different treatment than for past year actuals.

For the A&G forecast, full year 2019 costs were based on the first four-month actuals (unaudited) for 2019 multiplied by three (to represent twelve months). Those first four months of actual costs are weighted to JFL based on the Massachusetts Model, as described in Exhibit B-12 (PKMJF Response to Parkland IR 7.2):

The Mass Model allocates general and administrative expenses of the corporation to operating entities within the corporation. Costs incurred in departments that support the entire business operations such as Human Resources, IT, AP, Accounting, Scheduling, Procurement, Legal, Audit, Insurance, etc. are generally coded into an account on the parent company and allocated based on three factors: PP&E (plant in service), Revenue, and Direct Labour. Ratios are averaged and calculated as a percentage of the total for all operating entities and that average is used to allocate costs to the

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KMJF Jet Fuel Line each month.

There is no indication that this model was updated to reflect that the JFL was being directly allocated Field Payroll for the first time in 2019, even though it now has Direct Labour costs and therefore the allocations should change. There is also no suggestion that this model is in fact part of an annual audit by an independent third party or is properly assigning used and useful costs to JFL for recovery by ratepayers.

Further, the Mass Model cannot be tested for reasonability as it was not provided in support of PKMJF's Application. However, it is clear that the results are inconsistent with statements elsewhere.

These comparators make it clear that PKMJF is likely being overallocated A&G costs within the 2019 forecast (and potentially with the past few years of actuals) compared to what is used and useful for rate setting purposes.

In short, there is an issue of transparency with the 2019 A&G forecast costs that also impacts Direct Field Expense, Field Payroll specifically, given the transfer of costs for labour noted above for the purposes of rate setting.

The statement that there 'appears to be considerable overlap' was drawn from Table 10 of Appendix B of the InterGroup Report, on page B-22, reproduced below:

Table 9: Actual A&G Direct Staff Cost Comparison 2009 – 2018 with 2019 Forecast⁸

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019F
A&G											
A&G Direct Staff	333	352	397	489	632	688	595	676	647	1,044	-
Allocations	586	725	931	1,018	1,317	1,628	1,438	2,052	2,353	926	-
Total	920	1,077	1,328	1,507	1,949	2,316	2,033	2,727	3,000	1,970	1,358
Direct Field Expense - Direct Employee Expenditures											
Field Payroll											562
Employee Expense											93
Vehicle Expense											45
Total	-	-	-	-	-	-	-	-	-	-	700

PKMJF's actual A&G Direct Staff expenditures for 2018 were \$1.044 million. If this cost category was instead forecast for 2019 within Direct Field Expenditures, as PKMJF indicates, the 2019 A&G forecast should decrease by \$1.044 million, all else equal. As the difference between A&G from 2018 to 2019F is only -\$0.612 million (\$1.358 million less \$1.970 million). This decrease is, i) lower than the corresponding increase for Direct Field Expenses of \$0.700 million, and ii) does not offset the 2018 A&G Direct Staffing levels of \$1.044 million. These differentials, which in both cases result in higher 2019 forecast costs than if the cost transfer had been 1 for 1 from A&G to Direct Field

⁶ Exhibit B-41-1 CONFIDENTIAL Parkland (IR2)-PKMJF 3.2.1 and 3.2.2 Exhibit B-27-2, pdf pages 44-45 of 59

⁷ CONFIDENTIAL: PKMJF Supplemental Response to BCUC Order P-4-20, dated September 18, 2020, page 20

⁸ Exhibit B-25, KMJF further response to VAFFC IR 22.1.4, Appendix (Suppl.) VAFFC 22.1.4, pdf page 50 of 52.

For forecast 2019, as per Schedule 17 of Exhibit B-14, PKMJF does not categorize these costs in the same manner.

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Expenses, lead to the conclusion that there appears considerable overlap of staffing costs remaining in the A&G cost category.

This conclusion is further supported by the fact that there is a lack of transparency with A&G cost allocations which impact actuals and 2019 forecast, and information that is on the record contradicts the size of A&G allocations that PKMJF applies to the JFL.

On page B-24 of the InterGroup Report, VAFFC states:

For Field and Tank Major Maintenance costs, there is no supporting detail for these forecast costs despite the fact that there exists potential for considerable overlap with Integrity and even A&G Costs. Plus, there were no actual expenditures in this category for 2019. These costs (totalling \$355,000) should not be approved in revenue requirement, and instead removed as a subcomponent of Direct Field Expense (including forecast costs). These costs are provided for elsewhere. Further, unless PKMJF can provide detailed and specific known expenditures for 2020 or 2021 and can prove these costs are different than those included in Integrity costs, the BCUC should not include any costs in 2020 or 2021 either. [*Bold removed; underline added*]

- 7.4 Considering the financial statements of PKMJF and its predecessor have been audited annually by an independent third party, and the revenue requirement for the test period is calculated based on prior year actuals, please provide the basis for asserting Field and Tank Major Maintenance costs overlap with Integrity and/or administrative and general costs. Please provide any evidence in support of VAFFC's position.

Response:

Please see VAFFC's response to BCUC IR 7.3 and 7.5.

On page 6 of the further and better response to VAFFC IR 22.1, PKMJF states:

Schedule 16 of the Application, "Tank Major Maintenance" includes the following costs: (a) two to three annual tank inspections; and (b) API 653 inspections for each tank every 10 years. For 2019, KMJF anticipates inspecting Tanks A-3, A-4 and A-5. API 653 inspections, which are more extensive and expensive, occur at least once every 10 years per tank. Schedule 16 "Tank Major Maintenance" includes the estimated 2019 costs of inspecting 3 tanks but does not at this time include any amounts related to API 653 inspection costs. Prior to 2019, costs associated with this type of work were allocated in a different manner than in KMJF's current Application. Furthermore, KMJF submits that this type of work is a cost necessary for the operation of the Jet Fuel Line.

- 7.5 Please explain whether from VAFFC's perspective the above response from PKMJF provides clarity on the forecast tank major maintenance costs. If not, please explain why not.

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Response:

Similar to VAFFC's response to BCUC IR 7.3 above, PKMJF's 2019 forecast for the test period was not calculated based on prior year actuals. Further, as noted in the preamble above, PKMJF states that prior to 2019 these costs were allocated in a different manner.

The basis of InterGroup's statement that these costs are provided for elsewhere is based on the following:

- There are a number of forecast costs that have overlapping activity as the Tank Inspection costs based on the information provided by PKMJF, and the pre-ambled statement does not provide clarity to the following considerations:
 - PKMJF did not provide any evidence that these activities aren't being undertaken by its Direct Field employees [REDACTED], and if so this aspect of the cost would already be covered within Direct Field Labour.
 - If not undertaken by direct staff, are these activities undertaken by Outside Services (contracted), and if so, why are these costs not recorded through Outside Services in the Direct Field Expenses category or through Integrity Costs (which books its actual expenditures within the 'Outside Services' cost category)?
 - Last, these activities may be undertaken by A&G labour, which has a large forecast labour component.

The reason for questioning this in the first place, is when it came to 2019 actuals, there were no expenditures on Tank Maintenance even though PKMJF's forecast justification is that these costs occur annually. So either PKMJF's forecast justification that these are annual costs was wrong, or its forecast allocation was, and as stated in the original recommendation, these costs are already properly accounted for elsewhere within the revenue requirement.

If the BCUC determines that a separate allocation of costs for Tank Inspections is reasonable for tolls, the next question is whether \$355,000 is a reasonable amount to include. Tank inspections in prior years were recorded through Integrity Costs. As shown on Table 13 of Appendix B to InterGroup's Report, past years expenditures for Tank Inspections were miniscule, ranging from \$3,441 to \$11,385 and only occurred in about half the years between 2009 – 2018. Comparatively, PKMJF's 2019 Forecast (and based on its Application would apply with inflation for 2020 and 2021) has tank inspections combined at \$355,000.

Further, if these costs were still allocated through Integrity Costs, PKMJF would have normalized the annual expenditures over three years in its Application, from 2019 – 2021 instead of proposing for them to incur in each year at that amount plus inflation. While PKMJF states these are annual costs, but as noted before, this has not been backed up by 2019 and past year actuals.

⁹ Exhibit B-27, Appendix (Suppl.) VAFFC-KMJF 22.1.FTE (confid), page 1 & 2

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On page B-29 of the InterGroup Report, VAFFC states:

RECOMMENDATION: PKMJF claims “Outside Services” spending in Direct Field Expense (\$420k in 2019), that on its face appears to overlap with Direct Field Payroll and Integrity costs, exceeds previous years, and conflicts with a claimed 2021 retirement. Despite this context, PKMJF has not provided support for this level of spending in its forecast, although it was repeatedly asked.

Also, actual expenditures raise substantial questions related to the ability of PKMJF to control costs and prudently manage spending to that which is needed to safely operate the pipeline given the overlap with Integrity cost reporting and lack of supporting detail.

Unless PKMJF can provide evidence that these services are outside of the abilities of its Direct Field Payroll and can show a management plan for how Outside Service spending is minimized and any spending that has occurred is necessary and different in application than Integrity cost spending, these costs should be disallowed from revenue requirement within Direct Field Expense.
[*Bold removed*]

- 7.6 Considering the financial statements of PKMJF and its predecessor have been audited annually by an independent third party, and the revenue requirement for the test period is calculated based on prior year actuals, please provide the basis for asserting outside service costs overlap with direct field payroll and/or integrity costs. Please provide any evidence in support of VAFFC’s position.

Response:

Similar to VAFFC’s response to BCUC IR 7.3 – 7.5 above, PKMJF’s 2019 forecast for the test period was not calculated based on prior year actuals. With respect to forecast methodology, PKMJF states that for Outside Services:¹⁰

During the period of January 1, 2019 through April 30, 2019, KMJF only had one Outside Service expense that exceeded \$10,000 in Schedule 17 of the Application. This Outside Service was related to allocated legal fees paid to a third-party legal firm that assists KMJF’s parent company with its annual filings with the Securities and Exchange Commission (for a total of \$52,855 allocated to KMJF during January 1, 2019 through April 30, 2019).

None of the other Outside Services individually exceeded \$10,000. KMJF calculated the Outside Services in Schedule 17 of the Application based on actual allocated outside service expense for the period January 1, 2019 through April 30, 2019, which was then annualized (*i.e.*, multiplied by 3). Prior to 2019, as shown in Appendix (Suppl.) VAFFC-KMJF 22.1.4, “Outside Services” was not a category contained in A&G.

¹⁰ Exhibit B-25, PKMJF Supplemental Response to VAFFC IR 23.1(c), page 7

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The question in this proceeding is not whether actual costs pass an independent third-party audit as reasonable for accounting purposes, but whether the forecast costs for 2019 are reasonable and justified for inclusion in tolls. There are different standards for each type of assessment.

To this point, PKMJF has not provided sufficient justification for the level of forecast Outside Service costs it proposes to include in its revenue requirement (\$420,000 in 2019). When asked to support its forecast, PKMJF provided hundreds of pages of service contracts (most that were expired by the test period) that did not support forecast level expenditures. See pages B-23 to B-24 of Appendix B to the InterGroup Report that summarizes this.

The basis for asserting that Outside Services costs overlap with direct field payroll and/or integrity costs is that PKMJF's accounting practices for 2019 actuals reported outside services as one line item, with over [REDACTED] allocated in the year, [REDACTED].¹¹ This single line item is [REDACTED] than the \$420,000 forecast amount and the \$647,000 actual expenditure for Outside Services and must include Integrity Costs [REDACTED], see Table 11 of Appendix B to the InterGroup Report which reconciles this, page B-27). And while PKMJF states that these costs did not previously occur within A&G in the reference above, it is confusing that PKMJF is proposing the same methodology cost treatment as A&G costs.

Finally, even though PKMJF reports Direct Field Expense Outside Services and Integrity Costs in the same way for accounting purposes it is proposing different cost treatment for rate setting purposes – proposing to normalize Integrity Costs over three years, but charge the Direct Field Expenses allocation in each of the 2019 – 2021 years (with inflation).

- 7.7 Please elaborate on the basis for stating that “actual expenditures raise substantial questions related to the ability of PKMJF to control costs and prudently manage spending”. In the response please (i) address whether there may be a reasonable rationale for actual costs exceeding forecast, and if not why not; and (ii) provide supporting evidence for any costs that in VAFFC's opinion are not prudent.

Response:

First, PKMJF is the applicant and bears the onus of showing that costs are reasonable and prudent.

Second, InterGroup made the quoted statement because for 2019, PKMJF expended over [REDACTED] in actual Outside Services.¹² By comparison, this single line item within the Direct Field Expense cost category is [REDACTED] than any year prior for 2008 – 2018 for ALL actual Direct Field Expenses (including all Integrity Costs), not just compared to past year Outside Services.

¹¹ As per Exhibit B-41-1 Confidential Parkland (IR2)-PKMJF Appendices Income Statement and shown in Table 11 of Appendix B of the InterGroup Report, page B-27, line 15.

¹² As per Exhibit B-41-1 Confidential Parkland (IR2)-PKMJF Appendices Income Statement and shown in Table 11 of Appendix B of the InterGroup Report, page B-27, line 15.

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As no detail is provided outside of that single line item within PKMJF's income statements, it is not possible to determine what those costs included. However, it is fair to say that barring some sort of large issue (that would have likely been volunteered over the course of this review as justification for toll increases), the amount actually charged to Outside Services for 2019 raises concerns over cost control and prudently managed spending. A major concern also relates to periods where costs are avoided when tariffs are fixed (e.g., the years up to 2018) and then undertaken in anomalously large amounts once it is expected that tariffs will be re-set to include the amounts (e.g., 2019) – in other words, limited and disciplined spending in years when improved financial returns go to the shareholder, but lack of care and concern for cost control in years where they simply feed into higher tariffs. This is very worrisome.

On page 4 of the further and better response to VAFFC IR 22.1, PKMJF states:

Please see the attached Appendix (Suppl.) VAFFC-KMJF 22.1.5. The Appendix (Suppl.) VAFFC-KMJF 22.1.5 lists the outside services of KMJF related to the Jet Fuel Line. Some of the contracts are confidential. KMJF will further review which contracts require being provided subject to confidentiality terms.

- 7.8 Please explain whether the above referenced response, including the referenced appendix from PKMJF, provides clarity on the forecast outside services costs. If not, please explain why not.

Response:

It is understood this material was filed in Exhibit B-27-2 (Confidential). This Appendix included 1129 pages of various contracts with different outside contractors. This was reviewed in detail within Appendix B of InterGroup's Report, pages B-23 to B-24, with each block of contracts summarized to the extent possible. PKMJF also provided a two-page summary of the contracts in Exhibit B-25, pdf pages 51- 52. PKMJF's summary does not provide any cost detail or forecast assumptions, just names the type of service associated with each contract (for example [REDACTED]).

The above referenced Appendix does not provide any clarity on the forecast outside service costs for the following reasons:

- [REDACTED] and therefore do not support the forecast years in any way.
- Of all the contracts provided in Appendix (Suppl.) VAFFC-22.1.5, only one provided supporting cost detail [REDACTED]. Some others provide rate sheets although it is not clear how those rates correlate to the test year forecast.
- It is not clear that the contractors were retained solely for Outside Services and not for other cost areas such as Integrity Costs, A&G, or capital related or other cost components. For example, [REDACTED] and so it would not appear to relate to the item on which justification was requested. It is not understood how these differ.

- 
- There is no reconciliation between the contracts to forecasts costs to make it a useful appendix. In general, it is just an overwhelming amount of material without any practical use for this proceeding.

Last, PKMJF states elsewhere that its Outside Services forecast was calculated ‘based on actual allocated outside service expense for the period January 1, 2019 through April 30, 2019, which was then annualized (*i.e.*, multiplied by 3).’ It is not understood at a high level how individual contracts support this forecast methodology.

8.0

Reference: COST OF SERVICE
Exhibit C2-36-2, InterGroup Report, Appendix B, Section 3.1.3, pp. B-30, B-31, B-32
Operating Costs – Integrity Costs

On page B-30 of the InterGroup Report, VAFFC states:

PKMJF’s revenue requirement proposes to average Integrity Costs over three years 2019 – 2021 given the fluctuations of these types of expenses. PKMJF does not provide justification for why the three year time period was appropriate over another period of time.

On page B-32 of the InterGroup Report, VAFFC states:

PKMJF just spent similarly high levels in 2017 and it would appear that most if not all pipes have already been assessed within PKMJF’s standard five year timeframe. Averaging PKMJF’s forecast expenditures over five years instead of three would align with the user pay / cost causation principle, previously paced levels of spending and previously approved cost treatment. This results in normalized Integrity Costs of \$336,200 in revenue requirement. [*Bold removed*]

8.1 Please explain whether a five-year timeframe is standard industry practice for assessing the integrity of the pipeline assets. Include references as appropriate.

8.1.1 If a five-year timeframe is not standard practice, please explain how a five-year timeframe was established for PKMJF and whether, in VAFFC’s opinion, a five-year period is reasonable for the JFL.

Response to BCUC IR 8.1 and 8.1.1:

InterGroup is not in a position to offer an opinion on whether a five-year cycle is appropriate, or some other value. InterGroup’s evidence **accepts PKMJF’s position** that five years is the appropriate cycle based on compliance standard timing requirements.

It is a reasonably common practice to normalize inconsistent annual expenditures over the length of time that they provide benefit to set rates that

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minimizes volatility. The five-year timeframe as recommended in the above quoted text is based on PKMJF's disclosure that pipeline assessments occur in intervals of 5 years. If PKMJF only intended to operate the pipeline for 3 years (to the end of 2021) the prudent investment would be to not undertake assessment again in 2019 when it looks like these expenditures were last undertaken in 2017 (i.e., 2 years prior – as evidenced by the high levels of ILI and anomaly inspections/investigation taken at that time – see Table 13 of Appendix B to InterGroup's evidence) but to space out the activities for the full five years. Normalization of costs in this manner attempts to charge customers as if these costs were paced prudently and equally in each year.

However, it is not expected that the PKMJF pipeline will terminate service after 2021. The key consideration in InterGroup's recommendation for integrity cost treatment was to correct PKMJF's forecast to match the costs to the length of benefit. PKMJF's forecast was based on activities to meet planned and predictable compliance standards over "an interval of 5 years not to exceed 68 months", while "the vast majority of the forecast was set for the year 2019".¹³ In this manner, PKMJF appears to have included almost the full costs to meet a 5 year compliance standard into the 2019 forecast year.

- 8.2 Considering the test period spans three years, please elaborate on why VAFFC does not consider use of a three-year period for averaging integrity costs to be appropriate.

Response:

This is largely answered in VAFFC's response to BCUC 8.1 above, but the main reason is that PKMJF's forecast costs are set based on compliance standards that set inspection requirements for "an interval of 5 years not to exceed 68 months". As the costs being spent have a benefit for this length of time, charging for them in rates for three years would result in customers being overcharged, paying more in tolls than the cost of the service being provided to them.

- 8.3 Please explain why averaging PKMJF's forecast expenditures over three years is not consistent with the principle of cost causation principle.

Response:

The cost causation principle is generally understood to mean that customers that cause a cost to the system should be the ones to pay for it.

PKMJF's proposal to average these expenditures over three years was not based on cost causation but rather, due to its claim of pipeline abandonment at the end of this year, December 31, 2021.

If customers are truly only using the pipeline for three years, under cost causation they should not be charged for expenditures based on a five year compliance standard.

¹³ Exhibit B-11, PKMJF Response to BCUC IR2 4.6

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8.4 Please provide the supporting calculation for the normalized Integrity costs of \$336,200.

Response:

That calculation was based on a five year average of PKMJF's expenditures for Integrity costs, including 2019 actuals, 2020 forecast and 2021 forecast. From Exhibit B-39, Appendix Parkland (IR2)-PKMJF 7.1, page 3 of 4, Schedule 18:

$$(\$1,409,000 + \$222,000 + \$50,000) / 5 = \$336,200$$

The 2019 actual amounts were used in place of 2019 forecast simply because the amounts were more accurate. However, just as reasonably the BCUC could instead use PKMJF's forecast if it determines a five year average approach is reasonable. Per Exhibit B-14, Table 7 this would result in a normalized amount each year as follows:

$$\$1,622,000 / 5 = \$324,400$$

8.5 Please discuss how a five-year normalization period would be implemented in the context of the three-year test period.

Response:

A five year normalization period would provide \$336,200 to PKMJF in rates until such time as rates are revised. This is an appropriate normalized amount.

8.6 Please discuss the pros and cons of (i) a five-year average and (ii) a three-year average under a scenario where the JFL were to cease operation following completion of the VAFD project.

Response:

There is no reasonable prospect in PKMJF's application or the record supporting the termination of the JFL at year-end 2021. That is, the prospect of a 2021 final year was unreasonable on a forecast basis when PKMJF filed its application, and is unreasonable now based on the current record.

Based on PKMJF's cost justification, following the three year rate period 2019 – 2022, the pipelines have two years of remaining value, in that they have been fully inspected and maintained with integrity expenditures largely undertaken in 2019 (despite having just taken similar material expenditures in 2017). This is a benefit to PKMJF in future value of the pipeline. If PKMJF disposes of the pipeline this value can be assessed in any future acquisition.

Another benefit of the five year average approach is it properly allocates costs on a used and useful basis to toll payers for the annualized cost of service.

On page B-31 of the InterGroup Report, VAFFC states:

Given PKMJF's explanation for its forecast Integrity Costs above, that pipelines

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need to be assessed every five years, it follows that proper cost control and pacing would include assessment of 20% of pipelines each year, which would result in quite consistent costs year over year. At the very least, costs should be quite predictable within a five year period following planned inspections.

- 8.7 Please explain why VAFFC considers the integrity costs to be predictable given that necessary work to maintain the pipeline may only be known once the inspection work is completed?

Response:

Pipelines operators undertake routine inspection (such as every 5 years) to avoid major surprises and to undertake maintenance work and recommended repairs and upgrades in an orderly fashion. It should not be automatically assumed that significant unexpected expense will be discovered as part of setting prospective tolls.

Normalizing these costs over five years matches the overall expenditure with the useful benefit to ratepayers of these expenditures and reduces toll volatility.

- 8.8 Please discuss if the age of the pipeline in any way impacts integrity costs (e.g., it may cost more to maintain an older pipeline). If not, please explain why not.

Response:

InterGroup cannot provide an expert opinion in this area.

- 8.9 Please elaborate on why five years is an appropriate timeframe for reviewing integrity costs considering changes to codes, standards or regulations may warrant a more frequent review.

Response:

Please see VAFFC's response to BCUC IR 8.1.

- 8.10 Please discuss any potential consequences and risks associated with deferring integrity work.

Response:

InterGroup is not recommending deferring integrity work.

Rather, it is understood this work was already all undertaken in 2019. The InterGroup recommendation is solely related to setting tolls appropriate to the test period.

On page B-32 of the InterGroup Report, VAFFC states:

Even assuming that PKMJF's recent integrity spending has been appropriate from an engineering perspective, the BCUC should reject the level of Integrity

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Costs proposed by PKMJF for tolls. [*Bold removed*]...

The levels of spending and activity that PKMJF has undertaken in the past few years is not what would be expected from a utility preparing for pipeline abandonment.

- 8.11 Please elaborate on the basis for rejecting the proposed integrity costs and provide any evidence in support of VAFFC's position, including cites to any similar circumstances where the recovery of integrity costs have been denied by the BCUC.

Response:

Please see VAFFC's response to BCUC IR 8.10. VAFFC is not proposing that the BCUC should reject integrity costs. PKMJF's standard five-year average to recover those costs should be used because the JFL is expected to be in service for longer than the three years ending 2021. The unrecovered integrity costs can be recovered in the years following the test period, per PKMJF's past practice. Further, PKMJF's proposed need for accelerated depreciation is undermined by the level of activity and spending on integrity works.

- 8.12 Please clarify the level of pipeline integrity work, and the associated costs, VAFFC would expect for a pipeline that is planned to be abandoned in the near term.

Response:

It is expected that if a pipeline is going to be abandoned in the near-term only the minimum amount of integrity works to ensure safe and reliable operations until the terminal date would be undertaken, and evidence would be provided to support any and all activities undertaken with explanation to why they were required to be undertaken before retirement. Integrity work related to long-term asset health would be paused, for example.

Note that InterGroup's evidence has not analyzed whether the reported integrity spending was necessary, but instead focusses on with the period over which these costs are recovered. With its expertise in asset management, the BCUC may elect to be more skeptical about the integrity work and costs it allows into tolls.

