

IN THE MATTER OF the *Ontario Energy Board Act 1998*; S.O. 1998, c.15
(Schedule B);

AND IN THE MATTER OF an Application by Enbridge Gas Distribution Inc.
("EGD") for an Order or Orders approving or fixing just and reasonable rates and
other charges for the sale, distribution and storage of gas commencing January 1,
2009.

**WRITTEN ARGUMENT
OF BP CANADA ENERGY COMPANY ("BP CANADA") - ISSUE NO. 7**

I. Introduction

A. BP's Interest in this Proceeding

As noted in its letter of intervention dated October 30, 2008, BP Canada is one of the largest explorers, producers and marketers of natural gas in Canada, with significant business interests in Ontario. Thus it would be affected by the decision in these proceedings.

It should be noted that BP Canada and its affiliates operate in all gas markets in North America. The rules and regulatory and competitive frameworks vary, and BP adapts its practices and marketing activities in accordance with those rules and frameworks. If the rules in Ontario change, BP Canada will adapt. It does however have concerns and a point of view about the role of competition and market solutions, and has approached the issues in this hearing from that perspective.

BP Canada acknowledges that EGD shoulders the responsibility for system and supply planning, and carries default supplier obligations to its customers, particularly smaller volume residential and commercial customers. It is entirely appropriate for EGD to concern itself with the risk of supply failure. That risk affects all customers on EGD's system, and all parties, including BP Canada, engaged in the natural gas market. Thus all parties to this proceeding share a common interest in seeing that the system continues to operate in a reliable, safe, and efficient manner.

BP Canada takes no issue with EGD's supply planning design principles – the balancing of the design to minimize both costs and probability of supply shortfall. BP Canada agrees that the "ultimate goal of the planning process is to determine the optimal supply portfolio that will result in the lowest ... cost without jeopardising reliability ..."¹.

Similarly, BP Canada acknowledges that it is totally within EGD's authority and responsibility to select the weather-related criteria for planning purposes.

B. BP Canada's Position

It is not the planning parameters or Design Day ("DD") criteria with which BP Canada takes issue; rather, EGD's conclusions about the nature of the risk of supply shortfall, and the appropriate solution to the mitigation of that risk, warrant examination.

In summary, for reasons noted below, BP Canada believes that the market, working with the substantial excess capacity on TransCanada Pipelines Ltd. (TransCanada's") system, has shown repeatedly its ability to meet EGD market area needs. This includes suppliers meeting their firm delivery obligations. Thus, no mandated firm transportation contracting should be required. Alternatively, if the OEB has residual concerns about delivery reliability in the future, then in BP Canada's view there are other solutions that are more efficient, cost effective and complimentary to the on-going maintenance and development of a competitive market in Ontario.

II. Background

A. The Development of a Competitive Commodity Market in Ontario

In its Report "**Natural Gas Regulation in Ontario: A Renewed Policy Framework**", dated March 30, 2005², the Board reviewed the history of natural gas deregulation in Ontario, dividing it roughly into two phases.

In the first phase (1985-1996) the Board oversaw the facilitation of access for consumers to upstream markets through the unbundling of gas supply and long-haul

¹ Consumers Gas - Gas Supply Planning Design Criteria Study, Exhibit TCU-2/6; pages 115-155, Exhibit H.D1.2 (the "Planning Study")

transportation arrangements. In the result most large volume and a significant number of smaller volume customers entered into direct purchase arrangements.

During the second phase (1996-2005) legislative amendments were made to address, among other things, issues laid out by the Board in its **1996 Report on the Ten-Year Review of Natural Gas Deregulation**.³ Movement of smaller consumers from system to direct purchase supply continued, such that by 2005 over 50% of EGD's customers (by volume) and 40% by number accessed the direct purchase option. In fact, direct purchase volumes had been higher, but fell back slightly (**Policy Framework, page 8**).