- 8.13 In VAFFC's view, are PKMJF's proposed integrity costs reasonable given the age of the JFL? Please explain why or why not.

Response:

Please see VAFFC's response to BCUC IR 8.12.

InterGroup's evidence takes issue with the limited evidence that PKMJF put on the record to support the level of 2019 integrity costs as reasonable and required due to the age of the JFL, but is not able to provide an alternative value which the BCUC should find reasonable (except to the extent of normalizing the amounts over PKMJF's past 5-year practice).

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the BCUC as a reasonable basis for comparing the forecast costs in the Kinder Morgan Canada (Jet Fuel) Inc. – 2019 Tariff Filing Application (Application).

Response to BCUC IR 9.2 and 9.2.1:

Confirmed.

The evidence is referring to the review of operating costs for the purposes of setting tolls based on cost of service. It is reasonable to compare the 2019 forecast and overall growth with the last time tolls were set based on costs (2008) as one factor in assessing the overall reasonableness of PKMJF's revenue requirement.

It is commonly understood that PKMJF's service has not changed in the intervening years since the last toll-review by BCUC. There has been limited investment in any new assets. The overall function, design, construction standards and service expectations on PKMJF have not changed. For this reason, costs should be generally stable.

As a result, any marked change in operating cost growth that exceeds inflation merits careful attention. Further, as tolls were not set based on costs from 2009 – 2018 the BCUC should not automatically assume that the expenditures reported by PKMJF in these years were prudently incurred on behalf of ratepayers and justified for inclusion in tolls (particularly allocated costs as described in VAFFC's response to BCUC IR 9.1).

- 9.3 Please confirm, or otherwise explain, that as a public reporting entity PKMJF's parent company Pembina Pipeline Corporation, and its predecessors, are required to have its financial statements annually audited by a qualified, independent third party.

Response:

See VAFFC's response to BCUC 7.3.

Also note that the income statements provided on the record by PKMJF appear to be internally generated and there is no supporting auditor approval or sign offs specific for JFL in PKMJF's IR responses.

More generally, methodologies appropriate for accounting purposes are not always aligned with the most appropriate methodologies for rate setting and the objectives involved in auditing relative to rate-setting are different.

- 9.4 Please discuss why more recent actual costs are not a reasonable basis for comparing the forecast operating costs in the Application.

Response:

In the operation of the JFL, the supply of jet fuel to customers has not shown marked change in operations, capital requirements or customer demand over the long-term. This

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is a pipeline that has operated in much the same capacity for more than the last decade. As costs are available to review and benchmark over the long-term and there is no marked changes in operation or capital requirements that make these comparisons incompatible, it is very much appropriate to use long-term costs as a basis for comparing PKMJF's Application, not to mention the regulatory considerations that apply to the length of time since the last time costs were reviewed.

- 9.5 Does VAFFC consider an evaluation of the individual components of the proposed revenue requirement on a standalone basis to be sufficient? Please explain why or why not.

Response:

As this question is referencing the InterGroup Report, the response is provided by InterGroup, not VAFFC.

Both a bottom-up component level review of individual cost components and a top-down look at overall revenue requirement changes are important considerations for approving the final tolls. It is important to ensure that revenue requirement forecast methodology for each cost component is reasonable, accurate and likely, but also there are trends that emerge when looking at the overall revenue requirement request. In addition, the repeated classification changes and occasional material error correction instituted by PKMJF make line-by-line comparison alone a limiting approach.

For example, when comparing the overall proposed revenue requirement for 2019 to past years of actual revenue, its clear that PKMJF's Application is on par with previous year *revenue* (not including the abandonment surcharge) – the big change is what was a massive return on equity in past years is now reported as new cost levels to justify continuing the same level of tolls. When comparing individual cost components year-over-year, previous years costs were much lower than revenue, and now for 2019 have been inflated in almost all categories to meet the level of revenue that is being requested. Both pictures of the Application are important to consider.

- 9.6 Please discuss the value of incorporating a comparison to costs that were incurred over ten years ago.

Response:

Please see VAFFC's response to BCUC IR 9.2 and 9.4.

- 9.6.1 Please discuss the regulatory efficiencies of comparing to costs over ten years ago.

Response:

Comparing PKMJF's 2019 revenue requirement to costs over ten years ago provides regulatory efficiencies because tolls set in the intervening years from 2009 – 2018 were not approved based on cost of service. This is evident in the

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fact that tolls charged resulted in revenues much higher than costs in these years and provided [REDACTED] high returns to PKMJF. Using the 2008 year as a starting point for comparing cost growth provides an anchor to the last time tolls were set in this manner. This can then be a benchmark used to determine the appropriate cost growth year-over-year for setting the 2019 revenue requirement.

- 9.6.2 Please explain how inflation and other market adjustments would be addressed in comparing the forecast operating costs in the Application to costs from over 10 years ago.

Response:

Appendix B of the InterGroup Report takes this into account by comparing PKMJF's cost growth in the intervening period with overall Consumer Price Index (CPI) growth, a representation of inflation for BC over this period. For reference, CPI growth over the period 2008 – 2019 averaged 1.44% each year (see Appendix B, page B-3). However, the cost growth in PKMJF's reported costs (particularly to 2019) is many multiples higher than this level.

Another long-term market adjustment that is generally worth considering includes the changes in price for production fuel, however this cost component has not grown as materially in the intervening years as others.

On page 2 of the further and better response to VAFFC IR 22.1, PKMJF states:

KMJF has compared forecast 2019 operating expenses to levels incurred over the past five and three year periods and submits such a comparison is appropriate to determine the prudence of its applied for operating expenses, compared to operating expenses incurred over a historic period more than 5 years ago. ... demonstrates that KMJF's forecast 2019 operating expenses are 3.7% lower than the average level for the three-year period 2016-2018. Even looking back to the past five years, KMJF's forecast 2019 operating expenses are less than 5% greater than the average level for the five-year period 2016-2018. [*Emphasis added*]

- 9.7 Considering the financial statements of PKMJF and its predecessor have been audited annually by an independent third party, please elaborate on why VAFFC does not consider a comparison of forecast operating costs in the Application against actual costs incurred over the last three-year and five-year periods to be appropriate.

Response:

Please see the response to BCUC 9.3 and 9.6 above. PKMJF did not provide three years or five years of data to compare against forecast costs in the manner suggested by the question.

Further on page 2 of the further and better response to VAFFC IR 22.1, PKMJF states, "Regarding comparing year over year fluctuations in operating expenses, KMJF took into account that certain costs are often normalized over a longer period of time."

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- 9.8 Please discuss whether PKMJF's normalization of operating costs may impact the percentage increases being reported in VAFFC's evidence. If so, please quantify the impact.

Response:

PKMJF only normalizes forecast integrity costs and rate case costs in its 2019 Application. The forecast Direct Field Expenses and A&G costs are not normalized. Previous year actuals did not include rate case related costs and did not separate or normalize integrity costs out from Direct Field Expense for reporting expenses. In this manner, PKMJF's proposed normalization process does not impact year-over-year percentage increases.

For example, consider the statement made on pages B-9 & B-10 of Appendix B:

On a total expense basis (i.e. **not** including the proposed abandonment surcharge and return), PKMJF's 2019 forecast represents an increase in expenses of [REDACTED] from 2018 ([REDACTED] from operating cost increases alone). To be clear, the 2019 Application increases costs [REDACTED] from the last year of the negotiated settlement. Compared to 2008, forecast 2019 expenses have [REDACTED] or approximately [REDACTED] on average per year.

The above noted comparisons include the normalization of PKMJF's integrity costs and rate case costs for 2019 so does not impact the percentage increases being reported. As a result, any time a percentage increase is being reported based on PKMJF's forecast 2019 expenditures/revenue requirement, normalization is already factored in. Normalization may impact the comparison between a forecast increase and 2019 actual expenditures, but for this comparison, the conclusions being drawn were based on overall spending levels and not specifically the resulting tolls.

- 9.9 Considering certain costs are normalized, please comment on the appropriateness and relevance of comparing total operating costs from one specific year to another.

Response:

The premise of the question is not correct. PKMJF only normalizes forecast integrity costs and rate case costs in its 2019 Application.

It is appropriate to compare total operating costs from past years to PKMJF's 2019 Application. In the years 2008 – 2018, PKMJF did not normalize its integrity cost expenditures, so the entirety of this spending along with all other Direct Field Expenses are included in each year. A&G expenditures, Property Tax and Fuel & Power (the other operating expenses) are not normalized in any past years.

The substantial cost increase proposed for 2019 is relevant for assessing the appropriate level of tolls. More specifically, normalization does not explain the increase in total operating costs for 2019 compared to other years because this treatment in effect lowers 2019 forecast expenditures, yet even this lowered amount is much higher than past years.

- 10.0 Reference: COST OF SERVICE
Exhibit B-12, Parkland Refining (B.C.) Ltd. (Parkland) IR 7.2; Exhibit C2-36-2, InterGroup Report, Appendix B, pp. B-35, B-36, B-38
Operating Costs – Administrative & General Allocation**

On page B-35 of the InterGroup Report, VAFFC states:

The “Mass Model”, has not been approved by the BCUC or other regulator for use in rate setting. As well, PKMJF’s explanation above could not be verified from the supporting information provided. Nevertheless the apparent model outcome results in ... of all general and administrative overhead costs accrued from the period January – April 2019 allocated to the jet fuel pipeline, regardless of whether operation of the jet fuel pipeline requires such activity or if the allocation weightings used are appropriate cost driver weightings. [redacted text omitted]

In response to Parkland IR 7.2, PKMJF states:

With respect to general and administrative (“A&G”) costs from September 1, 2018 onwards, there are no administrative staff directly employed by KMJF. A&G costs are allocated by Kinder Morgan and KMC Services to KMJF using the Massachusetts Model (“Mass Model”), which is similar to the NEB [National Energy Board, now the Canada Energy Regulator] allocation model used by Canadian entities to allocate general and administrative type costs.

- 10.1 Please explain whether VAFFC considers the Massachusetts Model used by PKMJF to be a reasonable method for allocating administrative and general costs.

Response:

InterGroup cannot determine if the Massachusetts Model is a reasonable method for allocating A&G costs and confirming the costs as appropriate for setting tolls as it has not been provided or tested within this proceeding. The last tested model was the 2002 NEB Allocation model, and PKMJF’s assurance that the Mass Model is “similar”¹⁴ does not provide enough justification, especially given how much of PKMJF’s overall revenue requirement is made up of A&G costs and the extreme degree of escalation in these costs since the last BCUC review.

PKMJF’s interests in allocating A&G costs to the JFL are not necessarily aligned with ensuring cost causation and ‘used and useful’ expenditures being allocated in tolls. This especially holds true if parts of the parent company are unregulated. As a result, it should be a requirement that the underlying methodology be reviewed and approved as fair before approving the resulting cost allocation in tolls. As PKMJF did not file that information on the record, that step cannot be taken, and so Appendix B of InterGroup’s evidence provided supported recommendations that would bring A&G costs to a reasonable level based on the information available.

¹⁴ Exhibit B-12 Parkland IR 7.2

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- 10.2 Please discuss the pros and cons of the NEB allocation model used by Canadian entities to allocate general and administrative costs, and whether VAFFC considers this a reasonable methodology.
- 10.2.1 In VAFFC's view, is the NEB allocation model preferred over the Massachusetts model for allocating general and administrative costs? If yes, please explain why and specify the preferred characteristics of the NEB allocation model.
- 10.3 Please discuss if the Massachusetts Model is a reasonable proxy for the allocation of general and administrative costs.
- 10.4 Please comment on the differences between the Massachusetts Model used by PKMJF for the allocation of administrative and general costs in the proposed revenue requirement and the NEB allocation model.

Response to BCUC IR 10.2 to 10.4:

There was not a general "NEB allocation model used by Canadian entities" to review. In 2002 PKMJF filed an Allocation Study specific to its own circumstances for BCUC review and approval (Exhibit B-25, Appendix (Suppl.) VAFFC-KMJF 22.1.3). The study dealt with the allocation of costs between BCUC-regulated and NEB-regulated affiliates that shared services between assets.

Ms. Davies did not specifically review the 2002 Allocation Study in the course of preparing Appendix B and so cannot comment on that comparison.

In Ms. Davies' view the allocation study has broadly reasonable objectives and methods for cost allocation purposes. However, this study only provides examples and illustrations and does not actually give any underlying detail to the actual costs, drivers and methods used at that time, or that would be useful now.

The only appropriate conclusion that can be drawn is that there is not enough information provided on the record to support PKMJF's A&G cost allocation, despite multiple requests in information requests for this information to be provided.

It is common regulatory procedure to test:

- i) the overall level of spending in costs being allocated (as costs should be directly assigned as much as is possible before allocated from the general pool),
- ii) that all line items that are allocated to the jet fuel pipeline are being used specifically by the jet fuel pipeline, and finally that
- iii) the cost drivers used as the basis to allocate costs between assets are appropriate and reflect cost causation principles.

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None of these areas have been addressed in this proceeding.

On page B-36 of the InterGroup Report, VAFFC states:

Specifically, for the detailed A&G activities that the jet fuel pipeline is allocated costs for, there are many activities where it is not straightforward how these types of activities are used by the jet fuel pipeline. On its face there seems to be double counting between A&G allocated costs and directly assigned costs to the jet fuel pipeline in revenue requirement. Especially as revenue requirement for the pipeline includes salaries for five full-time employees, costs should not be allocated unless it is demonstrated that there is no overlap.

- 10.5 Considering the financial statements of PKMJF and its predecessor have been audited annually by an independent third party, and the revenue requirement for the test period is calculated based on prior years' actuals, please provide the basis for VAFFC's assertion that there is double counting or overlap in the proposed revenue requirement.

Response:

To clarify, the above referenced statement was specific to PKMJF's 2019 test year forecast costs, which has not been audited or approved by an independent third party, as auditors approve actual expenditures for financial reporting purposes.

Please see VAFFC's response to BCUC IRs 7.3 and 9.3.

On page B-38 of the InterGroup Report, VAFFC states:

While it is hard to estimate the exact extent to which of the A&G allocations should be included in revenue requirement, it is clear that PKMJF's proposed A&G allocation is overstated. Further, the BCUC cannot include some or all of these costs without detailed and supported cost drivers given the overlap of some cost categories with Direct Field Expenses cost components and time that has elapsed since the last thorough review. Based on the list provided above, it is reasonable to exclude the costs that do not appear to apply to the jet fuel pipeline and/or may be double counted through direct cost assignments, reducing the A&G allocation by \$250,255 for 2019.

- 10.6 Please provide the basis for reducing administrative and general allocations by \$250,255. In your response, please include any relevant evidence and calculations to support the proposed reduction.

Response:

The supporting basis for this is provided on pages B-36 and B-37 of Appendix B to the InterGroup report. Given PKMJF did not provide supporting detail to a level required to justify its A&G forecast, Ms. Davies attempted to review the high level job descriptions, noting where it is relatively clear that these costs are not being incurred specifically to support the Jet Fuel Line and/or are already provided for elsewhere.

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The \$250,255 is a sum of the costs from these line items as provided by PKMJF in Exhibit B-27-2, Confidential Appendix (Suppl.) VAFFC-KMFJ 23.1.2 (confid), pdf pages 1113 – 1129. The table below reproduces the Evidence from page B-36 to illustrate how that sum was calculated:

Table 1: CONFIDENTIAL –

11.0

**Reference: COST OF SERVICE
Exhibit C2-36-2, InterGroup Report, p. 13; Appendix C, pp. C-2, C-11, C-12,
C-14; Financial Accounting Standards Board, Accounting Standards
Codification, Master Glossary, ASC 360-10-35-4
Depreciation – Remaining Life of the Jet Fuel Line**

On page C-2 of the InterGroup Report, VAFFC states, "...PKMJF's now assumed final retirement date January 1, 2022 is contradicted by... the 25-year life expectancy used in the calculation of the Asset Retirement Obligation [ARO] reported in the PKMJF 2019 financial reports." [footnotes omitted]

On pages C-11 and C-12 of the InterGroup Report, VAFFC states:

¹⁵ As detailed in Appendix B to the InterGroup Report, page B-36. From Exhibit B-27-2, Confidential Appendix (Suppl.) VAFFC-KMFJ 23.1.2 (confid), pdf pages 1113 – 1129

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Even though 2010-2018 was a negotiated toll settlement period, there was sufficient evidence by 2009, 2011, and incontestably by 2013 that the VAFD project was proceeding. It was PKMJF's responsibility to either apply its practice of recalculating depreciation rates in response to a fixed date, or otherwise seek additional depreciation recovery. By not booking the appropriate depreciation expense needed to achieve full recovery by 2022 as designed, PKMJF received increased earnings and only now requests increased depreciation rates to make up for the shortfall. *[footnotes omitted]*

On page 13 of VAFFC's Direct Evidence, VAFFC states:

...PKMJF has misconstrued the effect of the depreciation rates established by PKMJF's 2010 depreciation study. The 2010 depreciation study established rates that should have allowed PKMJF to recover its net investment in the Jet Fuel Line (including any capital additions during the 2009-2018 negotiated settlement period) by the end of 2022. *[footnotes omitted]*

- 11.1 Please reconcile VAFFC's reference to the 25-year life expectancy of the JFL to VAFFC's assertion that by 2013 PKMJF should have known about the VAFD project and re-calculated depreciation rates to reflect a 2022 end-of-life.

Response:

The two references illustrate the range of lives put forth by PKMJF in the current proceeding.

The 25 year life is an estimate of the physical capability of the majority of the existing assets. As reviewed in the InterGroup evidence, as well as in the evidence of MNP commissioned by Parkland, [REDACTED]. It is also consistent with the depreciation rates in place prior to the adoption of accelerated depreciation. For additional information, see the InterGroup evidence at page A-26. The table provided there indicates that for the main asset class (Line Pipe), as of 2008, the remaining life was 36.9 years – approximately the same retirement date as arises for a 25 year life today (i.e., 2045).

Notwithstanding this reasonable expectation of a physical life to 2045, in 2009, PKMJF secured an agreement from the shippers to depreciate the assets in full by 2022. While this approach should have been deemed inconsistent with a common carrier framework, customers agreed to the principle and tolls were set to provide PKMJF with sufficient revenue to implement this approach. However, PKMJF did not implement the approach – they implemented an approach that depreciated all assets (whether existing at the time, or installed much later) over 13 years. PKMJF's actual approach makes no reasonable sense – if the assets are to be retired in 2022, why would an asset installed in 2016, for example, be depreciated over 13 years? Whether intentional or simply as a result of a failure to understand basic deprecation principles, the effect of PKMJF's approach is to under-record the depreciation that should have been recorded and over-record the profit that the company reported. This issue requires adjustment.

On page C-14 of the InterGroup Report, VAFFC states:

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...there is no clear retirement date of the JFL other than PKMJF's estimate of the VAFD Project in service date. **No prospect of continuing JFL operation has even been considered by PKMJF.** It is conceivable that Parkland and some other shippers (airline and non-airline) may use the JFL even if it had higher tolls. The JFL has a physical 25-year remaining life and PKMJF acknowledges that it connects to a myriad of supply sources: marine delivery options, the Parkland refinery, and the Trans Mountain pipeline. None of these factors have been fully considered to date. Regardless of which *longer* depreciation period might be best applied, the existing depreciation rates would provide full recovery of the remaining service value of the JFL assets by 2022, which is too short. Therefore, PKMJF's proposal for the depreciation rates in the current application is not supported and should be rejected. [*Emphasis retained*]

- 11.2 Please discuss from VAFFC's perspective the differences, if any, between an asset's physical life, useful life, remaining life, service life, and economic life.

Response:

Useful Life - the estimated time the asset or group of assets are expected to provide service.

Remaining Life – the remaining period of service which can be expected, on the average, from the equipment type under study. This period is measured from the time of implementation of the depreciation rates being designed to the expected ultimate retirement of the embedded investment in the equipment type under discussion. The remaining life of a group of property may be determined either through direct planning for simultaneous retirement of all assets within this group, or derived as a function of the age of the equipment type under discussion, its expected average service life, and the expected future retirement pattern (mortality curve shape). . The remaining life is an estimate, based on statistics, industry averages (which may be modified to take into account any known differences in operating conditions or nature of the equipment in the specific utility under study), planning, accounting changes or other foreseen life-affecting factors.

Service Life – the expected life of all assets in a group when new, based on experience (statistics) or estimates. The period of time from installation unit retirement from service. When dealing with a group of property containing many units, there is an expected wide dispersion of life, with some retiring soon after their installation and others providing many years of service. An average life for all assets within the group or account is calculated by determining the age at retirement for every asset in the account and plotting it as a percentage of the units surviving at each age interval (the graphical representation is called a survivor curve).

Economic Life – the total revenue producing life of an asset or group of assets.

For the purposes of accounting, and reporting profits and losses, it is important for a company to recognize the useful life and depreciate assets over this period because the consumption of the remaining value of the assets has been accelerated. For the normal regulated public utility, such accounting depreciation is also typically advised for rate-setting. For a review of the principles applicable to setting tolls for a common carrier, see VAFFC's response to BCUC IR 18.6.

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- 11.3 Given VAFFC asserts PKMJF's proposed depreciation rates are not supported and should be rejected, please comment on the depreciation rates VAFFC considers reasonable for the test period.

Response:

For the purposes of setting tolls, depreciation of the remaining investment should be spread over the full economic life that a reasonable and competent operator could secure from the assets, including by applying proper maintenance and protecting market share. As discussed in Appendix A (Intergroup evidence, page A-32), PKMJF's Application omits assessing means to continue to ship jet fuel from the Parkland refinery to YVR (plus some other volumes), and depreciation rates should accordingly be based on the outstanding net book value of assets (reduced by \$0.529 million to reflect the proper application of life span depreciation over the negotiated settlement period) over a life consistent with the true remaining capabilities of the assets, i.e., its physical life of 25 years.

For PKMJF's own accounting, as discussed in Ms. Lee's evidence, the appropriate economic life must be determined *first*, before the depreciation rates are calculated. On this point, the InterGroup evidence discusses the internal inconsistencies from PKMJF on the JFL's economic life.

The Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Master Glossary defines Useful Life as "The period over which an asset is expected to contribute directly or indirectly to future cash flows."

Further, ASC 360-10-35-4 states:

The cost of a productive facility is one of the costs of the services it renders during its useful economic life. Generally accepted accounting principles (GAAP) required that this cost be spread over the expected useful life of the facility in such a way as to allocate it as equitably as possible to the periods during which services are obtained from the use of the facility. This procedure is known as depreciation accounting, a system of accounting which aims to distribute the cost or other basic value of tangible capital assets, less salvage (if any), over the estimated useful life of the unit (which may be a group of assets) in a systematic and rational manner. It is a process of allocation, not of valuation.

Having said this, it is not imperative that the BCUC make a determination of the useful life of the JFL. The only determination required from the BCUC is with respect to toll-setting, which, as noted above, can and should be set based on the inherent potential embedded in the investment, which is 25 years.

- 11.4 Please identify the relevant factors from VAFFC's perspective that should be considered in determining the useful life of an asset for the purpose of setting depreciation rates in accordance with US GAAP.

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Response:

Please see VAFFC's response to IR 11.3 above regarding the use of a 25 year physical remaining life for setting tolls in this case, which is tantamount to the JFL's useful life.

Factors that should be considered in determining the useful life of an asset include an analysis of historical plant retirement data through the study date as well as the future retirement. Factors causing property to be retired include but are not limited to the following from Engineering Valuation and Depreciation (Marston, Winfrey, and Hempstad, 1953), Depreciation Systems (Wolf and Fitch, 1994), and the National Association of Regulatory Utility Commissioners (NARUC), Public Utility Depreciation Practices:

1. Physical Factors
 - a. Wear and tear
 - b. Decay or deterioration
 - c. Action of the elements and accidents
2. Functional Factors
 - a. Inadequacy or lack of capacity to supply what is required or demanded
 - b. Obsolescence
 - c. Changes in technology
 - d. Changes in demand
 - e. Requirements of public authorities
 - f. Management discretion
3. Contingent Factors
 - a. Casualties or disasters
 - b. Extraordinary obsolescence

Competition may influence some of all the functional factors. It can provide incentives to look for new technologies and can also affect the demand for services. It is important for the company requesting revised depreciation rates to address competitive pressures it faces and how the company is reacting or plans to react to those pressures. PKMJF has not done so.

In the case of groups of property that are expected to be retired at a single time, the major issue is estimating the date of final retirement. The forecast of that date must be based on evidence such as an operating license termination, availability of supply, or projected long term use.

- 11.5 Would VAFFC agree that depreciation is intended to allocate an asset's cost as equitably as possible to the periods during which the reporting entity benefits from the use of the asset? If not, please explain why not.

Response:

Depreciation is intended to allocate an asset's cost as evenly as possible over the period of its anticipated use. From an accounting perspective, depreciation seeks to ensure that the profits and losses from the entity are properly reported. In this sense, the term depreciation means the loss in service value not restored by current maintenance,

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It may also be particularly relevant to the Commission, in light of the InterGroup recommendations, to understand PKMJF's financial results as reported over the last 10 years. InterGroup has recommended that tolls be set on the basis that PKMJF's assets ought to have \$0.529 million more depreciation recorded against them than was reported, and the provision for removal should be assumed equal to \$3.671 million over this same period. The BCUC make want to consider whether it is reasonable to adjust depreciation up, and abandonment cost funding up, and correspondingly retained earnings down (at least for the purposes of setting tolls) given the context of low/missing balances due to significant earning. Such a determination could be supported in part by the evidence on the record that by failing to properly record these provisions, PKMJF secured an average of [REDACTED] in average returns over 10 years [REDACTED] in total), when the investment in rate base only justified \$0.7 million/year in the years preceding the settlement period. In short, PKMJF made [REDACTED] more over 10 years than would have been normally considered fair based on strict regulatory review.

12.2 In VAFFC's view, is PKMJF entitled to a certain rate of return on rate base? Please explain why or why not.

12.2.1 If yes, please specify what VAFFC considers to be an acceptable rate of return for PKMJF and provide reasoning.

12.2.2 Would the rate of return proposed by VAFFC provide PKMJF's investors with confidence in the company's financial integrity and allow PKMJF to maintain its credit worthiness and attract capital? Please discuss why or why not.

12.2.2.1 If not, what rate of return does VAFFC consider necessary to achieve such an outcome?

Response to BCUC IR 12.2 to 12.2.2.1:

InterGroup takes no issue with PKMJF's proposals for the calculation and level of return on a prospective basis for the purposes of setting tolls in 2019-2021. No adjustment has been proposed to the return on rate base, except as necessary to reflect changes in the value of rate base associated with the other InterGroup recommendations.

On page B-13 of the InterGroup Report, VAFFC states:

...from the 10-year period 2009 – 2018, which represents the negotiated settlement period, the cumulative net return (or overall return overall capital) was ..., averaging ... per year or approximately ... of total revenue. This level of return is excessive relative to any awarded in a cost of service based toll, in Canada or elsewhere. [redacted text omitted]

12.3 Please provide evidence to support VAFFC's submission that "This level of return is excessive relative to any awarded in a cost of service based toll, in Canada or elsewhere".

Response:

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There is no definitive source for the level of returns awarded by equivalent regulators in every situation, but through decades of experience with the setting of revenue requirements, InterGroup has never seen an award of Returns on Equity exceeding [REDACTED].

PKMJF's rate base for 2009 was determined to be \$9.775 million and the total return on rate base was \$0.753 million per year. This represented an average cost rate for capital of 7.71% (see InterGroup evidence Annex A Schedule 15). For 2019, PKMJF's rate base is proposed at \$4.757 million and a return on rate base of \$0.320 million representing a cost rate of 6.73% (Schedule 8 of Exhibit B-14). For simplicity, consider the average rate base over the negotiated settlement period then is approximately [REDACTED]. The evidence is that PKMJF earned an average net income of [REDACTED] per year over these 10 years (not counting the cost of debt) - even assuming there was no debt in the capital structure, this would be an average return on equity exceeding [REDACTED] on a sustained basis.

13.0

**Reference: COST OF SERVICE
Exhibit A2-1, p. 2; Exhibit B-13, VAFFC IR 12.1, 12.12; Exhibit C2-36-2,
VAFFC Direct Evidence, Section III(b)(i), p. 9; InterGroup Report, Appendix
C, Section 1.0, p. C-2; Section 2.2, pp. C-5, C-6; Section 3.3, pp. C-10, C-11;
Trans Mountain (Jet Fuel) Inc. 2007 Application for Approval of Tolls and
Accelerated Depreciation (2007 Application), Exhibit B-5, BCUC IR 6.1;
Order P-3-08
Depreciation – Revised Depreciation Rates**

On page C-2 of the InterGroup Report, VAFFC states:

A review of PKMJF's 2019 Depreciation Study indicates that the proposed depreciation rates are excessive and not justified. First, the 2010 negotiated depreciation rates were designed to fully recover the JFL assets by a retirement date of December 31, 2022. By PKMJF's own submission, those rates should have been revised, but were not, each year of the contract period to reflect the impact of additions and retirements. It was PKMJF's responsibility to regularly review the depreciation rates and underlying life components which, from all appearances, it did not. This would have reduced the reported undepreciated costs as of December 31, 2018. [*Emphasis added*]

13.1 With respect to the statement identified in the preamble above, please provide any evidence VAFFC may have showing PKMJF did not regularly review depreciation rates.

Response:

The evidence that PKMJF did not adjust its rates is shown through comparison of the depreciation rates from the negotiated settlement in Exhibit A2-1 with depreciation rates from the Application (Exhibit B-14, Schedule 5, as revised). The "existing depreciation rates" in the Application are identical to the negotiated settlement rates, despite the fact that some new assets were added and there remains only 4 years left to the original life span date of 2022. This is an error in application of the depreciation life span date of 2022.

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Exhibit A-2-1 provides the schedule for depreciation and amortization rates for the JFL to be effective January 1, 2010. Note 1 from the schedule states:

The proposed reduction in useful life is based on amortizing the net book value as January 1, 2010 of the remaining assets over the contract term plus 1/2. Reduction of the useful life to align with the contract term, reduces some of the risk to TMJ for not recovering the full asset value over the term of the negotiated agreement. TMJ further expects that a shipper may continue using the pipeline services after the term of the agreement expires.

13.2 Please confirm that the depreciation schedule agreed to during the negotiated settlement period established a 13-year useful life for the JFL and any future capital additions (i.e., all future capital additions would also have a 13-year useful life from the in-service date).

13.2.1 If confirmed, please explain the basis for VAFFC's concern regarding depreciation.

13.2.2 If not confirmed, please (i) provide documentation showing parties had agreed to a 2022 end of life for the JFL and any future capital additions, and (ii) explain how any capital additions would be treated for accounting purposes.

Response to BCUC IR 13.2, 13.2.1 and 13.2.2:

Not confirmed.

The depreciation schedule makes no mention of what depreciation rates to apply to additions incurred during the settlement period. However there is no sensible and internally coherent depreciation practice that would have all assets fully amortized by 2022, except the small amount of new additions which somehow would remain in service to 2023 or 2024 or 2025, etc.

Also see the PKMJF response to BCUC IR 3, 3.5.1.3, which states: "The last approved depreciation study for JFL lists the end of its life at December 31, 2022 based on BCUC-approved depreciation rates."

13.3 Please provide reference to the documents supporting that the JFL's asset retirement date is December 31, 2022.

Response:

See PKMJF's response to BCUC IR 3, 3.5.1.3, which states: "The last approved depreciation study for JFL lists the end of its life at December 31, 2022 based on BCUC-approved depreciation rates."

13.4 Please provide reference to the documents supporting that the depreciation rates during the negotiated settlement period were designed to achieve full recovery of the JFL,

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including any capital asset additions, by 2022.

Response:

Please see VAFFC's response to BCUC IR 13.2. Depreciation rates based on a final date of retirement, as is the case here, are naturally designed to provide full recovery of the associated net investments by that date when they will no longer be in service. Likewise, in order for additions incurred in the ensuing years to be recovered by the retirement of the JFL, they would have to be depreciated or amortized over the remaining years from the year added to December 31, 2022, as illustrated in Ms. Lee's evidence.

- 13.5 Considering TMJ expected that a shipper may continue using the pipeline services after the term of the agreement expires, please explain why PKMJF would not apply the rates as agreed by the schedule to capital additions made during the negotiated settlement period.

Response:

The "term of the agreement" referred to is to 2018 (9 years from the depreciation report). The depreciation terminal date was 2022 (13 years from the depreciation report, based on the "contract term plus 1/2" as cited). It is clear some shippers are indeed using the pipeline after the end of the term of the agreement in 2018. However, nothing in that citation suggests that PKMJF was designing rates such that some small capital upgrades or reinvestment that occurred during 2009-2018 would have enduring value beyond 2022 when the main pipeline itself was depreciated to zero.

Pages C-5 and C-6 of the InterGroup Report reference a response PKMJF made to BCUC IR 6.1 from the TJM 2007 Application for Approval of Tolls and Accelerated Depreciation (2007 Application)⁴, to support VAFFC's position that the depreciation rates were based on a 2022 retirement date and that the depreciation rates should have been recalculated each year to adjust for the impact of any incurred interim additions or retirements. VAFFC notes that applying this approach would likely require future additions and retirements to be expensed. BCUC IR 6.1 from the 2007 Application is reproduced below:

If the proposed 5-year remaining life is accepted, should the annual depreciation rate (Opening Net Book Value cost less accumulated depreciation) be updated in the remaining life (years 4-1) of the assets to reflect additions, retirements and more accurate retirement cost estimates?

Response:

TMJ will respond to this question in two parts: Depreciation rates on invested capital (i.e. assets) and Depreciation rate on the retirement cost estimate (i.e. cost of net salvage / removal):

- Depreciation rates on invested capital (i.e. assets): The depreciation rates as

⁴ <https://www.bcuc.com/ApplicationView.aspx?ApplicationId=154>.

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calculated for the invested capital are based on forecast 2007 closing balances. To the extent that the 2007 additions, retirements and proceeds differ from that provided for in the application, the depreciation rates should be recalculated. It is unlikely that these annual depreciation rates would need to be recalculated to reflect post 2007 additions and/or retirements as all capital improvements would be curtailed to the extent possible and if the expenditures are required, the costs would likely be expensed into the operations and maintenance accounts.

- Depreciation rate on the retirement cost estimate (i.e. cost of net salvage / removal): There is always some degree of uncertainty in developing a future retirement or abandonment cost estimate and to the degree that this cost can be better refined over time as better information becomes available it is recommended that these costs be reviewed annually and the depreciation expense on these costs adjusted accordingly.

By Order P-3-08 the BCUC denied TMJ's request to recover depreciation of the JFL over the proposed five years.

- 13.6 Given the BCUC denied TMJ's request for accelerated deprecation in 2008, please clarify why VAFFC would expect depreciated rates to have been recalculated each year during the negotiated settlement period.

Response:

The question is not clear. InterGroup did not rely on the 2007/08 5-year accelerated depreciation proposal to impose inferences on the 2009 negotiated settlement for 13 year accelerated depreciation. InterGroup was simply noting that when accelerated depreciation was discussed, particularly at a proceeding where PKMJF had the benefit of a widely-cited expert in depreciation as part of its team, all parties understood that once a life span is adopted, further capitalization of expenditures should be minimized, most spending (even on items that may otherwise be viewed as capital) should be expensed, and for those that are capitalized, recalculation of the rates is required.

Even though the BCUC denied the 5 year depreciation, this does not change the fact that accelerated depreciation over any terminal date period has the technical requirement for recalculation whenever new capital assets are added.

On page C-6 of the InterGroup Report, VAFFC states:

In keeping with the above, PKMJF should have either expensed spending during the negotiated settlement period (totaling \$3,354,000 as outlined below) or, if capitalized, PKMJF should have recalculated the remaining life and resultant depreciation rate each year during the 2010-2018 period for each account.

In response to VAFFC IR 12.1, PKMJF confirms it applies the United States Generally Accepted Accounting Principles (US GAAP).

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- 13.7 Please provide reference to the relevant US GAAP accounting standard that permits expensing of capital additions.

Response:

None of the InterGroup witnesses is an accountant. However, expensing capital additions was specifically referenced by PKMJF as the practice it would follow once accelerated depreciation was implemented (Exhibit B-5, 2007 Application, Responses to BCUC (IR1) 6.1).

- 13.8 Please provide the relevant US GAAP accounting standard that permits calculating depreciation expense for a capital asset on a basis other than the asset's useful life.

Response:

None of the InterGroup witnesses is an accountant. InterGroup is not recommending accounting practices or depreciation parameters for financial reporting purposes.

Note that PKMJF did not itself adopt this approach for financial reporting purposes. After determining that the useful life of the pipeline was only to 2022 (as part of the 2009 settlement), PKMJF started amortizing all additions over 13 years, even if the asset was added with less than 13 years remaining until 2022.

In response to VAFFC IR 12.12, PKMJF states:

It has only recently become apparent with a reasonable level of certainty that the Jet Fuel Line's economic life will end by 2021. As noted, only within the last year has the in-service date for the VAFD project become reasonably certain, including the Government of British Columbia's September 17, 2018 determination that the VAFD Project had been substantially started, the VAFD project receiving its final outstanding approval from the City of Richmond during the period these IR responses were being prepared (July 22, 2019), and recent confirmation on the VAFD website that its expected in-service date remains at the end of 2021.

- 13.9 Under a scenario where PKMJF were only notified of the VAFD project in September 2018, please clarify why PKMJF would have reason to request approval from the BCUC to re-calculate the remaining life and depreciation rates prior to that date.

Response:

PKMJF was aware of the VAFD project dating back to before 2007, and familiar with its progress throughout the next 10 years as VAFFC took step after step to advance the project.

With respect, the premise of the question is incorrect and does not reflect the reality of the extensive and numerous updates that PKMJF had available to it. For example, the 13-year accelerated depreciation adjustment embedded in the 2009-2018 negotiated settlement was based on VAFFC's development of the VAFD.

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The issue is not one of the degree of certainty, it is one of erroneous misapplication of the principle of terminal dates by PKMJF.

On pages C-11 and C-12 of the InterGroup Report, VAFFC states:

Even though 2010-2018 was a negotiated toll settlement period, there was sufficient evidence by 2009, 2011, and incontestably by 2013 that the VAFD project was proceeding. It was PKMJF's responsibility to either apply its practice of recalculating depreciation rates in response to a fixed date, or otherwise seek additional depreciation recovery. By not booking the appropriate depreciation expense needed to achieve full recovery by 2022 as designed, PKMJF received increased earnings and only now requests increased depreciation rates to make up for the shortfall. In other words, it benefitted financially by not implementing the 2010 depreciation rate design in a manner consistent with its own procedures. Shippers have already paid the funds that should be directed toward depreciation balances and should not have to pay twice.

- 13.10 Please discuss whether a common carrier is expected to react to or change operations based on speculation.

Response:

There is no conclusion in the InterGroup evidence to suggest PKMJF should have changed operations.

A common carrier should be expected to react to business information and respond in prudent fashion. Again, with respect, the premise of the question ("speculation") does not reflect the reality of the situation. PKMJF faced the risk of funding abandonment costs itself under the settlement and if it wanted to mitigate that risk it should have reacted to the very firm and increasingly permitted project by applying to the BCUC to vary the tolls derived from the settlement.

Otherwise, InterGroup recommends that PKMJF should have properly applied proper terminal life depreciation to 2022, as provided for in the settlement documentation.

For further discussion of the obligation of a public utility and common carrier to change its business decisions (e.g., to expand its system to meet an obligation to serve or the choice to run an existing system to obsolescence), please see VAFFC's response to BCUC IR 6.11.

- 13.11 With reference to the applicable US GAAP standard, please provide the basis for PKMJF to seek approval for accelerated depreciation in 2013.

Response:

InterGroup's interpretation of the 2009-2018 negotiated settlement, based on publicly available information, is that it established a terminal retirement date of 2022 (13 years) and that PKMJF misapplied the terminal date in relation to the depreciation of the capital

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additions it made during the settlement period.

InterGroup's view of the information about the VAFD available to PKMJF between 2009 and 2013 is that, if PKMJF sought to explicitly commence collecting abandonment funds to mitigate the abandonment cost risk it faced (as the settlement offers no protection and PKMJF was aware of the risk of abandonment, evidenced by the settlement's accelerated depreciation content), it should have applied to the BCUC before 2013 based on the information available to it at that time.

To do otherwise would be to grant PKMJF a protection (and foist upon shippers a risk, and a cost) that there is no legislative or policy or economic basis to implement.

- 13.12 Please explain where it was agreed depreciation for the JFL capital assets, including any capital additions made during the negotiated settlement period, were to be fully recovered by 2022.

13.12.1 If no evidence of such an agreement exists, please discuss why VAFFC considers that (i) depreciation expense was not appropriately recorded during the negotiated settlement period, and (ii) the depreciation during the test period is making up for the "shortfall".

Response to BCUC IR 13.12 and 13.12.1:

The evidence is in the depreciation schedule attached to the negotiated settlement (filed in this proceeding as Exhibit A2-1). Depreciation for *all* categories, per the last column, was *adjusted* to 13 years, or the end of 2022 (unless the physical life was *shorter*). While the document is silent as to what happens to additions in future years, there are two potential interpretations, and only one is consistent with depreciation practice and hence reasonable.

The first interpretation is that PKMJF could amortize all assets including new additions over 13 years. But under this interpretation, an asset added in 2018, for example, is amortized to 2031. This makes no sense if the entire pipeline asset base, including the mainline pipe, is expected to be retired in 2022.

The second interpretation is that all assets should be amortized over the remaining period to 2022. Only this interpretation makes any sense, and is the only interpretation that reflects proper depreciation practices.

Further, it is noted that PKMJF elected to apply the interpretation that increased the net income, at the expense of reducing net rate base.

- 13.13 Is it reasonable to conclude that PKMJF is revising the depreciation rates because it is only now aware of the status of the VAFD Project and impact the VAFD Project will have on the economic viability of the JFL? If so, please explain how the depreciation rates could be making up for a "shortfall". If not, please explain why not.

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Response:

Absolutely not. That would be a materially unreasonable conclusion.

PKMJF had abundant information about the status of the VAFD pipeline, sufficient to negotiate a 13 year life in 2009, and has not claimed surprise or ignorance of the underlying facts at any point in its Applications or information request responses. Please see also VAFFC's response to BCUC IR 2.6, 2.6.1, 2.8 and 2.8.1.

Regarding the impacts of the VAFD project on the JFL, PKMJF on the one hand claims it has not engaged with shippers to assess the impacts (beyond a newspaper interview), and on the other hand its former parent claimed during the transaction process that "minimal to no impact is expected to the KML jet fuel line should the VAFFC project advance" (as referenced in the response to BCUC IR 23.8). Also noteworthy are:

- 1) the testimony of Parkland, which has not made a determination of its future shipping needs; and
- 2) the evidence of VAFFC that the airlines may continue to ship on the JFL if tolls are appropriate and favourable.

13.14 Under a scenario where PKMJF sought BCUC approval for accelerated depreciation during the negotiated settlement period to achieve full recovery of the JFL and forecast capital additions by 2022, please comment on whether VAFFC would have been willing to absorb the incremental cost increase at that time. If yes, please explain why circumstances have changed. If not, please explain why not.

Response:

With respect, the question is hypothetical and not consistent with the facts in this situation.

That said, VAFFC members would have been willing to confirm that PKMJF would achieve full recovery of the JFL and capital additions constructed during the negotiated settlement, sooner than 2022 – but there would not have been an incremental cost to shippers, for the following reasons.

First, PKMJF already negotiated that precise approach to depreciation in 2009 – no further BCUC approval was required (see the response to BCUC IR 13.12 and 13.12.1 above).

Second, had PKMJF properly applied the depreciation approach, the PKMJF earnings would have still far exceeded any reasonable regulatory standard by factors of [REDACTED]. PKMJF would not have been motivated to come back to the BCUC (and did not) to apply for a new litigated toll on a cost of service basis that would have materially reduced the tolls it was already receiving.

Third, as noted above, VAFFC would not have faced a situation where a litigated toll

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would have been an “incremental cost increase” – had PKMJF opened its books for a toll review on a cost of service basis, there would likely have been a significant toll reduction.

- 13.15 Please explain how recording depreciation at a rate that achieves full recovery of the JFL is consistent with depreciation rates the BCUC directed and provided in Exhibit A2-1.

Response:

Please see the response to BCUC IR 13.12 and 13.12.1 above. The BCUC did not “direct” the rates from Exhibit A2-1; rather, it accepted the settlement between the parties.

- 13.15.1 In VAFFC’s view, did Order P-3-08 and the accompanying decision, in any way restrict PKMJF’s ability to use accelerated depreciation rates in subsequent negotiated settlement periods? Please explain.

Response:

No.

The Reasons for Decision accompanying Order P-3-08 do not preclude the use of accelerated depreciation rates in any future toll or negotiated settlement. Under a common carrier framework, much like any commercial negotiation, customers and suppliers are free to negotiate prices that reflect a reasonable set of trade-offs.

- 13.15.2 Please elaborate on how PKMJF received “increased earnings” during the negotiated settlement period by recording depreciation as directed by the BCUC. Please provide supporting calculations.

Response:

Very simply, because PKMJF did not record depreciation “as directed by the BCUC”.

Upon the expiry of the 10-year negotiated settlement, PKMJF erroneously (and self-servingly) applied a new interpretation to additions in future years (further described in the response to BCUC IR 13.12 and 13.12.1 above).

PKMJF’s approach reduced depreciation expense recorded, and correspondingly increased net income to the same degree. The calculations are set out in the InterGroup evidence at Appendix A, page A-30.

- 13.16 Please elaborate on how PKMJF benefitted financially by not implementing the proposed 2010 depreciation rate.

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13.16.1 Please quantify the test period depreciation costs that shippers have “already paid”. Provide supporting calculations and references to the source figures used for the comparison.

Response to BCUC IR 13.16 and 13.16.1:

PKMJF’s approach reduced depreciation expense recorded, and correspondingly increased net income to the same degree. The calculations are set out in the InterGroup evidence at Appendix A, page A-30.

On page 10 of VAFFC’s Direct Evidence, VAFFC states that “[t]he VAFD Project received its conditional EAC on December 11, 2013, and the EAO determined that the VAFD Project had been substantially started on September 18, 2018. PKMJF sought accelerated depreciation and abandonment costs on June 7, 2019.”

13.17 Given the above, please explain how it was “incontestable” by 2013 that the VAFD project was proceeding.

Response:

Any project goes through multiple stages of development, each of which represents progress and commitments by the developer. No single step is fully determinative of completion until the first barrel is shipped – by this standard, one could argue that the project still is unknown until it comes into operation.

The issue is when the progress, commitments and investments made are sufficient to recognize that a project is likely to proceed, and it is prudent to begin to take actions reflecting that expectation. As noted at paragraph 31 in the VAFFC evidence: “VAFFC aggressively permitted the VAFD Project between 2009 and 2013, spanning federal and provincial environmental assessments and related court actions. Matters were largely permitted by 2014.” For PKMJF, these facts were sufficient in at least 2009 to pursue accelerated depreciation. By 2013, the facts had only been strengthened.

Of note, during the 2014-2018 period, VAFFC continued to actively permit the VAFD with the City of Richmond. The City of Richmond’s opposition to the Trans Mountain Pipeline Expansion Project during this period complicated and delayed the progress of the VAFD beyond normal timelines. The critical and fundamental EAO permit was in hand.

Again, between 2009 and 2013, it would have been clear to PKMJF that a myriad of expert evidence had been marshalled, detailed plans were in place, property had been purchased, relevant stakeholders and indigenous, municipal, provincial, and federal governments had been fully consulted and engaged with, and the project continued to advance.

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- 14.0 Reference: COST OF SERVICE
Exhibit B-38, VAFFC IR 10.7; Exhibit C2-36-2, InterGroup Report, Appendix C, Section 3.1, pp. C-8, C-9
Depreciation – Misapplication of Group Depreciation**

On pages C-8 and C-9 of the InterGroup Report, VAFFC states PKMJF misapplied the Group Depreciation procedure in calculating depreciation expenses which has understated annual depreciation expenses and artificially overstated earnings, the effect of which could be material. Specifically, VAFFC's Intervener Evidence specifies the following error:

...in some cases where individual assets became fully depreciated, the original cost of those assets were no longer depreciated while not decreasing the tolls in a like manner. This is not group depreciation.