It is noteworthy that initially all transportation into EGD's franchise area was held by EGD, a common situation among LDC's. Flowing out of the commencement of deregulation in 1985, EGD renegotiated its contracts with TransCanada effective November 1, 1988 for a 15 year term. As direct purchase arrangements increased in the intervening years, EGD facilitated those arrangements by assigning a portion of its FT capacity held on TransCanada's system. Beginning earlier (but by far the largest volume occurred November 1, 2003) EGD permitted direct purchase marketers to turn back the TransCanada capacity, which was then not renewed by EGD. (**Transcript - May 8, 2009, pages 115-116**)

EGD did not require that the turned-back capacity be replaced with firm capacity on the TransCanada system, but assumed, apparently, that it was. In the result there was a substantial drop off effective November 2003 in the level of firm transportation capacity into the Ontario market.

In not holding FT contracts to fulfill their firm delivery obligations, the direct purchasers and their agents were doing nothing wrong, nothing illegal and were not in breach of contract or agreement with EGD. (**Transcript - May 8, 2009, pages 116,117**)

B. The Importance of Competitive Markets

² Ontario Energy Board - Natural Gas Regulation in Ontario: A Renewed Energy Policy Framework - Report on the Ontario Energy Board Natural Gas Forum- March 30, 2005 ("Renewed Policy Framework")

³ Ontario Energy Board - Report on the Ten-Year Market Review of Natural Gas Deregulation - September 27, 1996 ("Ten Year Review")

Throughout this history the OEB has continuously endorsed, where appropriate, competition, including competition in the gas retail sector, and has worked to enhance it.

For example, in the Ten-Year Review, the Board concluded "that a fully competitive gas commodity market will be more efficient than a regulated market. Accordingly, where an efficient and equitable market is possible and sustainable, the Board believes that customers can best be served by allowing the market to operate freely ..." (page 7).

In that report the Board noted that at the time the then current legislation was enacted, the natural gas market was not expected to include competition at the burner tip, capacity trading, marketing hubs, ABMs, futures contracts, electronic trading boards or a competitive gas commodity market (page 9). As a result, among other things, the Board noted the need, and its intention to ask, for legislative change. One of those amendments is found in Section 2 of the *Ontario Energy Board Act*:

"2. The Board, in carrying out its responsibilities under this or any other Act in relation to gas, shall be guided by the following objectives:

1. To facilitate competition in the sale of gas to users."

The second objective relates to protection of consumer interests with respect to prices and the reliability and quality of gas service.

In its Renewed Policy Framework, the Board made repeated, explicit note of the competition objective. In its discussion of the continuance of regulated gas supply, the Board acknowledged that it is guided by the objectives set out above. It concluded that "on the direct purchase side, the Board believes that consumers' interests are best protected through the development of robust competition ...", oversight of marketers and customer education (page 61). Later, the Board noted its belief that further unbundling of utility services would "facilitate competition by moving the regulated gas supply option and competitive options towards a level playing field." (page 66)

Further, in addressing the issue of security of supply the Board indicated that it was not convinced that long-term utility supply contracts were essential, and that "access to a

liquid [including downstream] hub provides the best assurance of secure access to competitively priced supply." (page 72)

It is not surprising then, that in its recently published **Filing Guidelines for the Pre-Approval of Long-Term Natural Gas Supply and/or Upstream Transportation Contracts**, Section 5.2 requires an assessment of retail competition impacts.

In its **Decision in EB-2005-0551 (Natural Gas Electricity Interface Review)**, Section 4.1 was entitled "To Facilitate Competition in the Sale of Gas to Users". The Board said the following, at pages 44 and 45:

"The Board has worked over time to ensure that Ontario consumers reap the benefits of commodity competition. The Board must continue to pursue this objective and can do so by facilitating the evolution of a robust market in Ontario. ... One way to do this is to encourage the development of innovative services and to ensure access to those services. Choice is the bedrock of competition. The evolution of the transactional services market is an example where innovative and flexible services have evolved within a market-based pricing structure."

The Board noted further, at page 45, that

"Enbridge argued that forbearance [from regulation] will foster innovation by facilitating the provision of storage services in the competitive market."

This then is the context in which the Board ought to review the EGD proposal. It also ought to have been the framework for EGD's assessment and development of solutions. As BP Canada will discuss below, this context was ignored by EGD, and this failure accounts in large part for the proposal's inadequacy.

III. **Rationale for the Proposal and Process Followed to Advance the Proposal**

It is important to understand how EGD arrived at its proposal, and the process it followed. In BP Canada's view both were flawed. They may be summarized as follows:

- (a) Sometime in 2007 EGD became concerned with the level of firm transportation capacity held by direct purchasers or their suppliers. (It is common ground that direct purchasers have a firm obligation to deliver

the supply Mean Daily Volume to EGD.) Indeed, it was characterized by Ms. Ghiridar as a sudden drop-off in firm transportation in 2006. (It was subsequently conceded by Ms. Ghiridar that the level of FT Contracts to the CDA may be seen as experiencing a sudden increase for the winters of 2004/05 and 2005/06, and the "drop-off" was actually a reversion to 2003/04 levels.) (**Transcript - May 8, 2009, page 117**)

- (b) Because the direct purchaser's obligation was for firm delivery to EGD, EGD summarily concluded that it must be back-stopped by firm transportation on TransCanada. (**See EGD response to BC Canada Information Request No. 7(a)**) It arrived at this conclusion without knowing how the direct purchase market was, in fact, being served and made no attempt, other than through casual conversation (**Transcript - May 8, 2009, pages 132, 135**) to contact direct purchasers or their suppliers to determine how the gas was getting to the CDA. But it did know that all supplies arrived as contracted for, including on the severe days in January 2004.
- (c) Having concluded that FT on TransCanada was required, senior management's approval was sought and obtained (**see response to Shell Information Request No. 5(iii)**), and the application was filed. Again, prior to the application, there was no consultation with the players in the direct purchase market.
- (d) No apparent consideration was given to the impact the proposal might have on arrangements made by direct purchasers - for example, the costs associated with unwinding hedges made with regard to gas purchases at the CDA. In fact, EGD was unaware this was even an issue until Direct Energy's Information Requests and/or Evidence. Enbridge knew prior to filing its application (and ought to have known if it did not years earlier) that there was no FT service to the CDA for a large volume. In these circumstances it is not surprising that the point of sale may have been the

CDA rather than Empress, and that CDA may have been the hedge location. **(Transcript - May 7, 2009, pages 35-38)**

- (e) No attempt was made to analyze the ostensible supply failure risk as to probability, even in a qualitative way. This is perhaps not surprising in the sense that EGD concluded early in its review that lack of firm transport equalled supply failure, curable only by firm transport. The solution proposed is for FT service – 365 days of the year. EGD acknowledged that the risk about which it is concerned is only for the winter season (November-March) and within that season, only about 15-20 days. **(Transcript - May 8, 2009, pages 130-131)** In fact, Ms. Ghiridar conceded that in January 2009, only on one day did EGD have real concern about gas supply showing up late in the nomination cycle.
- (f) As noted above, EGD made no real effort to ascertain how the gas was getting to the CDA on the coldest days of winter – that is, how the market worked. (It is common ground that it did.) Nor did EGD make any effort to ascertain the identity of suppliers behind the direct purchase arrangements. This is a bit surprising (but perhaps not so given EGD's early conclusion that firm equals firm), inasmuch as EGD itself contracts for approximately 250,000 GJ's/d of peaking supply without a requirement for firm transport back-stopping the firm supply obligation. **(Transcript - May 8, 2009, page 130)** It makes these arrangements with reputable suppliers based in part on their strength as a supplier and the integrity of their covenant. **(Transcript - May 8, 2009, page 133; May 7, 2009, page 17)** This arrangement has worked, and there is no reason it should not continue.
- (g) As originally filed, EGD's proposal applied to all direct purchase volumes delivered at the CDA and EDA. Perhaps as a result of meeting with stakeholders after the application was filed, EGD revised this to apply only to 90% of the MDV of the smaller volume users.

- (h) Subsequent to management approval and the filing of the application, EGD revised the underlying rationale and support for its proposal. The explanation started out as firm equals firm simpliciter – that is firm delivery obligations must be matched by firm transport, regardless of the nature of the risk (for example, that there is 1.5 bcf/d excess capacity to the CDA on TransCanada). Since that time the rationale was expanded to include:
- (1) the fact that direct purchase customers were paying for firm transport in their retail rates, and therefore were entitled to receive it;
 - (2) firm transport for an additional 200,000 GJ/d is somehow mandated by its 1995 Planning Study.