In response to VAFFC IR 10.7, PKMJF states:

PKMJF's understanding is that KMJF applied the group method of depreciation, but that in some rare instances individual vintage year assets were fully depreciated prior to the entire account becoming depreciated. PKMJF notes that if the 2019 depreciation study rates and approach applied, each account will become fully depreciated[sic] at the end of PKMJF's remaining economic life at the end of the currently applied for tolling period (assuming that there are no additions or retirements).

- 14.1 Considering that the instances where individual assets were fully depreciated prior to the entire account becoming depreciated were (i) rare and (ii) limited to "vintage year assets", please elaborate on the possible materiality of an error with the group method of depreciation.

Response:

The only evidence that the instances were (i) rare and (ii) limited to "vintage year assets", is the word of PKMJF. The instances admitted to by PKMJF are a symptom that PKMJF's data is suspect. Whether the effect of applying incorrect group depreciation practices would be material cannot be confirmed without more data. For proper confirmation, InterGroup has recommended that this data be provided, in recommendation 11 at page 8 of the InterGroup evidence.

- 14.1.1 Please discuss the likelihood of this error having a material impact on the revenue requirement in the Test Years.

Response:

See VAFFC's response to BCUC IR 14.1.

- 14.2 In a hypothetical scenario where the rates in the 2019 depreciation study are approved, and there are no additions or retirements, does VAFFC agree each account would be fully depreciated at the end of the JFL economic remaining life? Please explain why or why not.

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Response:

No.

The hypothetical scenario presumes that the JFL will not be producing any revenue once the VAFD project goes into service. There is no evidence that this will be the case.

15.0

**Reference: COST OF SERVICE
Exhibit C2-36-2, InterGroup Report, Appendix C, Section 3.3, pp. C-10, C-11
Depreciation – Cost of Removal – 2009 Unrecovered Removal Costs**

On pages C-10 and C-11 of the InterGroup Report, VAFFC states:

It is unclear how the unrecovered removal costs of \$58,669 shown in 2009 were determined. Also, there is no detail separately distinguishing interim retirements from the associated removal costs. There is also a question as to why those removal costs did not have any historical accumulated depreciation applied. As mentioned above, it is not clear how removal costs were treated prior to 2009. It is possible that the cost of removal shown in 2009 reflects the net of the net book value of the retirements less removal costs. Despite the fact that this was found acceptable in 2009 by all parties, the amount could be overstated.

15.1 Please provide any evidence VAFFC has supporting that the unrecovered removal costs could be overstated.

Response:

VAFFC does not have any specific evidence, but the onus belongs to PKMJF and, given PKMJF's inconsistent presentation of information and poor record with respect to depreciation practices and understanding, it is not known whether unrecovered removal costs were properly recorded. There are ambiguities in PKMJF's description of unrecovered removal costs. For example, these costs are described as removal costs, but PKMJF also indicated they included "the cost of current retirements and removals..." (see footnote 38 at page C-10 of the InterGroup evidence). What is meant by "the cost of current retirements" if it is not removal (i.e., why the "and")? Is it potentially a net book value loss on disposal (i.e., unrecovered capital costs?) – such items should always go to the group account in group depreciation.

15.2 Considering the unrecovered removal costs were found to be acceptable by all parties in 2009, please clarify the relevance of these costs to the current test period.

Response:

The unrecovered removal costs are being amortized over the remaining service life of the JFL. Current test period cost of removal expenses would be overstated to the extent the starting point in 2009 was overstated. While these unrecovered removal costs have little impact on tolls in the test period, they are particularly relevant because they illustrate inconsistent practices and a lack of understanding of group depreciation and

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removal cost accounting on the part of PKMJF.

- 15.3 Please discuss whether the alleged overstatement is likely to have a material effect on the cost of service in the Test Years.

Response:

No.

Please see VAFFC's response to BCUC IR 15.2.

- 16.0** **Reference: COST OF SERVICE**
Exhibit C2-36-2, InterGroup Report p. 6; Appendix A, pp. A-17, A-18, A-24
Negotiated Settlement History

On page 6 of the InterGroup Report, VAFFC states:

PKMJF (and the respective shareholders, at present and previously) operated the pipeline in a manner that failed to protect the inherent value of the assets, and not only permitted bypass, but acted in a manner that encouraged bypass and the resulting adverse impacts on the long-term value of the PKMJF assets. [Emphasis added]

Further, on page A-18 of the InterGroup Report, VAFFC states:

As a Common Carrier and not a franchised Public Utility, customers are not captive to PKMJF, and it is clear PKMJF undermined their market position and the long-term potential value of their assets by making their own service less economic than necessary. Events since that time underline this perspective. [Emphasis added]

- 16.1 Please explain how PKMJF "permitted bypass".

Response:

As set out in various sections of the InterGroup evidence and the record from the 2007 proceeding, PKMJF held the dominant position with respect to service to YVR.

As far back as the early 2000s or before, it was apparent that the YVR future needs could not be met by the single PKMJF pipeline. As noted at in the VAFFC evidence: "In 2007 ... PKMJF claimed that VAFFC had decided to bypass the Jet Fuel Line, and that as a result, the economic life of the Jet Fuel line was only five years" (paragraph 22). Indeed, VAFFC's argument from the 2007 proceeding noted that "VAFFC has met with TMJ several times since 2003 to advise TMJ that VAFFC is considering alternative ways of meeting future requirements and to request information on the future expansion potential of the TMJ pipeline" but that "TMJ has shown little interest in improving,

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expanding or even operating this pipeline in future”.⁵ This is consistent with the BCUC’s descriptions in Order P-1-06 where it notes PKMJF had only interim tolls for 2005 set at January 5, 2005 and an application to finalize these interim tolls was expected but instead PKMJF filed a letter December 14, 2005 that “informed the Commission that discussions with its Shippers had occurred during 2005 centered primarily on the long-term prospects of the jet fuel pipeline rather than finalizing 2005 tolls” and that the airlines never saw a proposal to finalize 2005 tolls until December 21, 2005.⁶

Concepts such as twinning the PKMJF pipeline were put forward but not followed through. A twinned pipeline would clearly have synergy advantages that an entirely new supply would not.

The PKMJF responses to this market threat were to materially increase prices rather than preserve its market position. With reference to Figure 1 of the InterGroup evidence (reproduced below), when faced with this market challenge, PKMJF took a pipeline that was operated for approximately \$3 million per year (2006) and sought \$6 million (2007 – reduced by the BCUC to \$3.5 million), received approval for \$4 million for 2009, re-negotiated this 2009 value up to almost \$5 million, negotiated \$6 million per year from 2010, and grew this value to \$7 million by 2018. PKMJF now seeks values exceeding \$7 million. These values all exclude the cost of removal (where any specific allocation was identified) which would have made costs even higher. These values also increase despite materially decreasing net investment, as little new capital is invested in a pipeline being managed for obsolescence.

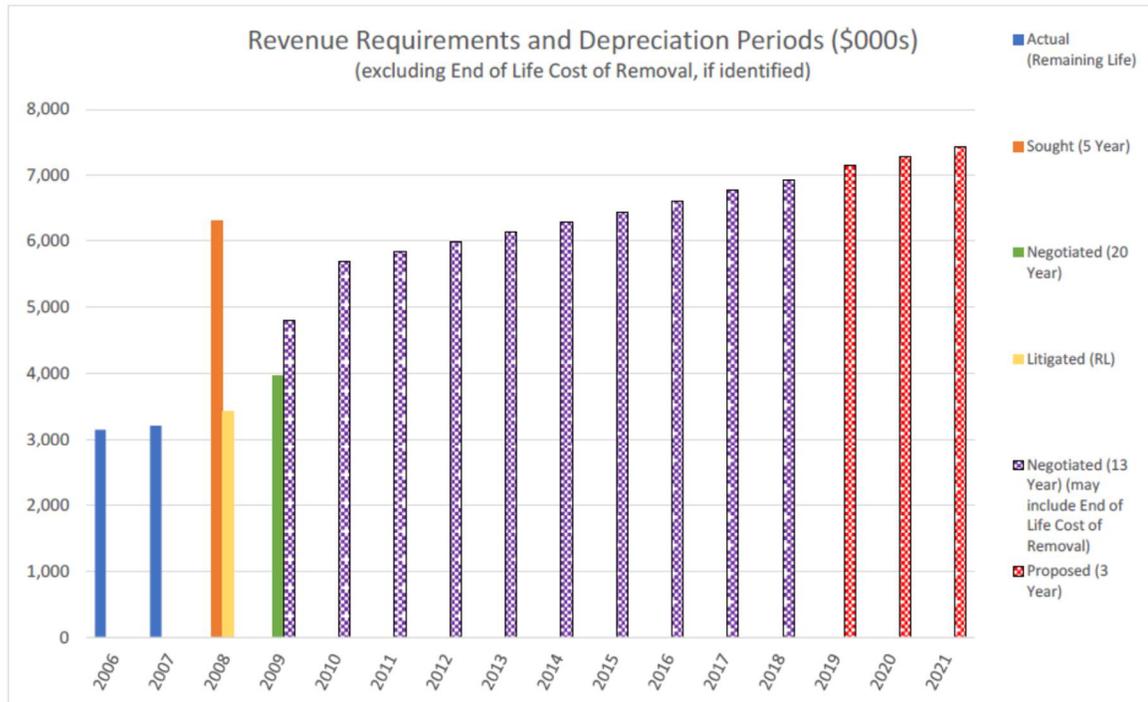
Regardless of when VAFFC made the critical decision to develop and make commitments to its new project, it faced market destroying tariff escalation. The rapidly escalating tariffs under the negotiated settlement for 2009-2018 made the PKMJF Jet Fuel Line less economic, and the VAFD project more desirable.

⁵ VAFFC argument, December 10, 2007, paragraphs 3.5 and 3.6

⁶ BCUC Order P-1-06, page 2.

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Figure 1: Revenue Requirements and Depreciation Periods 2006-2021



16.2 As an alternative to developing its own system, did VAFFC consider and/or approach PKMJF regarding the potential for a bypass rate? Please discuss.

Response:

Please see VAFFC’s response to BCUC IR 2.8.

VAFFC and PKMJF have been in regular discussions regarding the VAFD Project from the beginning. As noted in the VAFFC consultation tracking table referenced in VAFFC’s response to BCUC IR 2.8, during the early days of the VAFD Project, VAFFC:

“...consulted with TMJ about options for the expansion of the existing pipeline. TMJ expressed no interest in expansion and, in fact, advised VAFFC and the shippers that it was no longer interested in operating the aviation fuel pipeline. TMJ explained that the aviation fuel pipeline did not fit within the core business interests of the Kinder Morgan operation...”

Expanded capacity was necessary to meet the needs of VAFFC members and VAFFC proceeded to develop the VAFD.

16.2.1 If not, please explain why not.

Response:

Please see VAFFC’s response to BCUC IR 16.2.

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- 16.3 Please explain how PKMJF undermined their market position and the long-term potential value of their assets by making their services “less economic than necessary”.

Response:

Please see VAFFC’s response to BCUC IR 16.1. It is clear that a pipeline with relatively high fixed costs, which operated at a full recovery of revenue requirement of approximately \$3 million in 2006 would not have seen cost escalation to almost \$6 million by 2010. We now know that this corresponded to a booked return of over \$2.1 million⁷ in 2009 which represents over one-third of the tolls paid, and is triple the last awarded return which was in the order of \$0.7 million.⁸

On page A-17 of the InterGroup Report, regarding the 2009-2018 negotiated settlement period, VAFFC states, “The settlement documentation provided publicly to the BCUC lacks detail. Other than the total revenue requirement, and a depreciation schedule, no numerical detail is provided.”

On page A-24 of the InterGroup Report, VAFFC states:

At the time of the 2009-2018 negotiated settlement, for whatever reasons were relevant at the time, shippers agreed to a tolling regime predicated on the PKMJF assets being fully depreciated and no longer in service as of the end of 2022 (13 years from the negotiated implementation of accelerated depreciation at January 1, 2010).

Whatever the intent at the time of the settlement, PKMJF’s current Application effectively seeks to impose and crystallize now the identical outcomes that such improbable and commercially unreasonable approaches would have targeted, which is inherently double-counting abandonment recoveries from customers.

- 16.4 Please confirm that VAFFC was the negotiator and/or representative for its members at the time when the 2009-2018 negotiated settlement took place.

Response:

VAFFC understands that a VAFFC representative and Air Canada representatives participated in the negotiations leading up to the 2009-2018 negotiated settlement.

Please also see VAFFC’s response to BCUC IR 16.4.3.

⁷ InterGroup evidence Document C2-36-1, page B-14 Table 3.

⁸ See InterGroup evidence Document C2-36-2, pdf page 152.

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16.4.1 If confirmed, what shippers did VAFFC negotiate on behalf of?

Response:

Please see VAFFC's response to BCUC IR 16.4.

16.4.2 If not confirmed, who negotiated on behalf of shippers?

Response:

Please see VAFFC's response to BCUC IR 16.4.

16.4.3 If VAFFC was not part of the negotiations, how can VAFFC conclude that shippers agreed to a tolling regime based on PKMJF assets being fully depreciated by the end of 2022?

Response:

Please see VAFFC's response to BCUC IR 13.12, 13.12.1 and 16.4.

VAFFC was part of the negotiations leading up to the 2009-2018 negotiated settlement, but neither possesses any written agreement nor retains full knowledge of the detailed reasons behind the toll and depreciation schedules filed at the end of 2009.

VAFFC has adopted InterGroup's conclusion that shippers agreed to a tolling regime based on PKMJF assets being fully depreciated by the end of 2022. That conclusion is based on Ms. Lee's analysis of publicly available documents and the application of her – considerable and well-established – professional judgment and expertise. Her conclusion is clear and unambiguous: "The 2010 depreciation study established rates that should have allowed PKMJF to recover its net investment in the Jet Fuel Line (including any capital additions during the 2009-2018 negotiated settlement period) by the end of 2022."¹⁶

16.5 If VAFFC was the negotiator, please discuss and provide rationale for why shippers agreed to the tolling regime set out in the negotiated settlement.

Response:

VAFFC understands that one of airline shippers' significant motivations to agree to the negotiated settlement was to avoid Kinder Morgan intervening in the environmental assessment process to oppose the VAFD Project.

Please also see VAFFC's response to BCUC IR 16.4 and 16.4.3.

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16.5.1 Please explain whether shippers had any concerns about the tolling methodology at the time it was negotiated.

Response:

Please see VAFFC's response to BCUC IR 16.5 and 16.4.3.

16.5.1.1 If yes, were these concerns communicated to the BCUC and/or PKMJF? Please provide details, and any supporting documentation, if possible.

Response:

Please see VAFFC's response to BCUC IR 6.7, 6.7.1 and 6.7.2, 16.5 and 16.4.3.

16.6 Please discuss why the terms of the negotiated settlement were accepted for the 2009 to 2018 period but appear to be undesirable now.

Response:

Please see VAFFC's response to BCUC IR 13.12, 13.12.1, 13.14, 16.4.3 and 16.8.

PKMJF's costs of service, including a reasonable profit, were well below the amounts PKMJF received under the settlement. That fact is evident by comparing the 2009 tolls applied for and consented to on a single-year basis, and those applied for and consented to as part of the negotiated settlement.

Large revenues that exceed reasonable costs and a fair profit should therefore not continue. VAFFC members agreed to the settlement for reasons other than cost of service.

16.7 Please list the risks that shippers assumed during the 2009 to 2018 period.

Response:

With respect to tolls, the key risk was for volume. Please also see the discussion of risk allocation in response to BCUC IR 6.1, 6.2 and 6.9.

16.8 Please confirm that the current risks for each shipper are the same as the risks during the 2009-2018 negotiated settlement agreement. In the response, please include an explanation as to why risks that were assumed by shippers during the 2009 to 2018 period are now regarded as no longer fair nor appropriate.

Response:

The current risks, as they apply under the interim rates, appear to yield the same risks to shippers as 2009 to 2018. This is no longer fair nor appropriate as set out in the

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response to BCUC IRs 6.1, 6.4, 6.9, 6.11, 6.12, 16.5 and 16.6.

- 16.9 Please provide any further details or correspondence, in confidence if necessary, related to the discussions regarding the 2009-2018 negotiated settlement agreement. For example, any issues or concerns raised by VAFFC/other shippers or additional documentation related to volume risk.

Response:

Please see VAFFC's response to BCUC IR 16.4.3 and 16.5.

On page A-18 of the InterGroup Report, VAFFC states:

Surprisingly, even though PKMJF had no entitlement to guarantees of capital cost recovery or accelerated depreciation, the 2009-2018 negotiated settlement largely secured this right for PKMJF (i.e., all asset costs to be recovered by 2023). But this was not the only surprising aspect – PKMJF also secured tolls with material unexplained increases from shippers. Costs to shippers therefore increased with little rationale and no apparent added value. [Emphasis added]

- 16.10 Please discuss how the 2009-2018 negotiated settlement 'secured' the right for PKMJF to accelerate depreciation. In your response, please provide any evidence available to support this.
- 16.10.1 Please explain why shippers agreed to these terms if PKMJF had no entitlement to such rights.

Response to BCUC IR 16.10 and 16.10.1:

The depreciation schedule attached to the negotiated settlement sets out that the depreciation period is to be fixed at a maximum of 13 years, such that all assets are fully depreciated by 2022. This is provided in the current proceeding in Exhibit A2-1.

Under a common carrier framework, much like any commercial negotiation, customers and suppliers are free to negotiate terms that reflect a reasonable set of trade offs.

Please see also VAFFC's response to BCUC IR 16.4.3.

- 16.11 Please explain how PKMJF secured tolls with material increases from shippers.

Response:

The increases were negotiated. Under a common carrier framework, much like any commercial negotiation, customers and suppliers are free to negotiate terms that reflect a reasonable set of trade offs.

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16.12 Did VAFFC or any other shipper raise concerns with PKMJF or ask for the rationale behind the cost increases quoted above at the time of negotiations or during the 2009-2018 settlement period? If yes, please provide documentation to support this.

Response:

Please see VAFFC's response to BCUC IR 16.4.3 and 16.5.

Please see the slide deck from the Jet Fuel Line shipper meeting held on December 2, 2008,¹⁷ which was provided by PKMJF concerning its 2009 tolls, several months before settlement negotiations, attached as Appendix BCUC 16.12. VAFFC understands that shippers knew the toll increases were not based on cost increases but, rather, other trade-offs.

17.0

**Reference: COST OF SERVICE
Exhibit C2-36-2, InterGroup Report, Appendix A, pp. A-17, A-20
Negotiated Settlement Tolling Methodology**

On page A-17 of the InterGroup Report, VAFFC states:

The PKMJF settlement introduces to tolls the concept of shippers bearing risk for volume. This is achieved by setting an overall revenue requirement, and only finalizing tolls once the annual volumes are known and adjustments can be made to ensure PKMJF recovers the specified revenue requirement, regardless as to throughput. This form of tolling for PKMJF is unusual, and appears to only have been used once prior – the incentive tolling agreement from 1998-2002.

17.1 Please explain why this form of tolling is considered unusual for PKMJF if it has been used previously with shippers only a number of years prior to the 2009-2018 negotiated settlement period.

Response:

Please see the response to BCUC IRs 6.1, 6.4, 6.9, 6.11, and 6.12. The tolling method is unusual for shippers because a different method is applied on most other liquids pipelines and a different method has been applied for 39 of the past 53 years.

17.2 Please explain why VAFFC refers to the 1998-2002 tolling agreement as the "incentive" tolling agreement. In your response, please discuss the incentives that were agreed upon at that time.

Response:

The period was known as the "incentive" tolling period because that was the name given to the agreement by the parties to it. See Order P-3-98, and in particular page 2, paragraph 4 which sets out the specific incentives that are said to be part of the agreement (e.g., the efficiency incentive, the excess capacity incentive, etc.). Neither

¹⁷ See Exhibit C2-36-2 at pdf p. 147.

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VAFFC nor InterGroup has a copy of the Incentive Agreement to provide more detail than exists in the various Orders over the period, as well as P-1-06.

17.2.1 Did the 2009-2018 negotiated settlement agreement contain incentives? In your response please discuss what, if any, incentives were present and any benefits shippers/PKMJF received.

Response:

No. To VAFFC's knowledge, no written agreement was made. Clearly, no incentive mechanisms were filed with the BCUC. Accordingly, the only relevant incentives would be those natural to an operator under a regulated tariff, such as minimizing direct cash costs (e.g., O&M) in order to increase profits, and to maximize allocated costs to PKMJF away from unregulated affiliates (e.g., administrative allocations), all of which would make the returns to PKMJF appear less exceptional and set the appearance of a higher price benchmark going into the next litigated toll-setting period.

17.3 Please provide further details on the 1998-2002 incentive tolling arrangement, including but not limited to, who negotiated on behalf of shippers and if any complaints or concerns were raised by shippers during negotiations or throughout the tolling arrangement.

Response:

VAFFC has reviewed its records, and has been unable to locate any further details regarding the 1998-2002 incentive tolling arrangement.

17.3.1 Why did shippers agree to bearing the risk for volume during the 1998-2002 period? Please elaborate.

Response:

Please see VAFFC's response to BCUC IR 17.3.

17.3.2 During this period, were there any competitive alternatives to the JFL available, or considered by shippers? Please describe any such alternatives and whether shippers availed themselves of these alternatives.

Response:

During this period, tanker truck deliveries were the only alternative to the JFL for transporting jet fuel to YVR.

17.3.3 If other viable option(s) were available, or considered, such as a potential bypass during the 1998-2002 period, would shippers have agreed to bear the volume risk? Please explain.

Response:

No current VAFFC representatives recall the detailed discussions between

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shippers and PKMJF that resulted in the incentive tolling settlement agreement, as these discussions occurred more than 20 years ago. Similarly, VAFFC is unable to speculate on what shippers may or may not have agreed to in 1998, if alternative proposals had been considered at the time.

Please also see VAFFC's response to BCUC IR 17.3.

- 17.3.4 If there was another viable option, such as a potential bypass during the 2009-2018 period, would shippers have agreed to bear the volume risk? Please explain.

Response:

No current VAFFC representatives recall the detailed discussions between shippers and PKMJF that resulted in the 2009-2018 negotiated settlement agreement. Similarly, VAFFC is unable to speculate on what shippers may or may not have agreed to in 2008, if alternative proposals had been considered at the time.

Please also see VAFFC's response to BCUC IR 16.4.3 and 16.5.

On A-17 of the InterGroup Report, VAFFC states:

The revenue requirements for PKMJF jumped massively compared to all previous forecasts. For 2009, the revenue requirements were surprisingly revised upwards from the original 2009 proposed level of \$3.973 million, to \$4.800 million, a jump of 21% in the same year. This then escalated to \$5.694 million (a 19% increase) in 2010, a combined 66% increase (\$2.271 million) in 2 years, over the initially approved 2008 level. [footnote omitted]

The toll settlement provides no detail regarding justifying any PKMJF cost increases, outside of the depreciation revision on assets.

Further, on page A-20 of the InterGroup Report, VAFFC states:

The massive and unexplained increases arising from the 10-year negotiated settlement 2009-2018 give rise to significant questions about how the added revenue was justified and managed. Focusing just on the first 2 years – 2009 (second variant) and 2010, the revenue requirements jumped massively from the 2008 litigated and 2009 first negotiated revenue requirements...

- 17.4 Did VAFFC register any complaints related to cost increases, the toll methodology, or any other settlement terms to the BCUC or to PKMJF during the 2009-2018 negotiated settlement period? Please discuss.

Response:

VAFFC is not aware of any such complaints.

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17.4.1 If not, why not? In your response, please discuss whether this implies shippers were satisfied with the toll methodology during the 2009-2018 negotiated settlement period.

Response:

Please see VAFFC's response to BCUC IR 16.6, 16.12 and 17.4.

17.4.2 If the methodology was satisfactory during the 2009-2018 negotiated settlement period, is this methodology suitable now?

Response:

No. It is obvious from publicly available information that the toll levels agreed to were not cost-based tolls. Shippers agreed to the settlement at the time for reasons other than cost and no longer agree. Absent agreement, the methodology is unsuitable. The level of return achieved then was significant and should not repeat. Otherwise, please see VAFFC's response to BCUC IR 16.6 and 16.12 and 17.4.

18.0

Reference: COST OF SERVICE

**Exhibit C2-36-2, VAFFC Direct Evidence, p. 11; Intergroup Report, pp. 2-3, 6; Appendix A, p. A-3; Appendix B, B-2; Appendix D, p. D-10
Regulatory Principles**

On page 11 of VAFFC's Direct Evidence, VAFFC states:

In return for a franchise right (and duty) to provide service, the Public Utility receives the protections necessary to attract capital, typically including a reasonable opportunity to recover the cost of investments made on a prudent basis over the life of the investment, and earn a fair return on the invested capital.

In contrast, a Common Carrier does not generally receive the grant of any special authority or protection against competition.

The Application is clear that PKMJF is regulated by the BCUC as a Common Carrier. Through information request responses, however, PKMJF claims that the statutory protections accorded to Public Utilities in BC must be extended to it, including a guaranteed return on the appraised value of property. VAFFC opposes this claim. It does not fit either BC's statutory framework, the facts applicable to the Jet Fuel Line, or the history of regulation of the Jet Fuel Line. [footnotes omitted]

On pages 2 to 3 of the InterGroup Report, VAFFC states:

Common Carrier Principles are not Codified: As a Common Carrier (Part 4 of the Utilities Commission Act), PKMJF is under a framework with almost no specific

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legislative standards for tolls. The legislation is simply silent on matters such as the reasonableness of rates and the obligations of fair treatment to the shareholders. As a result, the proceeding occurs with major questions tied to the applicable regulatory (economic and legal) first principles. [Emphasis added]

18.1 In VAFFC's view, what are the applicable regulatory, both economic and legal, principles that should apply to a common carrier? Please list and discuss these principles as appropriate.

Response:

The main principles are as follows:

- Maintain a safe and reliable asset.
- Offer surplus capacity (i.e., that not reserved for own-use) on a non-discriminatory basis.
- Charge a price that is consistent for the same quantity and quality of service available to the open market participants (note, there is the potential for unique contract market pricing for individual customers or own-use under certain conditions).
- Fair pricing, preferably based on negotiations with customers but with recourse to a regulator to set prices based on a reasonableness standard, not unlike a cost of service standard for a utility. This is further set out in the InterGroup evidence at page A-10, and reproduced here:

For a Common Carrier, there is a hybrid outcome between the Public Utility and the competitive market. The investor in the Common Carrier has many of the characteristics of the entrepreneur – they make the decision to invest without legal (franchise) or natural monopoly barrier to a competitor. They make this initial investment on the premise they will recover their costs, but it is ultimately their own risks they are taking. Governmental orders would require that they offer their service to all who desire to use the service on a non-discriminatory basis, but at a price that is representative of a reasonable market value (as presumably evidenced by negotiation or a regulatory decision). As such, unlike a private entrepreneur, the Common Carrier cannot discriminate in service availability or price as between customers. Pricing for the Common Carrier could be established by negotiation with their customers, or resolved via a regulator with reference to a just or fair price. However, the freedom to set this price is not unlimited. The price must be reasonably linked to some value of service or cost to provide service for a set of well-managed long-term assets. An investment or action that does not lead to being a low and reasonable cost form of supply at each particular time will weaken the common carrier's value proposition to customers, and hence the enterprise's market position and its value. The benchmark fair or just price, then, would need to reflect a well-managed operation, consistent with a solid market position and the physical and long-term potential of the assets in the ground (broadly, this could be consistent with a fully allocated cost of service type of standard).

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Unlike Public Utilities, however, there is neither a desirable, nor a workable, means to ensure recovery of the common carrier's investment over the long-term. The outcome is not practical, since any charge above the value provided will lead to erosion of market – customers will simply forgo the service (e.g., where it is non-essential) or pursue other alternatives or service from competitors (including potential new entrants), or develop the service themselves (such as the stakeholders of VAFFC are now doing). The outcome of assured capital cost recovery is also not desirable, since forcing the market to support above-cost supply of services that could be provided at a lower cost is a clear inefficiency and net loss to society.

- Do not abandon assets or cease service without approval of regulators.

18.2 In VAFFC's view, should the regulatory principles applied for a common carrier differ from those of a public utility? Please explain why or why not.

Response:

Yes, the regulatory principles for a common carrier and public utility differ for very good legal and economic reasons. Please see Appendix A of the InterGroup evidence, section 2.

18.3 In VAFFC's view, what are a common carrier's entitlements with regards to toll setting? In your response please discuss whether any protections should be afforded to a common carrier.

Response:

Please see VAFFC's response to BCUC IR 18.1, and the InterGroup evidence, Appendix A, section 2. There are clear entitlements that exist for a common carrier with respect to toll setting, including the right to negotiate with customers to an acceptable tariff, and in the absence of such negotiation, the right to receive a rate established by an arm's length regulator. The rate to be established by the regulator should take into account all of the principles set out in VAFFC's response to BCUC IR 18.1 and the InterGroup evidence, Appendix A, section 2.

18.4 If, as VAFFC states, the legislation is silent on matter such as the reasonableness of rates and the obligations of fair treatment to shareholders, please discuss what is a reasonable approach in VAFFC's view to ensure fairness for both the common carrier (and its shareholders) and shippers.

18.4.1 Please explain why this approach should be adopted.

Response:

See the response to VAFFC BCUC IR 18.1 and the InterGroup evidence, Appendix A, section 2.

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On page B-2 of the Intergroup Report, VAFFC states, “For the past decade, PKMJF’s tolls were set based on a negotiated settlement, where revenue requirement was not established based on a pure cost of service framework.”

- 18.5 Please discuss why a “pure cost of service framework” was not used during the 2009-2018 negotiated settlement.

Response:

Under a common carrier framework, much like any commercial negotiation, customers and suppliers are free to negotiate terms that reflect a reasonable set of trade offs. The 2009-2018 negotiated settlement reflects terms that were presumably acceptable to the parties.

Please also see VAFFC’s response to BCUC IR 16.4.3.

- 18.6 Please discuss whether, in VAFFC’s view, a cost of service-based approach is appropriate for setting tolls for a common carrier in circumstances where a negotiated settlement has not been reached.

Response:

In the broadest sense, prices for service can be set by a regulator based on 3 different measures – (a) rates set at the direction of government, (b) rates set based on the “value” of service (with the next lowest cost alternative serving as the relevant benchmarks), or (c) rates based broadly on the “cost”. In this sense, yes, rates for a common carrier that cannot be negotiated should primarily be set based on a cost-based metric (i.e., negotiations may focus on (b) or (c), while failed negotiations that revert to a regulator should focus mostly on (c) with only limited attention to (b)).

Having said this, this is not strictly the same as a “cost of service” based approach as it would be understood for a public utility. The public utility has explicit legal rights, such as an opportunity to recover all prudently incurred costs, which do not extend explicitly to the common carrier for very good and principled reasons, and ought not be reflexively extended in practice. For a further explanation as to why this is the case, please see VAFFC’s responses to BCUC IR 18.1, 6.11, and InterGroup evidence, Appendix A, section 2.

Simply put, the common carrier framework begins with an operation that has been developed by an entrepreneur, but is handy for a broader use. The core of the common carrier concept of service is simple non-discrimination. The policy declaration is that the operation is handy enough that it should be made available to all who want to use it. This is the full extent of the first-principles, public interest rationale.

Regulation of tolling on common carriers is not an end-goal in and of itself, it is a backstop recourse when customers and the common carrier owner cannot come to an agreement on pricing, and the principle of “non-discriminatory use” becomes threatened by the common carrier over-exerting their market position. The basic question for toll-setting then is not one of precision, like in the case of public utilities, it is one that answers the basic questions *what ought it cost to provide this service if the operator is*

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doing it well, and not exercising excessive market power?

On page 3 of the InterGroup Report, VAFFC states:

Common Carriers and Public Utilities Differ: The status as a Common Carrier in BC is distinct and entirely separate from the far more prescriptive and well-established framework for setting rates and tolls for regulated Public Utilities. These rights and obligations, arising from Public Utility status, are not reflective of the PKMJF reality, and cannot be rottenly or reflexively applied to PKMJF.

18.7 Please discuss what is meant by 'not reflective of the PKMJF reality'.

Response:

PKMJF is not a public utility.

18.8 Please discuss what specific rights and obligations VAFFC is referring to in the above preamble and to what extent these are not applicable to a common carrier.

Response:

The rights and obligations referred to above are those extended in law and practice and economic theory to a public utility. For a further explanation, please see the responses to BCUC IR 18.1, 6.11, and InterGroup evidence, Appendix A, section 2.

On page A-3 of the InterGroup Report, VAFFC states:

It is clear from PKMJF's filings that PKMJF errs in its conclusions regarding its entitlements to recoveries from toll-payers. Such entitlements might be arguable in a scenario where PKMJF was a Public Utility. However, PKMJF is not a Public Utility, it is a Common Carrier. The distinction is critical, and of substantial import [sic] to the tolls that are merited in 2019-2021.

On page A-4 of the InterGroup Report, VAFFC states:

Despite PKMJF's status as a Common Carrier, many of its proposals are fundamentally rooted in concepts that apply to Public Utilities, but not necessarily to Common Carriers. The status of a Common Carrier reflects an Industrial Organization that lies somewhere between an industry without price and service regulation, and the heavily regulated status of a Public Utility. This fundamental misunderstanding or error by PKMJF leads to incorrect conclusions regarding its entitlements to recovery of costs.

18.9 Please discuss which proposals by PKMJF are 'fundamentally rooted in concepts that apply to public utilities...'

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Response:

PKMJF has proposed many revenue requirement items that assume they possess a protected and entitled position which is not supported in the facts. The proposals include accelerated depreciation, the right to foist volume risk on shippers, the right to collect all abandonment costs in the remaining 3 years (based on the life span asserted by PKMJF) because PKMJF elected to book nothing to the removal cost reserve even though [REDACTED] profits were earned by PKMJF for the past decade, and the – incredible, unprecedented, and rejected elsewhere – right to retroactively seek post-hoc abandonment true-up adjustments.

On page D-10 of the InterGroup Report, VAFFC states:

It was not VAFFC’s responsibility to have pursued dismantlement earlier. That responsibility was clearly a business decision of PKMJF, one that it chose to disregard, if it is to be believed that tolls in the period 2009-2018 were insufficient to provide for an abandonment reserve.

Additionally, waiting until this late date to seek explicit abandonment cost recovery is not consistent with Bonbright principles of fairness and avoiding undue discrimination and the corollary principle of intergenerational equity. It is patently unfair and discriminatory to begin collecting abandonment funds now that should have rightly begun some years ago when the risk of bypass was clearly known. Intergenerational inequity would be caused by this PKMJF failure to set aside funds (or to claim to have failed to set aside funds) for abandonment earlier. [Emphasis added]

18.10 Please confirm, or explain otherwise, that VAFFC considers Bonbright principles of utility rate setting applicable to public utilities.

18.10.1 If confirmed, to what extent do the principles apply to a public utility?

Response to BCUC IR 18.10 and 18.10.1:

Confirmed. The Bonbright principles of a sound rate design apply to public utilities, but only to a more limited extent to common carriers. For example, the Bonbright principles of price stability, understandability, and fair apportionment among customers are inherent to the concept that a common carrier provides non-discriminatory access. Similarly, pricing that encourages efficiency (including both conservation and increased use when the value so merits), feasible application, and freedom from controversies as to applicability are universally applicable pricing principles in economics.

In contrast, the Bonbright criteria such as revenue stability for the owner and the fair return standard (i.e., the opportunity to earn a return of and a return on effectively all invested capital) apply to public utilities, but are not prioritized for common carriers. There is no such priority.

For example, the PKMJF revenues escalated from approximately \$3 million in 2006 to \$6 million in 2010, and the company earned a return in 2010 that was [REDACTED] the “fair return standard” level of approximately \$0.7 million set for 2007. Yet, such negotiated

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tariffs are a valid component of the common carrier framework so long as agreed to by customers and so long as the tariffs do not prevent non-discriminatory access to the pipeline. If the Bonbright principles were applied in full, the BCUC would have had to review the negotiated outcome to ensure that it was in the public interest. This is not necessary in a common carrier framework where customers have elected to accept the tolls rather than file a complaint.

Customers have the power to negotiate such tolls, and pay amounts that yield a return for the common carrier far higher than the fair return standard would dictate, and such tolls are valid and final, but this does not mean that the BCUC cannot determine that PKMJF failed to appropriately record its costs over that period (particularly including costs to appropriate to an abandonment reserve, and to properly depreciate the assets). These examples are part of the InterGroup recommendations in this proceeding.

18.11 Please confirm, or explain otherwise, that VAFFC considers Bonbright principles of utility rate setting applicable to setting tolls for common carriers.

18.11.1 If confirmed, please explain why the principles for utility rate setting apply if, as stated in evidence by VAFFC, PKMJF is a common carrier and the principles are not codified?

18.11.1.1 To what extent do the principles (e.g. a fair rate of return on invested capital) apply to a common carrier? Please elaborate.

18.11.1.2 If the principles should apply to different extents for a public utility and a common carrier, please explain why, giving examples if possible.

18.11.2 If not confirmed, please explain why not.

18.11.3 If not confirmed, why does VAFFC raise the Bonbright principles of fairness, undue discrimination, and intergenerational equity in its submission?

Response:

For a full discussion, please see VAFFC's response to BCUC IR 18.10.

Also on page D-10 of the InterGroup Report, VAFFC states:

PKMJF contends that its proposed toll surcharge collection is not discriminatory because abandonment costs are allocated in the same manner as the JFL's annual revenue requirement based on relative volumes shipped by each shipper. However, as shown in a PKMJF information request response, the proposed abandonment surcharge represents a 62.2% increase in revenue requirements over the 2018 approved revenue requirement and a 58.2% increase over the 2019 interim toll increase.

While PKMJF does not consider 2018 to 2019 Revenue Requirements (including the abandonment surcharge) to be an apples-to-apples comparison, as it asserts no abandonment costs were included in the 2018 Revenue Requirement, I believe the comparison is valid in determining a true and fair picture of the impact of the surcharge on customers. On its face, this amounts to rate shock directly resulting from PKMJF's suggestion that it failed to pursue abandonment costs

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until now even though it was fully aware of the imminent VAFD Project.
[Emphasis added]

18.12 Is the concept of rate shock applicable to users of a common carrier's assets (e.g., shippers)? Please discuss.

18.12.1.1 If yes, please explain why this principle should apply and how it is applicable in a competitive market.

Response to BCUC IR 18.12 and 18.12.1.1:

Avoidance of rate shock is a strongly encouraged, though not universally applicable, aspect of good toll design for public utilities. This is because, sometimes, underlying costs change to a degree that avoiding rate shock is impossible without also excessively muting price signals, or failing to provide a fair return (which are themselves poor rate design outcomes). Many times, however, the drivers of rate shock in public utilities are not external factors such as increases in the price of fuel, but rather, regulatory matters such as deferral balances etc.

In this sense, the risk of rate shock for a common carrier is less likely than for a public utility. A common carrier's yearly tolls ought to better reflect underlying costs and reasonable market conditions, and not be excessively tied to a precise return of and return on capital like a public utility.

The current situation is not a scenario in which rate shock ought to occur. The pricing shock proposed by PKMJF arises solely because PKMJF has suggested it must have a fully funded abandonment reserve in 3 years, and that it has none today. This is erroneous on multiple levels, as discussed in the InterGroup evidence:

- 1) It is not credible that PKMJF ceases service in 2021, and was not credible at the time of the Application.
- 2) PKMJF's abandonment cost estimates are overstated.
- 3) Even if PKMJF did have a need for abandonment balances in 2022, those balances should be made up from a balanced and extended recovery over the full and well-managed life of the assets. The assets in this case have a remaining physical life of 25 years. The fact that they may never see that life is in part a risk that an entrepreneur (such as a common carrier) takes by building or buying the asset, and in part how PKMJF has managed its assets. PKMJF should be able to include a reasonable annual cost of abandonment in the test years represented as a reasonable total forecast abandonment cost spread over many years – not an immediate accelerated risk transfer to shippers.
- 4) It is not credible that PKMJF has no factual, or constructive, present valued obligation for the abandonment recorded as a reserve on its balance sheet as of year-end 2018. The facts today regarding bypass are not materially different than they have been for the last 10 years (when PKMJF accelerated the depreciation to the end of 2022). PKMJF's tolls for the last decade had ample room to accrue such reserves while still maintaining Returns on Equity at robust, even [REDACTED]

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levels. The presence of such reserves would mute the rate shock that needs to be considered at this time.

19.0 Reference: COST OF SERVICE
Exhibit C2-36-2, InterGroup Report, pp. 2–3; *Utilities Commission Act, Part 4*
Jurisdiction

Part 4 of the *Utilities Commission Act* (UCA) relates to the regulation of carriers, purchasers and processors. For example, section 65 (3.1) is as follows:

65 (3.1) Without limiting subsection (2) (b) or (3), the commission may establish conditions with respect to a common carrier in relation to any of the following matters:

- (a) a toll that may be charged by the common carrier;
- (b) extensions, improvements or abandonment of service.

19.1 Please discuss, in VAFFC's view, what the BCUC's jurisdiction is with regards to setting tolls for common carriers.

Response:

Please see VAFFC's response to BCUC IR 18.1.

19.2 In VAFFC's view, does the BCUC have the jurisdiction to set any conditions it considers relevant when setting tolls? Please explain why or why not.

Response:

No. The BCUC's jurisdiction to set conditions when setting tolls is confined to the purpose of its power to regulate common carriers regulation and make associated declarations.

The purpose of declaring an existing asset to be a common carrier (rather than stepping back and letting the market operate without regulatory intervention) is to ensure non-discriminatory access to an asset that exists and which, at a policy level, should have its surplus capacity open to all users on an equal basis. The purpose of declaring an existing asset a common carrier is not so the public can shoulder various new costs and risks for the entrepreneur who undertook the development on their own initiative.

As a result, the toll needs to rein in the common carrier owner from excessively exercising their market power. The toll also needs to avoid penalizing shippers by foisting upon them risks that they have no rationale to bear.

19.3 In VAFFC's view, what factors should the BCUC consider when establishing tolls? Please elaborate.

19.3.1 Does VAFFC consider that the setting of tolls should be in line with or similar to the setting of rates for public utilities under sections 59-60 of the UCA? Please

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discuss.

19.3.1.1 If yes, how similar, and what aspects?

19.3.1.2 If no, please explain why not.

19.3.2 Does VAFFC consider that the tolls set by the BCUC should not be unjust, unreasonable, unduly discriminatory, or unduly preferential? Please discuss.

19.3.3 What conditions are reasonable to establish when setting tolls in a competitive market? In your response, please discuss how the BCUC should set a toll that is a surrogate for a rate established by market participants.

Response:

Please see VAFFC's responses to BCUC IR 18.1, 18.10, and 19.2.

19.4 In VAFFC's view, does the BCUC have the jurisdiction to approve depreciation rates for common carriers? Please discuss.

Response:

Not explicitly. The BCUC can set tolls. In setting tolls, it can take into account what ought to be charged for depreciation of assets needed to provide the service.

19.4.1 In what ways, if any, does the BCUC's authority with respect to the approval of depreciation rates differ between common carriers and public utilities? Please elaborate.

Response:

Some jurisdictions' public utility legislative schemes, generally including BC, explicitly identify depreciation as a rate component to identify and manage. While this is not explicitly the case under the *Utilities Commission Act's* common carrier regime, identifying and managing the depreciation of assets assists in setting fair toll levels across asset lives. Beyond that fact, there are no constraints that require the BCUC to use or not use general depreciation rates and concepts for common carriers.

19.5 In VAFFC's view, does the BCUC have the jurisdiction to approve and allocate abandonment costs for common carriers? Please discuss.

19.5.1 In what ways, if any, does the BCUC's authority with respect to the collection of abandonment costs differ between common carriers and public utilities? Please elaborate.

Response to 19.5 and 19.5.1:

The BCUC does not explicitly have the jurisdiction to approve or allocate abandonment costs. The BCUC has the jurisdiction to set tolls to ensure that the common carrier is not undermining the basic principle of non-discriminatory access, and conditions under

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which a common carrier must accept energy resources, including abandonment of service. Tolls should be rooted in the reasonable costs to provide the service, if it were provided by a competent and efficient operator making use of assets over their existing life. Such tolls should include sufficient funds to build up an abandonment reserve over the useful life of the assets, based on reasonable abandonment cost estimates prepared in a timely way.

The BCUC does not have jurisdiction to “allocate” abandonment costs to shippers outside of a toll component as described above, and does not have jurisdiction to allocate abandonment costs to shippers retroactively based on past service.

19.6 In VAFFC’s view, does the BCUC have the jurisdiction to approve capital structure and allowed rate of return for common carriers? Please discuss.

19.6.1 In what ways, if any, does the BCUC’s authority with respect to the approval of capital structure and allowed rate of return differ between common carriers and public utilities? Please elaborate.

Response:

The BCUC has the jurisdiction to set tolls that are reasonably representative of the cost to supply the service, if supplied by a competent and efficient operator making use of assets over their existing life. Such costs would include the cost of committed capital. To determine that cost, the BCUC ought to assess a reasonable mixture of sources of capital representative of a competent and well-financed operator.

On pages 2 to 3 of the InterGroup Report, VAFFC states:

Common Carrier Principles are not Codified: As a Common Carrier (Part 4 of the Utilities Commission Act), PKMJF is under a framework with almost no specific legislative standards for tolls. The legislation is simply silent on matters such as the reasonableness of rates and the obligations of fair treatment to the shareholders. As a result, the proceeding occurs with major questions tied to the applicable regulatory (economic and legal) first principles. [Emphasis added]

19.7 In VAFFC’s view, does the absence of a prescribed set of circumstances when setting a toll for a common carrier mean that the BCUC has unfettered discretion to set the tolls based on relevant considerations? Please discuss.

Response:

No.

Please see VAFFC’s response to BCUC IR 19.2 – 19.7.

The common carrier framework is grounded in non-discriminatory access, and regulation only as necessary to achieve this policy objective. If customers can receive such access at a toll they find acceptable through negotiation, then this objective has been achieved and BCUC has no further need to set tolls. If the negotiation approach has not worked

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and parties have resorted to their rights to seek a declaration and have the BCUC set tolls, then the tolls should be representative of a competent, efficient and well-financed operator making use of assets over their existing useful life. If the common carrier in question is not an efficient operator, not able to make use of the asset over its existing life, or not able to achieve the throughput that is possible and forecast as part of a reasonable business case assumption, then such risk should lead to adverse outcomes on the part of the entrepreneur developer/operator, and should not be a risk passed off to shippers.

C. ABANDONMENT COSTS

- 20.0 Reference: ABANDONMENT COSTS
Exhibit C2-36-2, InterGroup Report, p. 7; Appendix A, A-24; Appendix D, pp. D-8, D-11
Abandonment Cost Recovery – Negotiated Settlement Period**

On page 7 of the InterGroup Report, VAFFC states:

PKMJF knew or ought to have known (according to the PKMJF scenarios) sufficient information about abandonment costs to include accruals to some form of abandonment liability or reserve starting in 2009 (as part of the negotiated settlement). Failing to record such accruals led to excessive net income being recorded during this period, and harm to customers from failing to record an appropriate funded Abandonment provision.

On page A-24 of the InterGroup Report, VAFFC states:

It is not credible that a regime was implemented which targeted known and fixed, stable revenues for years out of the remaining 13 year life of the pipeline, but failed to consider establishment of any abandonment fund. To so conclude would be to find that PKMJF deliberately accepted an omission of the chance to fund the future costs of abandonment during the last 10 of 13 years of the pipeline. Either PKMJF would have to have been supremely confident that it could, to be colloquial, assuredly wallop shippers for abandonment costs in the final 3 years, or PKMJF would have had to be intensely oblivious to this pending risk. Neither of these is credible... more likely, the settlement was acceptable to all parties, including PKMJF, because it was understood to provide PKMJF with sufficient funds to address abandonment consistent with a 13-year life adopted for depreciation...

- 20.1 Did the parties to the 2009 to 2018 negotiated settlement agree to include the collection of costs associated with abandonment of the JFL as a component of the negotiated settlement? Please elaborate.

Response:

No current VAFFC representatives or members recall the detailed discussions between shippers and PKMJF that resulted in the negotiated settlement agreement.

It is clear in 2009 that PKMJF was aware of the VAFD and aware that abandonment fund collection should commence. The parties chose to increase PKMJF's compensation and leave the settlement silent on abandonment cost collection. In

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VAFFC's view, that silence leaves the risk with the carrier, where it belongs, and consistent with the findings and rulings of the National Energy Board.