The first is a red herring relative to the underlying risk issue and in any case is largely a function of a billing system about to change. The second misrepresents what the plan actually requires. As noted earlier, the Planning Study mandates a balance between cost (read as a proxy for firm vs. less expensive and more flexible transport options) and reliability. The conclusions of that balancing act in 1995 might be, and in BP Canada's view should be, quite different compared to today. The Planning Study and then appropriate contracting solutions were pre-Alliance Pipeline, pre-Northern Border expression, pre-TransCanada expansion. TransCanada was a constrained system and there was very little uncontracted capacity into the CDA. **(Transcript - May 8, 2009, pages 122, 123)** It is not clear under what circumstances (if not the current scenario) economic efficiency can be realized and a portfolio of contracting options employed, when FT contracts are determined to be necessary regardless of excess capacity on feeder pipelines.

- (i) The proposed solution, even though principle driven (firm equals firm) does not meet its purported objective. EGD has noted that it is not

mandating contracting path, but as a practical matter, because there is no short-haul capacity available, the direct purchasers must contract for FT on the northern segment of TransCanada's main line. However, EGD has indicated that it is not insisting that the receipt point for such contract be Empress. It could, if a party chose, be North Bay. **(Transcript - May 8, 2009, pages 126, 127)** To not be as concerned about reliability at North Bay as you would be the CDA means either:

- (1) there is no unmanageable risk at North Bay (and therefore not at the CDA); or
 - (2) EGD has not really thought this proposal through.
- (j) That the proposal might not have been fully thought through may be attributable to the fact that:
- (1) The analytical approach was flawed;
 - (2) Effectively no alternatives were considered; and
 - (3) This proposal is an interim plan and there is a longer term solution not currently before the Board.

The analytical approach and question of alternatives and the road(s) not taken will be addressed below. With respect to a longer term plan, this was not apparent in the evidence filed with the application, but rather emerged through the discovery process, technical conference, and cross-examination. In summary, it would appear that EGD will advance a vertical slice (or other) solution to be effective 2 to 3 years from now. If vertical slice, EGD will contract for an incremental level of firm transport on TransCanada (and perhaps other pipelines?) and then assign back to direct purchasers a pro-rata slice of all firm transportation arrangements. The common feature between the longer term plan and the current proposal appears to be incremental firm transport. Doubtless a process,

including a collaborative, consultative element, will be part of the development of this solution. For the moment, one cannot help but speculate that the current proposal is driven, at least in part, by a view to a new long-term framework.

The historical context, and the Board's approach and legislative mandates related to competition, form an important lens through which EGD's proposal must be viewed. The status quo, pursuant to which direct purchase volumes are delivered to the CDA on services other than FT on TransCanada, has been in effect to varying degrees, since before 2003. The market has worked every single day. There has never been a supply failure associated with transportation capacity. There is no evidence that supply has been redirected to higher-value markets (an implied suggestion in Dr. Overcast's evidence on re-examination in circumstances where there is no fixed cost transport associated with a supply obligation). **(Transcript - May 8, 2009, page 204)** The reality is that there is now, and will be for the foreseeable short-term future, substantial excess capacity on TransCanada to the Ontario market. Markets, and players in those markets, are finding efficient solutions as an alternative to going long on transportation with its associated fixed cost. (Innovative and flexible services have evolved within a market-based pricing structure, as noted by the Board in EB-2005-0551 (see page 5 above).) Indeed, that is how EGD's peaking supply contracts are served.

The market was tested in January 2004 and passed the test. It was successfully tested again in January 2009. Those examples are used by EGD in support of its proposal. They really are examples of why its proposal is not necessary, or, at least, more than is required.

It is perhaps moot to consider what EGD's portfolio would look like today if direct purchase had never occurred. The principles of the Planning Study (or some similar) would still govern. The debate would be, as it is here, about the appropriate balance between cost and efficiency, and reliability – between long-term, fixed expensive contracts on the one hand, and a mix of those and creative solutions to address real risks, with an appropriate probability assessment (even if only qualitative) on the other.