VAFFC's conclusions regarding abandonment costs are further informed by InterGroup's analysis of publicly available documents and the application of Ms. Lee's considerable professional judgment and expertise. See, for example, the following excerpt from page A-25 of InterGroup's evidence:¹⁸

In short, the only reasonable way to set forward-looking tolls today in the wake of the negotiated settlement, would be to assume PKMJF acted or was expected to act consistent with a prudent pipeline operator during that period. This would yield an abandonment reserve as of December 31, 2018 of between \$2.556 million and \$3.671 million (likely the latter). Such a reserve should be directed by the BCUC to be established (for the purposes of setting 2019-2021 tolls), effective December 31, 2018, out of PKMJF's past tolls which were instead recorded as net income to the shareholder. To be clear - these amounts should not be collected from toll-payers a second time. Revenue Requirements for 2019 and going forward should be set to reflect abandonment funding for the remainder of reasonably estimated abandonment costs over and above this level (see the complementary evidence of Patricia Lee) over the appropriate depreciation period.

[Footnotes omitted]

Please see also VAFFC's response to BCUC IR 16.4.3 and 20.7.

20.1.1 If yes, please provide any documentation in VAFFC's possession that demonstrates such an agreement was reached.

Response:

Please see VAFFC's response to BCUC IR 20.1.

20.1.2 If not, please explain why VAFFC expected PKMJF to be collecting abandonment recoveries without any formal confirmation.

Response:

Please see VAFFC's response to BCUC IR 20.1. The key point is that VAFFC opposes PKMJF collecting recoveries *now* to replace amounts it could have, but did not, account for then, when it knew that it was prudent to commence abandonment collection. PKMJF is at risk, not shippers, and was compensated for assuming risk.

20.2 Please provide any documentation VAFFC has regarding PKMJF's plans to establish an abandonment fund for the JFL during the 2009 to 2018 negotiated settlement period.

¹⁸ Exhibit C2-36-2.

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Response:

VAFFC does not have any documentation regarding PKMJF's plans to establish an abandonment fund for the JFL during the 2009 to 2018 negotiated settlement period.

- 20.3 If VAFFC cannot provide documentation respecting the collection of abandonment costs during the negotiated settlement period, please explain the basis for VAFFC's submission that it is "...likely, the settlement was acceptable to all parties, including PKMJF, because it was understood to provide PKMJF with sufficient funds to address abandonment consistent with a 13-year life adopted for depreciation."

Response:

Please see the InterGroup evidence Appendix A, section 4.3. Please also see VAFFC's response to BCUC IR 16.1, 16.4.3 and 20.1.

The recollections and views of parties to a settlement arrived at 12 years ago, where there were multiple trade offs and scant documentation in the final agreement, are of limited value in determining how the settlement proceeds and outcomes ought to be addressed.

More relevant are the inputs that are known to be operative in the time frame, with a reasonableness test applied to the outcomes. In this regard, the following points are noted:

- The settlement should be understood to reflect a package of complementary concessions. This is the basis for interest-based or trade-off-based negotiations.
- The settlement would be internally incoherent if it adopted accelerated depreciation (on the basis that end-of-life was sufficiently foreseeable) but did not contend with abandonment costs.
- The settlement reflects a period when shippers already had certainty on 2009 tolls, at approximately \$4 million per year. Yet shippers negotiated tolls to bump up (from this final level) to \$4.8 million that same year, and to almost \$6 million the following year, with further annual increases thereafter. The only documented, identifiable cost increase was accelerated depreciation, which was responsible for only \$0.236 million of this increase⁹.

On the basis of these facts, it does not seem credible that parties simply handed PKMJF almost \$2 million a year in extra tolls despite PKMJF only incurring \$0.236 million per year in extra costs.

⁹ Per Exhibit A2-1, Appendix 1 to the Negotiated Settlement, the depreciation expense for 2009, at the 20 year life projection, was \$0.544 million, and the same assets for 2010, at the 13 year life projection, was \$0.780 million. This included "normal" cost of removal and retirements.

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- 20.4 Please discuss whether it is standard industry practice for abandonment costs to be included as a component of negotiated settlements presented to the BCUC and/or the Canadian Energy Regulator.

Response:

InterGroup is not aware that there is any specified or codified standard industry practice, one way or the other.

- 20.5 Please explain the harm to customers that VAFFC states resulted from PKMJF's "...failing to record an appropriate funded Abandonment provision."

Response:

The harm that arises for customers is that they paid tolls that skyrocketed by almost \$2 million a year from the original 2009 approved value to the 2010 negotiated value, and PKMJF seeks to claim all of this added tolls as enhanced net income (well above any reasonable return that could have occurred under a litigated proceeding) rather than record this as funding for abandonment costs. The harm that arises is PKMJF now asserts that a projected massive \$11.862 million liability exists for abandonment and that nothing has been set aside to date, so the full \$11.862 must be collected from 2019-2021 shippers.

On page D-8 of the InterGroup Report, VAFFC states:

Regulators can provide the opportunity and mechanisms for recovery but it is the responsibility of the company, in this case PKMJF, to pursue the recovery when the need arises. With respect to the provision for abandonment costs, PKMJF failed its responsibility.

On page D-11 of the InterGroup Report, VAFFC states:

While the costs of abandonment are part of PKMJF's normal business operations, the fact that PKMJF has acted in an imprudent manner with respect to this issue by not seeking a dismantlement provision before now mean that it should bear the risk of dismantlement cost recovery or at least a portion thereof rather than the shippers.

- 20.6 In VAFFC's view, is there a specific point in the lifecycle of a pipeline by which a common carrier must establish an abandonment reserve fund or risk being unable to recover abandonment costs from users? Please explain.

Response:

No, there is no such specific point. First, there is no regulatory imperative that the common carrier ever establish an abandonment reserve. The common carrier concept is, at its heart, an entrepreneurial model, in which the developer and owner take on broad risks of their investment. Declining to set aside funds for abandonment is one risk the operator may elect to take on (in the absence of other oil and gas regulations that require such funding). Where tolls are litigated, the regulator ought to include provision

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for funding abandonment costs, somewhat more heavily weighted to the latter years of an asset's life (as the NEB articulated, when abandonment timing can be perceived). This is not unlike the principles behind an ARO, which is only fully recognized and the liability quantified once credible costs and plans are available.

With respect to reasonable toll-making, a natural opportunity arises to address abandonment reserves. Once an asset with a defined life is beginning to be paid down (typically the latter stages of the asset's life), there is increased financial potential to build up abandonment reserves. In these latter years, the Net Book Value will have declined, such that returns and interest costs are lower, and it is possible to prepare a more credible abandonment plan with a reasonable estimate of retirement date. Recent public utility regulatory decisions, for example, have now raised the issue that straight-line methods may not be required in principle for net salvage costs, but that regulatory principles of "used and useful" and intergenerational equity may in fact be better fulfilled by approaches that collect a larger share of net salvage in the latter years of an asset's life.

For example, see AUC Decision 20272-D01-2016 re: ATCO Electric, particularly section 8.5.

Consider also the case of the Salt Caverns facility owned by ATCO Pipelines (AP). In Alberta Utilities Commission proceeding 22011, AP owned a salt cavern storage facility which had a decommissioning study prepared for the purposes of calculating the future clean-up liability, much like the ELM study in this proceeding (though the decommissioning study in that case had other technical weaknesses which do not appear present in the ELM study in this case). AP proposed to include in its revenue requirement the beginnings of amounts needed to build up a type of reserve towards funding these costs, even though the main assets were presumed to have 23.1 years remaining life, or up to 20-40 years as a range. The AUC rejected this proposal as the decommissioning was not close or credible enough (there was no specific retirement date proposed or justified), and the plans did not consider relevant alternative such as a sale of the asset rather than a clean-up and reversion to farmland (AUC Decision 22011-D01-2017, section 9.5). The Commission did not indicate AP would never recover abandonment costs, just that the decommissioning proposal was premature. In short, abandonment costs can be recovered over a reasonable period that is not too late in the asset's life, but also must be rooted in a properly prepared proposal (re: timing, approach, costs) that could not be properly detailed too early in the asset's life

Also note that InterGroup's proposals in this proceeding are not rooted in the idea that PKMJF failed to act early enough to establish an abandonment reserve. Rather, the main contention with abandonment costs is that (a) it should be reasonably inferred that a balance ought already exist of \$3.671 million (not \$0 as asserted), (b) the total cost ought be \$8.333 million (not \$11.862 million as proposed), and (c) the recovery period for the difference ought be 25 years (the physical capability of the assets and useful life under prudent operation) not some truncated period that results in the risks of underuse being transferred to shippers rather than owners, particularly where (i) this life termination is suspect (the line may operate much longer), and (ii) if it does retire in this truncated time frame, it reflects a material inaction on the part of the owners to protect their market position – or at minimum take reasonable commercially available steps to keep their asset a going concern. After all, the JFL directly connects a refinery that must

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continue to produce jet fuel as part of standard operations to an airport that, pre-pandemic, continued to experience strong growth and fuel consumption.

20.6.1 If yes, please provide any precedent VAFFC is aware of where the collection of abandonment costs, in whole or in part, were denied by a regulator due to the pipeline owner's failure to establish an abandonment reserve sooner. Please provide any relevant supporting documents in your response.

Response:

VAFFC is not aware of any such precedent.

20.6.1.1 For each instance identified, please explain how abandonment costs were funded.

Response:

Please see VAFFC's response to BCUC IR 20.6.1.

20.7 Please provide any evidence VAFFC may have that demonstrates PKMJF failed to seek recovery of abandonment costs when 'the need arose'.

Response:

The evidence is the fact that PKMJF did not request recovery of abandonment costs either through negotiations for tolls or by way of an application to the BCUC since 2007. It is InterGroup's position that PKMJF had all opportunities to accrue reserves for abandonment costs out of the significant revenues recorded from 2009-2018. In short, it is not that PKMJF "failed to seek" recoveries that is the core of the problem – it is that PKMJF sought and received more than sufficient toll revenue, but failed to record it as should have been expected by a responsible operator, electing instead to take these amounts as excess profits notwithstanding the risk it knew it faced.

20.8 Please discuss any differences in the way abandonment costs are funded by common carriers versus public utilities.

Response:

Please see the response to BCUC IR 6.11, 6.12, 18.1, 18.2, and 18.12.

20.9 Please discuss whether pipeline users have a responsibility to budget for a portion of the costs associated with abandonment of the pipeline.

Response:

The costs of abandonment are a valid component of a pipeline's costs over its life.

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20.9.1 Please explain how VAFFC's views its obligations with respect to the eventual abandonment of the JFL.

Response:

Shippers are toll-payers. Their rights are to receive shipping services. Their obligations are to pay the duly established (by negotiation or litigation) tolls for shipping service when the service is provided. Shippers arrive, leave, change suppliers, change shipment methods, start-up, and go out of business. They gain no constructive rights of ownership of the facilities, and carry none of the risks of ownership except to the extent they elect to accept such risks as part of negotiations. Shippers record no future liability related to having bought a service in the past, and ought not be exposed to future liability. Shippers have no obligation to use the common carrier services, except to the extent they negotiate to accept such duty.

Use of a common carrier is a fundamentally transactional relationship, not an ownership stake. It is not a permanent affiance, it is purchase and sale of a quantity of service which, if conditions are favourable, may be repeated multiple times, or terminated.

Customers' obligations for eventual abandonment are solely represented by customers paying duly established tolls at the time they are in force (or indeed electing not to pay such tolls and not to use the service, if they are simply uncompetitive).

21.0

Reference: ABANDONMENT COSTS
Exhibit C2-36-2, VAFFC Direct Evidence, p. 11; InterGroup Report, p. 10;
Appendix D, p. D-10
Abandonment Cost Recovery – Intergeneration Inequity

On page 10 VAFFC's Direct Evidence, VAFFC states:

Once the VAFD becomes operational, VAFFC does not expect its members to cease all shipments of jet fuel on the Jet Fuel Line. Rather, VAFFC expects members will ship on the Jet Fuel Line opportunistically, when it makes economic sense to do so, taking into account different jet fuel source prices and overall transportation cost options.

On page 7 of the InterGroup Report, VAFFC states:

The amount of abandonment costs to be collected in the Test Years should be the total estimated cost, less the amount appropriately accrued as of 2018, divided by a reasonable estimate of the remaining potential physical life of the assets (in particular, 25 years...). [redacted text omitted]

On page D-10 of the InterGroup Report, VAFFC states:

It is patently unfair and discriminatory to begin collecting abandonment funds

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now that should have rightly began some years ago when the risk of bypass was clearly known. Intergenerational inequity would be caused by this PKMJF failure to set aside funds (or to claim to have failed to set aside funds) for abandonment earlier. [footnote omitted]

- 21.1 Please identify any changes to the composition of shippers and/or the apportionment of throughput volumes between shippers on the JFL since the JFL became operational.

Response:

The only current shipper on the Jet Fuel Line that is a member of the VAFFC consortium is Air Canada. VAFFC is unable to identify changes to the composition of shippers and/or the apportionment of throughput volumes between shippers on the Jet Fuel Line since the Jet Fuel Line became operational, without expending unreasonable effort. VAFFC notes that this information should be readily available to PKMJF, as the operator of the Jet Fuel Line since at least 1968.

However, VAFFC notes that, historically, Canadian Airlines, Air Canada, Chevron, Imperial Oil, and Parkland (the successor to Chevron) have all shipped on the Jet Fuel Line at various times.

- 21.2 Please discuss the potential for intergenerational inequity under a scenario where the costs of abandoning the JFL are recovered over a 25-year period, during which time VAFFC's members, and potentially others, ship on an opportunistic basis following completion of the VAFD project.

21.2.1 Please discuss how any potential intergenerational inequity could be mitigated.

Response to BCUC IR 21.2 and 21.2.1:

With respect to intergenerational inequity, please see the response to BCUC IR 20.6 and 20.9. The mitigation of intergeneration inequity is achieved by the InterGroup proposal as described in the final paragraph of the response to BCUC IR 20.6.

On January 6, 2020, Pembina Pipeline Corporation informed the BCUC that it had acquired the JFL from Kinder Morgan Canada (Jet Fuel) Inc.

- 21.3 Please discuss whether the concept of intergenerational inequity applies to owners, as well as users, of common carrier facilities and the basis for VAFFC's position.

Response:

Intergenerational inequity is a concept for users rather than owners. Owners are not the primary concern, as they either remain the same over time, or change but only after a price negotiation in which each party can protect themselves or walk away. In this case, both apply – the actual utility assets have been owned by the same company since their inception. The shares of that company have changed hands, but only after negotiation on values.

- 21.3.1 Please discuss whether it would be appropriate for PKMJF to bear the risk of being unable to recover abandonment costs for the JFL as a result of the actions

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of previous owners.

Response:

PKMJF is the owner of the asset and has always been the owner of the asset. The common carrier assets are owned by the same company today as since establishment (despite multiple name changes). The fact that shares changed hands is no different than for any publicly traded company – and it is not apparent that the Commission owes any duty of protection under the legislation or policy framework for common carriers to the new owners at the expense of old owners, or to old owners at the expense of new owners, or any manner in between.

It would be unfathomably distorting to this and any future market transactions if a new owner elected to purchase shares from the previous owner, and the regulator acted to protect the new owner from the previous owner at the expense of shippers by somehow transferring responsibility for all abandonment costs to the shippers. This is particularly problematic when the shippers had no say in the share transaction, received no proceeds from the sale, and made all efforts to intervene and bring to public light the previous owner's underrecovery of abandonment as part of this ongoing regulatory process.

22.0

**Reference: ABANDONMENT COSTS
Exhibit C2-36-2, InterGroup Report, Appendix D, p. D-10
Abandonment Cost Recovery – Rate Shock**

On page D-10 of the InterGroup Report, VAFFC states:

...as shown in a PKMJF information request response, the proposed abandonment surcharge represents a 62.2% increase in revenue requirements over the 2018 approved revenue requirement and a 58.2% increase over the 2019 interim toll increase. While PKMJF does not consider 2018 to 2019 Revenue Requirements (including the abandonment surcharge) to be an apples-to-apples comparison, as it asserts no abandonment costs were included in the 2018 Revenue Requirement, I believe the comparison is valid in determining a true and fair picture of the impact of the surcharge on customers. On its face, this amounts to rate shock directly resulting from PKMJF's suggestion that it failed to pursue abandonment costs until now even though it was fully aware of the imminent VAFD Project.

- 22.1 Please describe any measures that VAFFC would propose to limit the potential for rate shock to all shippers under the following scenarios: (i) PKMJF abandons the JFL following completion of the VAFD project; and (ii) PKMJF continues to operate the JFL until the assets have reached the end of their physical life, during which time VAFFC's members ship on the JFL on an opportunistic basis following completion of the VAFD project. Please explain any assumptions used in the response.

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Response:

Under either scenario, the abandonment costs should be considered to be funded to the sum of \$2.556 million as of opening 2019. The total to be collected should be set at \$8.333 million. The remaining costs to be funded therefore total \$5.777 million. The revenue requirement for 2019, 2020, and 2021 should be set to include 1/25th (i.e., based on the useful life reasonably attributed to the assets) of the outstanding amount, or \$0.231 million per year. This should be divided by the reasonably expected throughput potential of the line, as estimated by 2018 throughput of 7,436,296 bbl (per Exhibit B-11, Table 2.2, pdf page 9) or \$0.031/bbl (small further adjustments may be required to address gathering facility usage versus mainline tolls). This toll should be included in 2019, 2020 and 2021 tariffs. This same toll concept (\$0.231 million per year divided by reasonably estimated throughput) should apply to each future year that the line remains in service, unless something different is negotiated between PKMJF and shippers.

PKMJF should retain responsibility for all abandonment costs incurred, whether funded from shipper revenues or not funded (i.e., if PKMJF does not achieve the full potential life or usefulness of its investment).

This is a principled and internally consistent recommendation (i.e., it can be applied today without perfect foresight of how long the line will be in service) which does not create rate shock.

23.0

**Reference: ABANDONMENT COSTS
Exhibit C2-36-2, VAFFC Direct Evidence, p. 3, 10, 15; InterGroup Report, Appendix C, p. C-2; Appendix D, p. D-4; Exhibit B-38, VAFFC IR 15.3; Exhibit B-11, BCUC IR 11.10.1, 11.10.2; Exhibit B-13, VAFFC IR 12.6(c); Exhibit B-39, Parkland Refining (B.C.) Ltd. (Parkland) IR 12.1
Abandonment Cost Recovery – Abandonment Trusts and Asset Retirement Obligations**

On page D-4 of the InterGroup Report, VAFFC states:

While the JFL is not regulated by the NEB, PKMJF submits that the guidelines established by the NEB [National Energy Board] (now the CER) in MH-001-2012 are a reasonable basis for abandonment assumptions in the present circumstances. In addition to estimating costs, the NEB/CER framework also addresses concepts related to abandonment trusts. [footnote omitted]

In addition to regulatory approaches, there are accounting requirements to ensure investors are aware of liabilities related to asset retirements such as abandonment. These requirements are Asset Retirement Obligations (AROs) and result from a legal obligation to retire or decommission a plant asset.

VAFFC continues that “The use of an abandonment trust fund, as opposed to an ARO, is comparatively rare in Canada and the United States” and that it is VAFFC’s understanding that “...major federally regulated pipelines in Canada have abandonment funds while provincially regulated pipelines do not.”

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On page 3 of VAFFC's Direct Evidence, VAFFC states that "...the abandonment fund PKMJF proposes is novel to the BCUC, of a type rejected by the National Energy Board, and inappropriate to these circumstances."

On page C-2 of the InterGroup Report, VAFFC states that "...PKMJF's now assumed final retirement date January 1, 2022 is contradicted by... the 25-year life expectancy used in the calculation of the Asset Retirement Obligation reported in the PKMJF 2019 financial reports. [footnotes and redacted text omitted]

- 23.1 Please discuss whether, in VAFFC's opinion, the CER guidelines provide a reasonable basis for preparing estimates of the costs associated with abandonment of the JFL.
- 23.1.1 If not, please specify the alternative assumptions VAFFC would recommend and why these assumptions are more appropriate than use of the CER guidelines as proposed by PKMJF.

Response to BCUC IR 23.1 and 23.1.1:

InterGroup's evidence recommends that the abandonment cost estimates filed by PKMJF be assessed on their merits. InterGroup accepts that the CER has provided guidelines which were relied upon by PKMJF (and ELM) in preparation of their cost estimates. InterGroup has accepted the ELM cost estimates, with limited exceptions, as reasonable given it is the best information available. The exceptions relate to assumptions regarding (i) the removal percentage in Richmond, and (ii) the calculation of post abandonment activities, for which it appears ELM inadvertently applied to the entire pipeline, and not solely those portions that would be abandoned in place. This is further described in the InterGroup Appendix D pages D-13 to D-15.

- 23.2 Please elaborate on VAFFC's statement that PKMJF's proposed abandonment fund is "of a type rejected by the National Energy Board", including identification of the specific instance(s) where the CER rejected a similar proposal and the basis for such rejections.

Response:

The "type" referred to and rejected by the National Energy Board is an abandonment fund with a true-up mechanism. The NEB firmly rejected true-ups in its Reasons for Decision RH-2-2008 on the basis that pipeline owners properly hold the responsibility of identifying when to apply to the NEB to commence collecting funds, managing the adequacy of trust balances, and remaining ultimately accountable for the cost of abandonment. There are no additional specific instances where the NEB or CER rejected true-up structures because the NEB firmly rejected the concept in principle at the outset of establishing abandonment funds. VAFFC is likewise unaware of any CER-regulated pipeline that has applied to commence collecting funds from shippers for abandonment trust purposes only a year or two away from the projected disbursement of such funds.

- 23.3 Please provide a detailed explanation as to why VAFFC considers PKMJF's proposed implementation of an abandonment trust to be "inappropriate to these circumstances".

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Response:

Please see VAFFC's response to BCUC IR 23.2 concerning the unacceptability of an abandonment trust with a true-up structure. Further, as there is very little time between the proposed start of collecting funds and beginning to spend funds, the administrative cost and burden of an abandonment trust cannot be mitigated over a long collection period. A serious application to the BCUC to establish and rely on an abandonment trust to fund the costs of abandonment would have described the intended collection and dispersal of funds with a reasonable level of detail, including investment guidelines and timelines.

On page 15 of VAFFC's Direct Evidence, VAFFC states, "Carriers are entitled to forecast and collect funds in anticipation of abandonment costs, but the obligation to do so in a timely and accurate way lies with the carrier."

On page 10 of VAFFC's Direct Evidence, VAFFC states:

The VAFD Project received its conditional EAC [Environmental Assessment Certificate] on December 11, 2013, and the EAO determined that the VAFD Project had been substantially started on September 18, 2018. PKMJF sought accelerated depreciation and abandonment costs on June 7, 2019.

In response to VAFFC IR 15.3, PKMJF states, "Prior owners of the JFL operated under US GAAP accounting rules which did not require asset retirement obligations (ARO) to be recorded for this asset."

In response to BCUC IRs 11.10.1 and 11.10.2, PKMJF states, "An ARO liability is reported when a reasonable estimate of the fair value of the legal obligation can be made", and "While it is premature to report an ARO for accounting purposes, it is not premature to implement KMJF's proposed abandonment surcharge for ratemaking purposes."

In response to VAFFC IR 12.6 (c), PKMJF states, "KMJF is not aware of any issues raised by KMJF auditors since 2009 regarding recognition of any Asset Retirement Obligation."

In response to Parkland IR 12.1, PKMJF confirms that it recognizes as ARO in its accounting records for the current and most recent fiscal year.

23.4 Please discuss the practical differences between the use of an ARO and an abandonment trust and whether the two concepts are mutually exclusive.

Response:

The two concepts are not mutually exclusive, but serve different purposes and are based on separate concepts. The most notable distinction is the legal status of a trust, as opposed to simpler ARO balance sheet liability (which may be unfunded). Indeed the purpose of an ARO is for financial reporting, to clarify and quantify future obligations that the entity will face – to the extent there is a formal trust that will fund future costs, then the entity will not face financial exposure or liability for those same costs.

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The NEB's Land Matters Consultation Initiative Stream 3 considered this issue in detail. Major Canadian pipelines disagreed on whether AROs or trusts were preferable. Trusts were proposed as more tax efficient and hence cheaper for customers, as well as avoiding unfunded liabilities. Trusts were opposed as being more administratively complex. The NEB opted for the trust vehicle, in part because of the long timelines available that would allow trust mechanics and administration and costs and contribution estimates to be refined and made efficient over time.