IV. **The Road Not Taken**

It is apparent that no meaningful consideration of alternatives was undertaken by EGD. In part this likely occurred because judgment and principle entered into the decision-making framework prematurely, and the process ignored the historical and contextual issues about competitive markets discussed above. Compare and contrast the following two approaches:

- (a) Direct purchasers are obligated to deliver 457,000 GJ/d (sum of the MDV's) to EGD on a firm supply basis.
- (b) Direct purchasers have not contracted for FT service on TransCanada and are meeting their firm supply obligations to EGD in other ways.
- (c) TransCanada cannot absolutely guarantee delivery using other than FT service.
- (d) There is therefore a risk of non-delivery on peak winter days and near-peak days.

(Note: At this point there is no difference in approach.)

Enbridge Approach

- (e) Firm supply must be underpinned by firm transportation (the application of judgment and principle prematurely).
- (f) Direct purchasers (later revised to approximately 50% of the direct purchase market) must back-stop their obligations with FT service.
- (g) Because there is no short-haul capacity available on TransCanada, there is no alternative to FT service on TransCanada's northern line.

(Note: No questions asked.)

A Different Approach

- (h) There is currently 1.5 bcf/d of excess capacity on TransCanada.
- (i) Notwithstanding the lack of firm transportation associated with the direct purchase volumes, what has been our experience to date? Have there been supply failures associated with lack of firm transportation. Is this likely to change over the short, medium, longer terms?
- (j) Can we quantify the risk of non-delivery? Quantitatively? Qualitatively?
- (k) For what period does such risk realistically endure – all year, winter season, a number of days in winter season?
- (l) How are the direct purchasers, agents and their suppliers currently discharging their firm delivery obligations? How confident can we be in their continued performance?
- (m) Who should we involve in this analysis and, if appropriate, the development of solutions? Director purchasers and agents? Natural gas marketers and suppliers? TransCanada? Consumer groups?
- (n) Assuming the risk (whatever its measure) is only for a certain number of days, what might be done to eliminate or mitigate that risk? What are the alternatives available?
- (o) For each alternative:
 - (1) what is the cost to Ontario consumers, both system supply customers and direct purchase customers?
 - (2) can we assess the degree to which risk has been mitigated?
 - (3) what is the impact on competition in the sale of gas?

- (4) what is the impact on the development of competitive sales and pricing hubs in Ontario?

Taking into account all of the foregoing, a reasoned approach can be developed. The options range from doing nothing at all, to accepting EGD's proposal to compel direct purchasers or those on their behalf to acquire FT service.

If the conclusion is that, taking into account the factors above, that there is no unmanageable risk, then the answer is do nothing.

On the other hand, BP Canada recognizes that no one wants to see a supply failure or be associated with one (This includes gas suppliers, for whom a reputation as being reliable is everything.) EGD's special role and obligations in dealing with consequences are acknowledged. The Board's objectives include reliability of gas supply.

If, after going through a proper analytical and decision-making framework, one concludes some action is warranted, then BP Canada offers the following suggestion to get to an appropriate solution.

V. The Alternative

It is clear from the record that EGD's concern relates to the risk of supply failure on a relatively few number of days during the winter season. That would suggest that any solution obligating a supplier to have firm transport for 365 days, or for the entire winter, is inefficient and ultra-conservative.

In BP Canada's view, assuming the Board is of the view that something is warranted to mitigate the risk of supply failure on peak or near-peak days in winter, it should direct EGD to meet with stakeholders and others who may contribute to the solution, and develop a peaking-type back-stop arrangement - an insurance policy of sorts - for a number of winter days. This approach should be acceptable to EGD as it enters into arrangements of this kind (approximately 250,000 GJ/d) to meet its peak day obligations.

The costs associated with this back-stopping arrangement should be borne by all customers for three reasons:

- (i) EGD provides balancing and peaking services to the entire bundled service market (both system supply and direct purchase customers) (**Transcript - May 8, 2009, page 128**);
- (ii) the new arrangement is intended to address market requirements and a "risk" that is a function of the development of the market in Ontario;
- (iii) the ongoing facilitation and development of a competitive market in Ontario is important and for the good of Ontario.

Should it ever be used (which is unlikely given the evidence to date of the market's ability to meet its obligations) then a proportionate share of the fixed costs, and commodity charges with penalties, should be passed on to the non-performing party.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 2nd DAY OF JUNE, 2009



J. David Brett
Counsel to BP Canada Energy Company