23.4.1 Please explain whether, on a forward-looking basis, the use of an ARO by PKMJF for the JFL is (i) reasonable and appropriate, and (ii) preferable to an abandonment trust.

Response:

Again, an ARO and abandonment trust are not mutually exclusive. The use of an ARO for financial statement purposes is a question of accounting standards. None of the InterGroup witnesses is an accountant. For the purposes of toll-setting, tolls should take into account the estimated costs related to future removal. The chief concern with an abandonment trust in this case is timing – if PKMJF's claim of imminent retirement is accepted – for the reasons discussed in the response to BCUC IR 23.4.

23.5 Please describe the specific circumstances, if any, under which US GAAP requires an ARO be established.

Response:

Please see VAFFC's response to BCUC IR 23.4.1.

23.5.1 Please explain how any US GAAP requirements regarding establishment of an ARO are applicable to PKMJF and the JFL.

Response:

Please see VAFFC's response to BCUC IR 23.4.1.

23.5.2 Please discuss whether it would be appropriate for PKMJF to start collecting abandonment funds absent establishment of an ARO. Please provide cites to any relevant precedent.

Response:

Please see VAFFC's response to BCUC IR 23.4.1.

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23.6 In VAFFC's view, when is an entity obligated to establish an ARO? Please explain.

Response:

Please see VAFFC's response to BCUC IR 23.4.1.

23.7 Please discuss what year VAFFC would have expected PKMJF to establish an ARO.

Response:

Please see VAFFC's response to BCUC IR 23.4.1. For the purposes of appropriate recognition of abandonment costs in regulatory tolls, please see the InterGroup evidence, Appendix A, section 4.3. Specifically, PKMJF had sufficient information as of 2009 to accelerate depreciation and hence begin recording some form of provision for abandonment, and sufficient information as of 2013 to increase the estimate.

23.7.1 Given the EAO determined that the VAFD Project had been substantially started on September 18, 2018, is it reasonable to assume that PKMJF could have reliably estimated the fair value of the abandonment costs and recognized the ARO after this date? Please discuss.

Response:

No. There was more than sufficient information **before** this date to begin recognition, including evidence that accelerated depreciation was sought (and received) as part of the 2009 settlement.

23.7.1.1 In VAFFC's view could the ARO have been established prior to September 18, 2018. If so, on what basis would it have been established.

Response:

Please see VAFFC's response to BCUC IR 23.7.

23.7.2 Please discuss, from VAFFC's perspective, how the threshold for recognizing an ARO is determined (e.g., nominal value, probability etc.).

Response:

Please see VAFFC's response to BCUC IR 23.7.

23.8 Considering the financial statements of PKMJF and its predecessor have been audited annually by an independent third party, please discuss why PKMJF's financial statements did not sufficiently meet the accounting test to record an ARO for financial accounting purposes if there was sufficient evidence to support the VAFD project was proceeding and full recovery of the JFL was to be completed by 2022.

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Response:

Please see VAFFC's response to BCUC IR 23.7. This outcome would be puzzling if the purpose of PKMJF's financial statements was to disclose material facts about the financial condition of the company. However, this appears consistent with PKMJF's practice with regard to opacity of disclosure, including when it indicated [REDACTED]

24.0

**Reference: ABANDONMENT COSTS
Exhibit C2-36-2, InterGroup Report, Appendix D, pp. D-13, D-14
Abandonment Cost Estimates – Pipeline Removal vs Abandonment in Place**

On page D-13 of the InterGroup Report, VAFFC states, "ELM consulted the City of Richmond, the City of Burnaby, and the BCOGC [BC Oil and Gas Commission] concerning the abandonment of the JFL via email," and that ELM assumes abandonment in place "unless there is a compelling reason to remove a segment of the pipeline."

VAFFC continues that in response to ELM's inquiry, "The City of Richmond indicated its expectation for the pipeline to be removed as part of the abandonment process but no compelling reason was given for that expectation."

Also on page D-13, VAFFC states:

While any BCOGC Order regarding removal may govern, the fact is that no plan has been submitted to the BCOGC and may not be for a significant while, depending on when exactly the JFL ceases operations. Moreover, the plan submitted to the BCOGC must include rationale for removal rather than abandonment in place. There is no reasonable rationale at this point to assume total removal is appropriate.

24.1 Please discuss the level of justification VAFFC considers necessary before it is reasonable for pipeline abandonment cost estimates to assume pipeline removal as opposed to abandonment in place.

Response:

Pipeline removal is costly and typically unnecessary for environmental or socio-economic reasons, except in limited circumstances. In fact, pipeline removal can be more disruptive than appropriate stabilization-in-place alternatives. Despite this, many parties who are not well versed in pipeline abandonment may start with an implicit

¹⁹ Exhibit B-48, Appendix A, pdf p. 32, Q. 148.

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assumption that removal is necessary or the default practice.

It should therefore be assumed that stabilization-in-place will be the practice for the majority of the line, until it is demonstrated that detailed and well-informed consultation has occurred, and appropriate proposals and assessments have been filed and reviewed with the relevant governing bodies. The PKMJF information filed in this proceeding does not meet this threshold.

- 24.2 Please discuss whether PKMJF's relationship with and obligation(s) to the municipalities along the JFL route differs in any way from that of a public utility.

Response:

VAFFC is not aware of a material difference in the relationship between a common carrier and a municipality and a public utility and a municipality.

- 24.3 Please describe the BCOGC's jurisdiction over whether the JFL will be removed or abandoned in place. Please include cites to any relevant legislation and/or regulations empowering the BCOGC in this respect.

Response:

Pipeline abandonment is an oil and gas activity regulated under the *Oil and Gas Activities Act* and the *Pipeline Regulation*, as well as the *Environmental Protection and Management Regulation*. Section 3 of the *Pipeline Regulation* prescribes adherence to the latest version of CSA Z662, including for abandonment purposes. Section 10.16 of CSA Z662 describes the general considerations that pipeline applicants must take into account in a documented pipeline abandonment plan, including landowner consultation, risks, environmental effects, and overall impacts of the proposed final configuration.

Application must be made to the OGC to abandon a pipeline. The application must include the abandonment plan, including the extent to which the pipeline will be removed and document engagement with affected landowners (public or private). To the extent there is a dispute with the abandonment plan, the OGC will adjudicate it.

- 24.3.1 In VAFFC's opinion, what factors does the BCOGC consider when reviewing pipeline abandonment plans and proposals to remove sections of pipeline, rather than to abandon the asset in place? Please highlight what role, if any, the preference of the host municipality plays in the BCOGC's decisions.

Response:

VAFFC is not aware of BCOGC decisions that have adjudicated the proportion of pipeline to abandon in place based on municipal preferences. VAFFC understands that the BCOGC considers the overall cost, disruption, environmental effects, and public consultation outcomes when it comes to removal. In some cases, full removal causes more disruption and risk than abandonment in place, and in some cases (locations) the opposite is true.

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24.3.2 Please describe any instances VAFFC is aware of where the BCOGC reviewed a pipeline abandonment plan that was not supported by the host municipality. How, and on what basis, did the BCOGC decide in these instances?

Response:

VAFFC is not aware of BCOGC decisions that have adjudicated pipeline abandonment plans opposed by municipalities.

24.4 Please describe the BCUC's jurisdiction respecting abandonment of the JFL.

Response:

The BCUC has jurisdiction to impose conditions on a common carrier in respect of pipeline abandonment and the common carrier must seek leave of the BCUC to discontinue service for abandonment.

24.4.1 Please explain in what ways, if any, the BCUC's jurisdiction respecting abandonment of the JFL overlaps with that of the BCOGC.

Response:

VAFFC understands that the broader contours of this question are presently before the BC Court of Appeal. With respect, it is not relevant to the present issue of whether and, if so, to what extent, the ELM cost estimates should form the basis for establishing an abandonment fund or equivalent.

24.4.2 Please discuss how any overlap in jurisdiction between the BCUC and the BCOGC respecting abandonment of the JFL might impact the decision as to whether sections of pipeline are removed or abandoned in place.

Response:

The OGC will require a serious pipeline abandonment plan from PKMJF at some point in the JFL's life and, presumably, the same plan would be put before the BCUC to help identify or refine a reasonable cost of abandonment estimate for tolling or abandonment fund or equivalent purposes.

On page D-14 of the InterGroup Report, VAFFC states:

There was no successful contact with the City of Burnaby so ELM assumed 20% removal and 80% abandonment in place to give some recognition for possible future development in industrial and commercially zoned areas. ELM was also instructed by PKMJF to assume municipal preferences received the full effect in the cost estimates. Given there was no compelling reason for the City of Richmond's expectation for total removal, I suggest assuming 20% removal and 80% abandonment at this time. This is in line with PKMJF's expectations that some removal may be reasonable due to the amount of recent redevelopment.

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24.5 Please provide a detailed explanation as to why an assumption of 20 percent removal and 80 percent abandonment in place is appropriate for estimating abandonment costs for the JFL in the City of Richmond.

24.5.1 If the 20 percent removal and 80 percent abandonment in place assumption is based on PKMJF's assumptions for the City of Burnaby, please compare the existing land uses along the JFL route in the two cities and explain why it is reasonable to expect similar levels of future development along the pipeline route in both cities.

Response to BCUC IR 24.5 and 24.5.1:

There is extremely limited and poor information on the record on PKMJF's abandonment plans, given PKMJF's assertion that the line will end service at the end of 2021, which is exceptionally soon for this type of planning. As a result, the only option is to work with coarse estimates. ELM indicates that "It is assumed that landowners, municipalities, and regulators will allow for pipeline abandonment in place unless there is a compelling reason to remove a segment of the pipeline" (ELM Report page 7, in Exhibit B-10). Note that the ELM report concludes that 5.25 km of the Richmond pipe is in agricultural setting (40% of the Richmond portion) with the remaining 60% urban, but that the Burnaby portion is 100% urban (ELM Report page 9, in Exhibit B-10). Based on this factual difference, there is no logic to the removal for Richmond being 100%, while the removal for Burnaby being 20%. If anything, InterGroup's evidence is conservative by replicating the 80:20 ratio for Burnaby to Richmond - a more fulsome implementation of consistency would only assume 20% of Richmond's urban portion was removed, and 0% of the agricultural - for a total removed of only 12% overall.

Also see VAFFC IR2 6.1(Exhibit B-38) and BCUC IR3 5.5.

25.0

**Reference: ABANDONMENT COSTS
Exhibit C2-36-2, InterGroup Report, Appendix D, p. D-15
Abandonment Cost Estimates**

On page D-15 of the InterGroup Report, VAFFC states that "The minimum total adjustment to ELM's abandonment cost estimate is therefore a decrease of \$3,528,363 from \$11,861,577 to \$8,333,214 as shown in the table below. There may be other concerns from an engineering perspective."

25.1 Please describe the type(s) of engineering concerns related to ELM's abandonment cost estimate VAFFC considers possible or probable.

Response:

VAFFC is not able to commission an engineering assessment of ELM's abandonment cost estimate for the purpose of responding to this information request response, and is therefore unable to provide specific examples of engineering concerns arising from

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ELM's report.

Ms. Lee assessed ELM's abandonment cost estimate on the basis of her expertise with respect to depreciation and abandonment, and provided specific recommendations arising from this assessment (see pages D-3 and D-14 of the InterGroup Report).

Ms. Lee also noted that, in general, ELM's abandonment cost estimate is "more in line with what would be expected for a retirement/abandonment more than 10 years out" (page D-12 of the InterGroup Report), and that "significant concerns arise about the quality of the report, and its underlying assumptions and data inputs given the scale of toll impact that arises" (page D-3 of the InterGroup Report).

Based on VAFFC's review of the ELM abandonment cost estimate, the following examples illustrate some of the concerns arising with respect to the quality of ELM's report, and its consistent tendency to err on the side of more expensive options:

- a) It is evident that the Calgary-based ELM staff are not familiar with the Lower Mainland generally, as illustrated by ELM's observation that "the Fraser River will likely not freeze for extended periods";²⁰
- b) ELM assumed 100% removal for the portion of the JFL within the City of Richmond based on one email from the City of Richmond;²¹
- c) ELM has no documentation or calculations to support many of its assumptions;²²
- d) ELM's post-abandonment monitoring cost estimates are calculated based on the entire length of the JFL being abandoned in place. PKMJF confirmed that this calculation conflicts with ELM's pipeline removal cost estimates, which are calculated based on the removal of approximately 13.2 km of pipeline in the City of Richmond and approximately 5.0 km of pipeline in the City of Burnaby, respectively;²³
- e) ELM incorrectly represented that it prepared a site-specific decommissioning cost estimate for the infrastructure at the Shell Burmount Terminal.²⁴ In fact, ELM selected the high range of the Base Case values;²⁵ and
- f) ELM developed a ground up cost estimate for the removal of 6 block valve sites, despite ELM only inspecting 5 block valve sites because ELM ran out of time before returning to Alberta. ELM determined that there would be no material difference in the estimates for these sites based only on statements from Kinder Morgan representatives.²⁶

²⁰ Exhibit B-10, Final Site-specific Abandonment Cost Estimate Report at pdf p. 16.

²¹ As stated by PKMJF, "[t]he assumed removal of parts of the JFL within the City of Richmond [was] driven by the communication from the City of Richmond": Exhibit B-37, PKMJF Response to BCUC IR 5.12 at pdf p. 34.

²² See, for example, Exhibit B-38, PKMJF Response to VAFFC IR 7.5(a) at pdf p. 40.

²³ Exhibit B-38, PKMJF Response to VAFFC IRs 4.1-4.4 at pdf pp. 23-24.

²⁴ Exhibit B-10, Final Site-specific Abandonment Cost Estimate Report at pdf p. 15.

²⁵ Exhibit B-38, PKMJF Response to VAFFC IR 7.1 at pdf p. 39.

²⁶ Exhibit B-38, PKMJF Response to VAFFC IR 7.3 at pdf p. 40.

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25.1.1 Please explain the impact (e.g., an increase or a decrease) to PKMJF's estimated cost of abandonment that would result from realization of any of the above engineering concerns. Please provide any relevant assumptions and calculations in your response.

Response:

VAFFC is unable to provide a specific analysis of the estimated cost impact.

Please see VAFFC's response to BCUC IR 25.1.

26.0

Reference: ABANDONMENT COSTS
Exhibit C2-36-2, InterGroup Report, Appendix D, pp. D-10, D-11, D-12;
Exhibit B-14, pp. 26–27
Abandonment Cost Estimates – Estimate Uncertainty

On pages D-11 to D-12 of the InterGroup Report, VAFFC states:

The unit cost estimates contained in the Final Abandonment Report generally appear to be within industry standards. Cost activities are reasonable for abandonment that is expected sometime in the distant future. They are not reasonable however if abandonment is really expected to take place in three years, which is PKMJF's position. The detail in the Final Abandonment Report is not what would be expected for a planned near-term abandonment.

On page D-10 of the InterGroup Report, VAFFC states:

...if PKMJF had sought an abandonment provision to begin prior to 2013 when there was a high degree of certainty of the VAFD Project, tolls would have had a longer period, up to a full 13 years, to provide for estimated abandonment costs. In such a case, either the abandonment costs could have been a new accrual that simply reduced PKMJF's net income it otherwise recorded, or it could potentially become part of the revenue requirement in a new negotiated settlement, if one was needed.

VAFFC continues, "It is patently unfair and discriminatory to begin collecting abandonment funds now that should have rightly began some years ago when the risk of bypass was clearly known."

On pages 26 to 27 of Exhibit B-14, PKMJF's Amended Revenue Requirement and Final Tolls Application for 2019-2021, PKMJF states:

KMJF proposes that, following the completion of the physical decommissioning and abandonment of the Jet Fuel Line, the relevant party will refund any surplus to shippers or bill shippers for any shortfall based on the difference between the estimated abandonment costs collected and the actual cost incurred for abandonment, which will become known at that time. KMJF proposes that the true-up amount be refunded to or collected from shippers based on volumes shipped during the total period during which the abandonment cost surcharge was collected (the "**Abandonment Cost Estimate True-up Mechanism**"). [footnote omitted]

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26.1 In VAFFC's opinion, how should the risk of variances between estimated and actual abandonment costs for the JFL be allocated between PKMJF and shippers?

Response:

The risks should reside wherever the parties negotiate them to reside. The ideal situation is that PKMJF and shippers reach an agreement which specifies these terms. Absent this, please see the response to BCUC IR 20.9.1 – that is, shippers are users of the pipeline, they are not owners and should not be exposed to liabilities beyond paying a price to receive a service. There is no reason to shift a risk that resides with an entrepreneur in any other commercial venture to past shippers of record, just because that the underlying asset is declared to be a common carrier.

Further, as noted in paragraph 60 of VAFFC's evidence,²⁷ the NEB has already considered these issues, and determined that:

- a) "Pipeline companies are ultimately responsible for the full costs of constructing, operating and abandoning their pipelines, and the Board will hold the regulated company responsible for these costs";²⁸ and
- b) "Companies are accountable for their own performance and are expected to identify and manage risk throughout a facility's lifecycle".²⁹

VAFFC submits that the BCUC should follow the precedent established by the NEB in its Reasons for Decision RH-2-2008, which resulted from a large regulatory proceeding with broad, compelled participation by industry members.

Indeed, PKMJF agrees that the guidelines set out in the NEB Decision & Reasons MH-001-2012 (which followed from a direction in Reasons for Decision RH-2-2008) are "a reasonable basis for abandonment assumptions in the present circumstances and in the absence of abandonment guidelines in the jurisdiction in which the JFL is located".³⁰

26.1.1 Assuming PKMJF was allowed to recover its estimated costs of abandonment, please explain the treatment VAFFC would propose if: (i) actual abandonment costs were greater than estimated, such that PKMJF had not fully recovered all abandonment costs from shippers; and (ii) actual abandonment costs were less than estimated, such that PKMJF had over collected abandonment costs from shippers.

Response:

VAFFC would propose that the NEB's approach from RH-2-2008 be employed: (i) if actual abandonment costs were greater than estimated, such that PKMJF had not fully recovered all abandonment costs from shippers, PKMJF should be

²⁷ Exhibit C2-36-2, pdf p. 16.

²⁸ NEB Reasons for Decision RH-2-2008 at p. 32.

²⁹ NEB Reasons for Decision RH-2-2008 at p. 34.

³⁰ Exhibit B-37, PKMJF Response to BCUC IR 3.1.2, pdf pp. 16-17.

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responsible for any difference in costs, and (ii) if actual abandonment costs were less than estimated, such that PKMJF had over collected abandonment costs from shippers, then PKMJF should apply to the BCUC for direction. The NEB considered made no findings concerning surpluses, other than that sufficient lead time and regular trust fund management reviews should ensure surpluses are minimized.

Again, PKMJF bears the risk associated with the abandonment obligations for the Jet Fuel Line, for which it is compensated through the profit it earns (return).

26.1.1.1 If VAFFC's proposed treatment differs from that of PKMJF's, please explain any differences and why VAFFC believes its proposal to be preferable

Response:

Please see VAFFC's response to BCUC IR 26.1 and 26.1.1.

See also paragraph 43 of VAFFC's evidence:³¹

PKMJF also seeks a new dedicated abandonment fund, to be implemented in what PKMJF claims as the last year of service for the Jet Fuel Line. The request is unprecedented. The abandonment funds administered by the CER are intended to be collected over decades. As described later, PKMJF also seeks an unprecedented "true-up proposal" under which shippers will be either refunded any surplus amounts collected by PKMJF or billed for any shortfall. However, none of the CER-administered funds provide pipelines the ability to trueup any fund shortfall by invoicing the last shippers remaining. When faced with that proposition, the NEB rejected it wholesale.[footnote] The BCUC should do likewise.

Footnote: NEB Reasons for Decision RH-2-2008 at p. 32: "Pipeline companies are ultimately responsible for the full costs of constructing, operating and abandoning their pipelines, and the Board will hold the regulated company responsible for these costs".

26.2 Please discuss whether the regulatory treatment of abandonment cost estimate risk between the asset owners and users differs between common carriers and public utilities, and if so, why. Please provide cites to any regulatory precedent relied upon in the response.

Response:

Yes – please see the response to BCUC IR 20.9.1 and the principles set out in BCUC IR

³¹ Exhibit C2-36-2.

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VAFFC Response To BCUC (Public)
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6.11, 6.12 and 18.1.

- 26.3 Please describe the specific refinements to the cost estimates provided in the Final Abandonment Report that VAFFC considers to be necessary before the estimates would be reasonable to support near-term abandonment of the JFL.

Response:

It is not clear what is meant by the estimates and plans being “reasonable to support near-term abandonment of the JFL”. Abandonment of the line is like a very large capital project – it requires an immense amount of detail and planning, engineering and geotechnical information, securing permits, issuing tenders, securing any needed financing, coordination with multiple parties including municipalities, contracting for transportation, demolition, disposal, etc. The detail missing from the filing, which would be needed to initiate abandonment, is staggering. This is a >\$10 million undertaking according to ELM, through an urban area, with two municipalities, covering a likely period of years. It is not possible in the IR response process to provide a fulsome description of all of the information needed to undertake this description.

As to the information that is needed to support collection from customers, please see the response to BCUC IR 26.5.

- 26.4 Please discuss the level of cost estimate certainty VAFFC considers would have been necessary for PKMJF to have started collecting abandonment funds from shippers during the 2009 to 2018 negotiate settlement period.

Response:

As noted in the response to BCUC IR 20.3, the most reasonable interpretation of the 2009-2018 settlement agreement is that it did provide sufficient revenue that “abandonment funds” were “collected”.

- 26.5 Please explain whether, absent further refinements, VAFFC considers the level of precision presented in the Final Abandonment Report to provide a sufficient basis for initiating the collection of abandonment funds from shippers.

Response:

Yes. InterGroup considers the cost estimates presented in the Final Abandonment Report (as adjusted per the InterGroup recommendations) a sufficient basis to permit collection of abandonment funds. One issue, however, is with the period of time estimated until abandonment.

- 26.6 In VAFFC’s opinion, would abandonment cost estimates with a comparable or greater level of uncertainty to those presented in the Final Abandonment Study have provided a sufficient basis for initiating the collection of abandonment funds from shippers in 2013? Please explain why or why not.

Response:

Please see the response to BCUC IR 26.5.

PUBLIC (REDACTED) VERSION
VAFFC Response To BCUC (Public)
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- 26.7 If VAFFC considers the abandonment cost estimates presented in the Final Abandonment Study to be sufficient for PKMJF to have begun collecting abandonment funds from shippers in 2013, but insufficient for such use today, please explain the reason(s) for VAFFC's position.

Response:

Please see the response to BCUC IR 26.5 and 26.3. The issue is not that the cost estimates are insufficient, rather, it is the period of time estimated until abandonment. Certainly, if the fund was initiated earlier, the costs could have been refined over time, including identifying cost savings techniques in removal.



Shipper Meeting
December 2, 2008

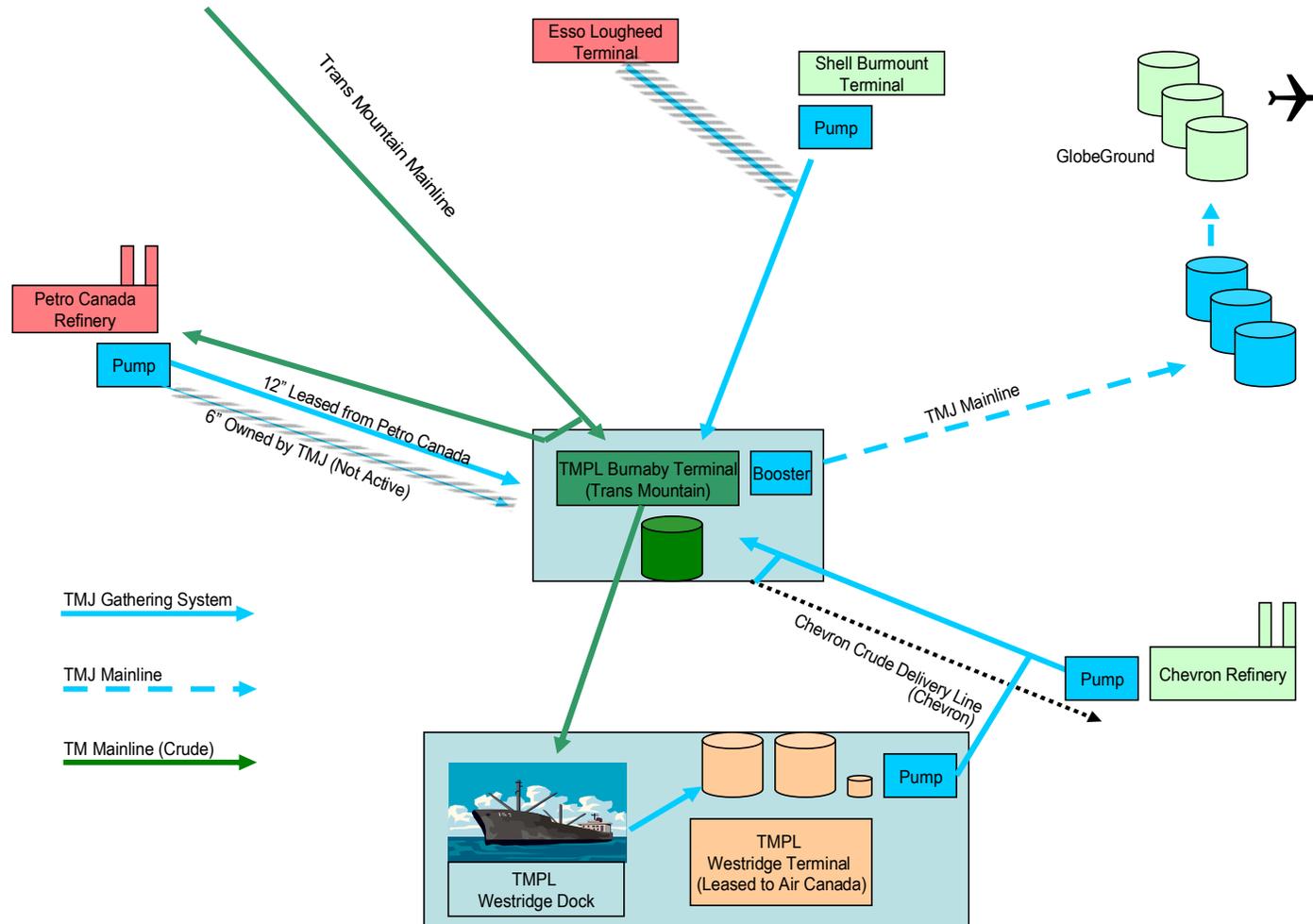
Agenda



➤ Meeting Objective

- Review System, Performance, Metrics
- Operations Review
- 2009 Tolls Overview
- Future Expectations

System Schematic

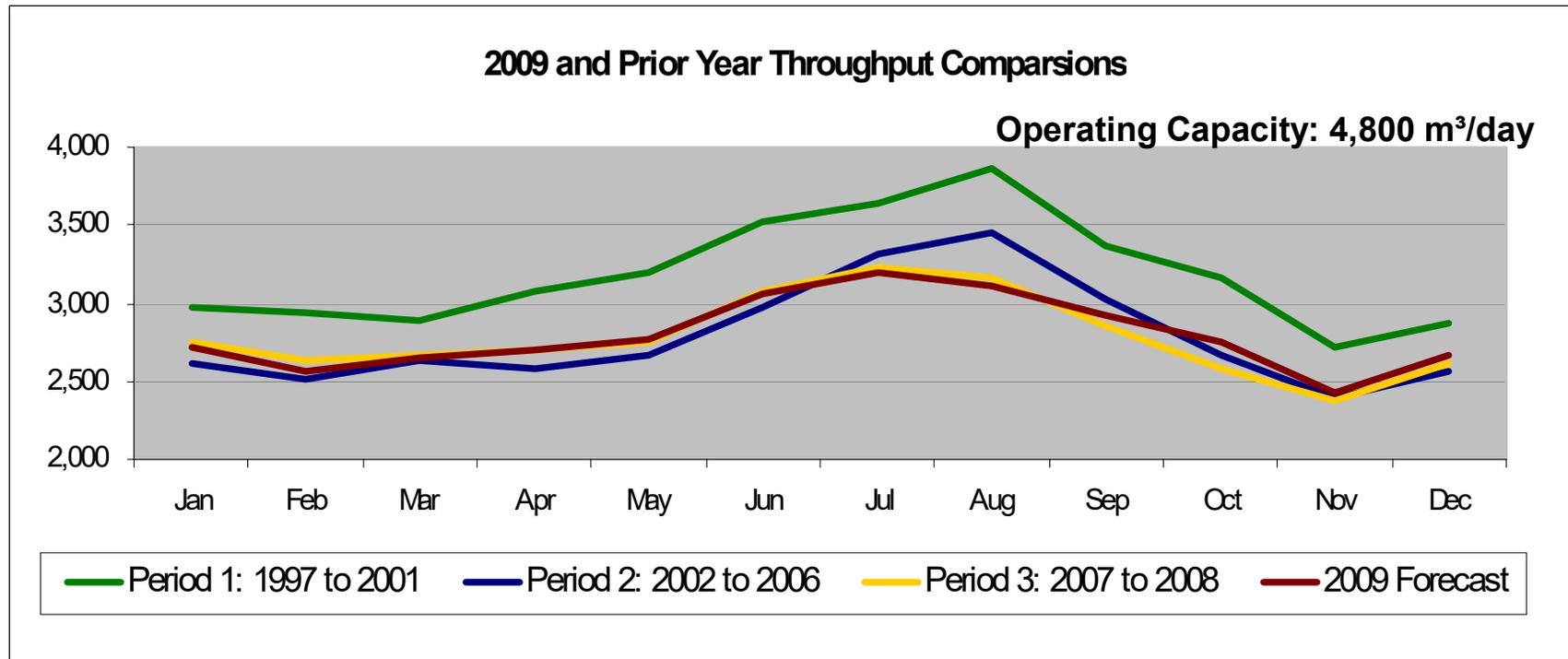


System Configuration/Metrics



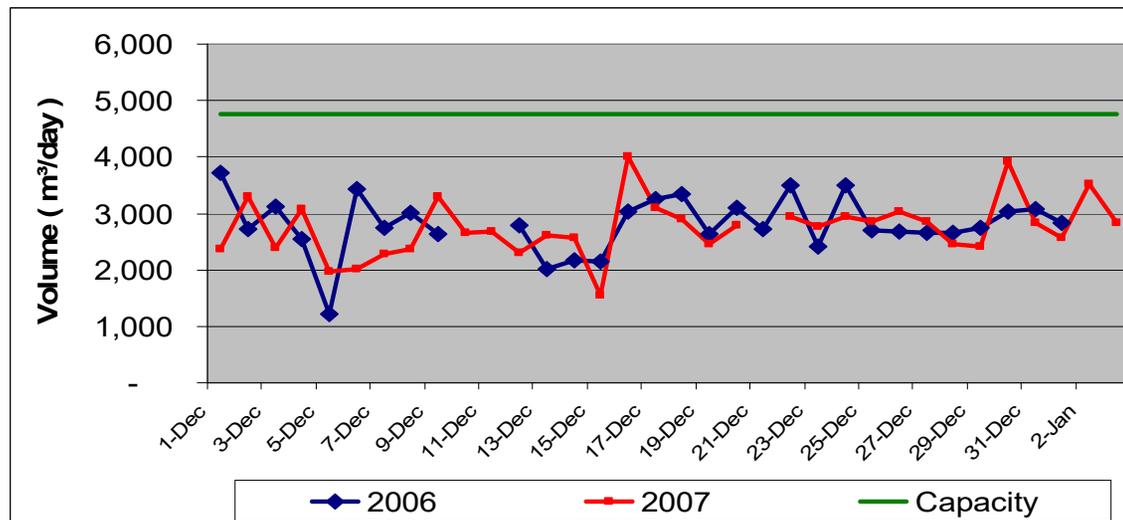
	2008/2009	2000
Connected terminals & pumping facilities:		
- Active (#) / Inactive (#)	3 / 1	5 / 0
Intermediate pump stations (#)	1	1
Length of pipeline (km)	41.3	41.3
Tanks at Vancouver International Airport (#)	5	5
- Tanks total working capacity (m ³)	6,180	6,180
Shippers:		
- # with Volumes > 20K m ³ / year	2	5
- # with Volumes < 20K m ³ / year	1	1
System Capacity (m ³ /day)	4,800	4,800
Total System Volumes (m ³ /day)	2,776	3,152
- Volume reduction since 2000	14%	

Overview of Monthly Volumes



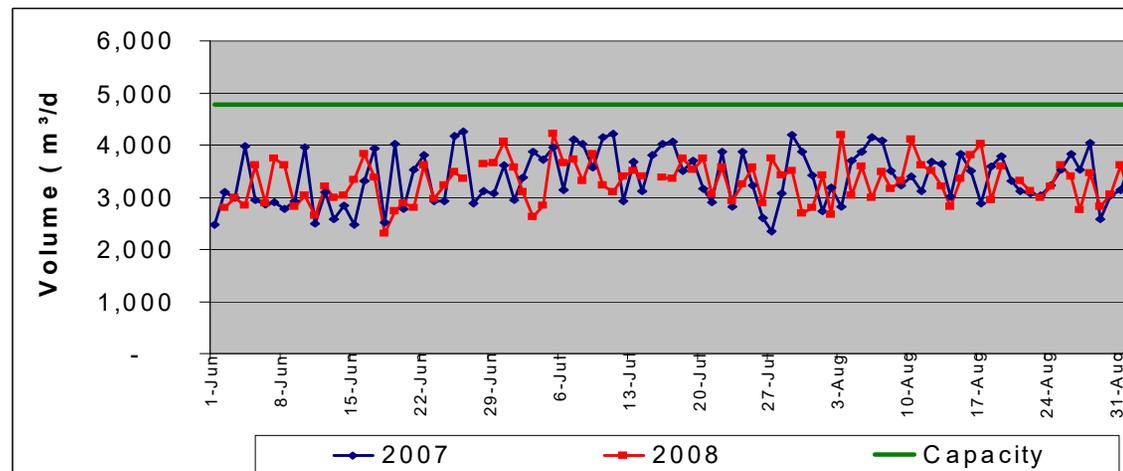
Data Table	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Annual
Period 1: 1997 to 2001	2,980	2,944	2,883	3,075	3,197	3,517	3,640	3,858	3,365	3,164	2,718	2,870	3,184
Period 2: 2002 to 2006	2,610	2,505	2,631	2,582	2,668	2,971	3,308	3,458	3,034	2,667	2,385	2,557	2,781
Period 3: 2007 to 2008	2,723	2,604	2,633	2,675	2,720	3,047	3,186	3,119	2,809	2,547	2,357	2,589	2,751
2009 Forecast	2,662	2,531	2,575	2,656	2,719	2,996	3,112	3,047	2,847	2,692	2,375	2,613	2,737
2009 to Period 3	-2.2%	-2.8%	-2.2%	-0.7%	0.0%	-1.6%	-2.3%	-2.3%	1.3%	5.7%	0.8%	0.9%	-0.5%

Peak Month Throughput



Volumes for Dec.
2006 & 2007

**1 day in 2007 that
reached 4,000 m³/day**



Volumes for June
through Aug. 2007 &
2008

**13 days (2007) that
>4,000 m³/day & only
5 in 2008**

2008 Throughput



	March Forecast	October Prediction	% Change
Volumes:			
- Mainline	2,860	2,767	-3.3%
- Gathering System	37	27	-27.0%
Total	2,897	2,794	-3.6%
Revenues ^[1]	3,423	3,307	-3.4%
ROE	8.71%	7.53%	-13.5%

Note: [1] In previous years, TMJ has recovered this level of shortfall by applying a surcharge on the subsequent year's volumes.

System Performance/Metrics



- **Mainline Volumes have steadily declined since 1997**
 - ❑ Average volume in 1997 was 3,264 m³/day declining down to 2,767 m³/day in 2008
- **Number of larger shippers has declined from 5 to 2 (monthly volume > 1,700 m³)**
- **Current economic environment suggests there will be lower pipeline utilization than previously experienced or predicted**
- **This suggests that TMJ will then face**
 - ❑ Lower than desired utilization (on average < 60% of capacity)
 - ❑ Higher than desired tolls (increase > 20%)
 - ❑ Increased risk of switching to alternate transport modes

Operations Review



- Pipeline Protection programs
- 2007 Internal Line Inspection
- 2009 Cathodic Protection
- Major Capital and Operating Programs
- Quality Assurance

Pipeline Protection



➤ **TMJ operates in the lower mainland**

- ❑ This is a high risk and high consequence corridor with increasing incidence of encroachments and unauthorized ground disturbances

➤ **In 2007/2008 KMC transformed its pipeline protection model to create focused units whose sole responsibility is pipeline protection. This recognized that:**

- ❑ Pipeline Protection is a “hot” topic with regulators who require all companies demonstrate their ability to protect their asset appropriately.
- ❑ With increasing development in proximity to the pipeline, the level of required support, pipeline protection and surveillance is increasing.

Pipeline Protection Program

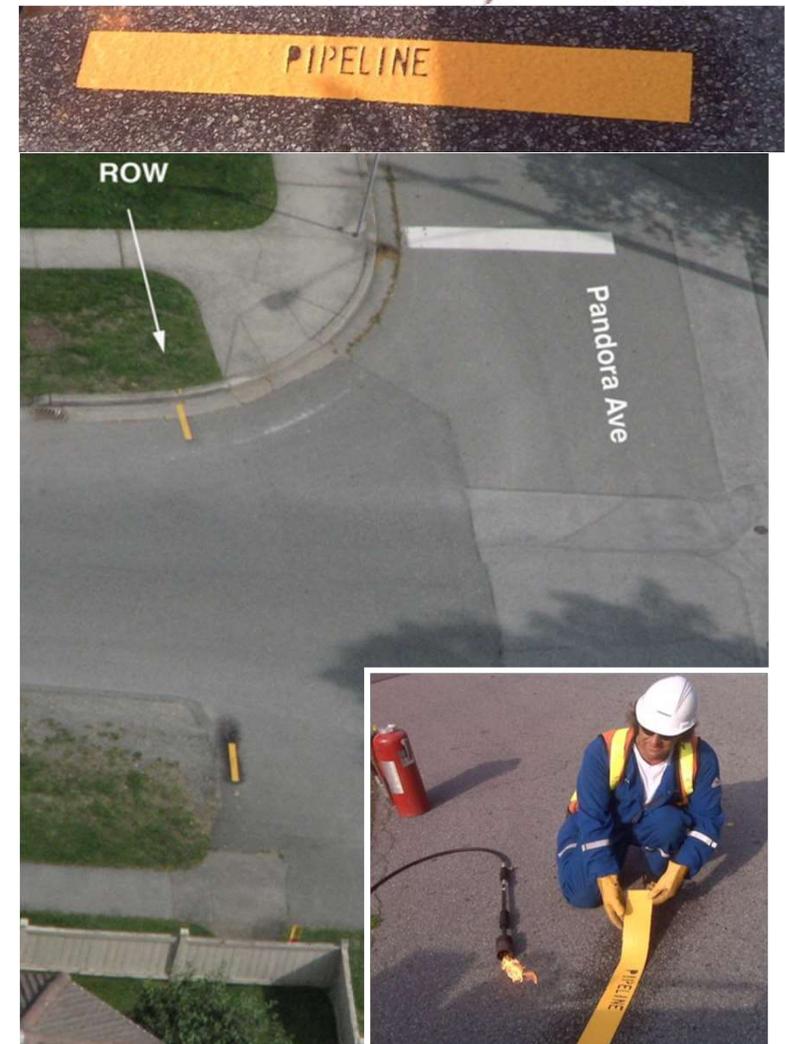


Increasing effort to avoid unauthorized ground disturbance activity on TM Jet

- Public awareness programs and training
- Aerial and driving patrols
- Management of line markings and third party crossings

Line Marking Inventory & Upgrade

- Upgrade marking to “line-of-sight”
- Create GIS inventory of markers
- Co-incident depth of cover surveys
- Site inspection during work done by third parties in proximity of the pipeline



In Line Inspection - 2007



- **ILI (smart pig) run was completed in 2007 with results and action plans implemented in 2008**
 - ❑ Engineering assessment was completed on all identified anomalies and program work identified
- **14 dent anomalies were identified for investigation**
 - ❑ All critical dent anomalies were repaired in 2008
 - ❑ 2008 repairs include:
 - 4 dents repaired to date, with 2 to be complete by year end;
 - 8 remaining dents all operate at lower stress levels and will be repaired in future years.
- **27 corrosion features identified**
 - ❑ 3 verification digs are to be completed in 2009 (to ensure tool accuracy)
 - ❑ No future corrosion digs anticipated at this time

Cathodic Protection



➤ 2008 Program update

- Rectifier replacements with remote monitoring units complete
- Completed annual CP survey

➤ 2009 Program

- Remediate shorted casing - capital \$40K
- CP survey performed annually to meet code requirements - operating \$15K

Capital Programs: 2008 / 2009



	2008		2009
(\$000)	Plan	Final	Plan
2008 Projects			
- Expansion Joint Replacement (Airport)	83.7	70.0	
- Cathodic Protection Program (rectifiers replaced)	45.6	35.7	40.0
- Airport Tank Valve (spare)		7.0	
- Pipe Repairs (4 locations cutout and replaced)		276.0	
2009 Projects			
- Stress Relieve NPS 6 Line @ Byrne Road/Marine Way			75.0
- Byrne Road Monitoring (study)			12.0
- General Sustaining Capital			20.0
Total	129.3	388.7	147.0
Note: Pipeline repairs were completed in 2008 as a result of 2007 ILI results.			

Operating Projects



➤ 2009 Planned Increases (\$156K)

- ❑ 3 Corrosion Anomaly Verification Inspections (\$50K)
- ❑ 15 natural hazard ground inspections, 2 depth of cover surveys and 1 natural hazard remediation (\$35)
- ❑ CP annual survey (\$15)
- ❑ Increased costs for Pipeline Protection (\$56K)

➤ 2008 work focused on completing the capital pipeline repairs identified by the 2007 ILI

Quality Assurance



➤ Jet Fuel Filtering

- Burnaby (two vessels) 2008 YTD
 - 16 filter vessel change outs
 - better than 2007 by 50%
 - approx. \$1,150 per change out
- Airport (two vessels) 2008 YTD
 - 8 filter vessel change outs
 - better than 2007 by 27%
 - approx. \$1,800 per change out
- Same number of changes outs expected for 2009

Operations Conclusions



➤ Cost for maintaining & operating the pipeline will not go down

- Prudent owner responsibility and regulatory oversight will tend to increase costs over time
- TMJ is approaching 40 years old, requiring on going attention to protect the pipeline, and to provide service and quality of service to shippers
- In 2009, the pipeline protection program and structure will be fully in place and the costs will be fully shared with TMJ

➤ TMJ operates as an “adjunct” to the larger Trans Mountain pipeline, receiving many benefits from this association

- Trans Mountain is currently finalizing a “Code of Conduct” that may result in increased costs to TMJ

2009 Tolls Overview



Key Issues

- Depreciation rate review
- Collection of Abandonment fund review
- Increasing Costs
- 2009 toll prediction

Depreciation Study



➤ Need?

- ❑ Pipeline rates have diverged from 1994 study and the then approved rates, declining from approximately 3.0% to 2.5%

➤ Action required?

- ❑ Reset rates using agreed to life
- ❑ Proposal, starting with NET book value:
 - Long life assets are reset using 20 years
 - Selected assets are reset using physical life
- ❑ Why agree? – avoid cost of performing economic life study and business risk assessment

➤ Result?

- ❑ Increase average depreciation rate to 3.35% (up 0.8%) or back to average life of approximately 30 years, same as previous

Collect Abandonment Funds



➤ BCUC 2008 Decision

- ❑ Consideration of issue was set aside until further progress is made on determination of tax treatment
 - This is unlikely to occur unless interested parties can demonstrate need or desire to implement. NEB process may or may not be able to demonstrate need.
 - Current economic environment likely to make this a difficult “sell” to Federal Government as it may be seen as “lowered taxes” for pipelines & oil companies – not necessarily seen as “in the public interest”.

➤ Collection is prudent at this time

- ❑ Principles for collection are:
 - Landowners should be held harmless from cost of pipeline abandonment
 - Abandonment is a cost of operating a pipeline
 - TMJ has the added risk that line of sight is short
 - Governments should not be responsible for funding pipeline abandonment
 - Regulators can consider the application and approve the collection of funds
- ❑ Lack of defined tax mechanics should not over rule prudent actions taken by pipelines,

Collect Abandonment Funds



➤ Proposal

- ❑ Begin collection based on current abandonment estimate
 - \$3.0M, assumes abandonment in place and sectioning the pipeline
 - TMJ will refine estimates during 2009
- ❑ Use proposed depreciation life – approximately 30 years
- ❑ Funds to be held for this purpose and this purpose only
- ❑ Funds deemed to earn a return based on the average GIC or selected government bond rates permitted by QET's
- ❑ Funds will not be tax exempt, CEPA is working on a strategy to again request pension fund or QET type tax exemption for payments (fund earnings will be subject to tax – based on preliminary comment from Finance)
- ❑ Once abandonment funding mechanisms are clarified, segregated funds will be transferred to the appropriate financial vehicle (i.e. strong potential for trust type mechanism)

➤ **Example of calculation provided on Appendix 1 would be adjusted from 20 to 30 years.**

Increasing Costs



(\$000)	2008		2009	%
	Approved	Update	Proposed	change
Rate Base	9,784	9,949	9,787	-2%
Revenue Requirement				
- O&M plus ILI & hearing amortization	2,084	2,043	2,413	18%
- Return on Capital	720	773	751	-3%
- Return of Capital	415	414	546	32%
- Provision for Income Taxes	219	218	264	21%
- Refunds	(15)	(15)	(3)	
Total	3,423	3,433	3,970	16%

Note Revenue Requirement does not include provision for collection of abandonment.

Tariff Changes - Tolls



➤ Proposal – Mid December filing:

- ❑ January 1, 2009: 2008 tolls interim & then final
- ❑ March 1, 2009: 2009 tolls final
 - Tolls calculated on a prospective basis
- ❑ Approved and Proposed tolls:

\$ / m ³	2008	2009
Mainline	2.3965	3.0333
Gathering Facilities	0.8932	1.0478
Total	3.2897	4.0811

- ❑ Toll Increase is 24%, 16% for costs, 8% for volumes

Tariff Changes – Rules & Regs



➤ Proposal

- ❑ CSA Standard reference (Definition (f))
- ❑ Tickets will no longer be signed through elimination of manual tickets and transition to Centralized Control Centre Operation (Rule 45)
- ❑ Proposal for Measurement (Rule 40):
 - TMJ meters all receipt batches,
 - Proposal to use GlobeGround meters for all delivery tickets
 - KMC to research as part of required changes to meet Centralized Control Centre Operation.
 - Minor modification to streamline inventory management process may be required.

Future Considerations



➤ Higher Throughput drives Lower Tolls & Expansion:

- ❑ Key to TMJ viability is to increase throughput
- ❑ Pipeline has not pumped close to capacity since 1999 (9 years) due to lower demand
 - for 2008, maximum capacity achieved was approximately 80% of capacity for only 5 days, or 1.4% of the year
- ❑ Impact of recession on TMJ?
 - More throughput on the pipeline would reduce risk
- ❑ How might this be achieved? How might perceptions be changed? The pipeline can move more volume.

Expansions



- Previous studies identified phased expansions for base load growth

Capacity m3/d	Expansion
4896	existing
6240	add pump hp
7200	add more pump hp
9600	add pump hp and loop upstream of YVR

- Expansion should match system load factor
 - ❑ Base load growth – pumping power or pipeline looping
 - ❑ Peak demand growth – storage
- Recent use shows TMJ has a low load factor punctuated by short duration peak throughput events
 - ❑ Additional end use storage should be considered before expansion of base load facilities

Questions / Action Items



➤ Questions?

➤ Tariff Approval Process:

- ❑ Shippers confirm receipt of documentation
 - Provide indication of support or lack of support for key elements of filing by December 12
 - TMJ to communicate back to Shipper by December 16
- ❑ TMJ to complete filing with changes as discussed
 - Filing Date December 18
- ❑ Anticipated Approval Date – March 1, 2009
 - Provides 60 days for BCUC review and approval