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January 25, 2011

VIA EMAIL, RESS and COURIER

Ms Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street,
27th Floor
Toronto, Ontario
M4P 1E4

Dear Ms Walli:

Re: Enbridge Gas Distribution Inc. ("Enbridge")
Pre-Approval of Long-term Transportation Contract
Ontario Energy Board ("Board") File No.: EB-2010-0333

As decided on January 20, 2011 at the joint hearing of applications from Union Gas and Enbridge for long-term contracts with TCPL, attached please find Enbridge's Reply Argument.

Enbridge's Reply Argument is also being filed through the Board "RESS" and will be available on Enbridge's website at www.enbridgegas.com/ratecase, as of January 26, 2011.

Yours truly,

SLSpratt

Shari Lynn Spratt
Supervisor Regulatory Proceedings

cc: Mr. David Stevens, Aird & Berlis LLP
All EB-2010-0333 Interested Parties (via email)

ONTARIO ENERGY BOARD

IN THE MATTER OF the *Ontario Energy Board Act*, *1998*, S.O. 1998, c. 15, Sched. B, as amended;

AND IN THE MATTER OF an application by Enbridge Gas Distribution Inc. for an order or orders pre-approving the costs associated with a long-term gas transportation contract.

ENBRIDGE GAS DISTRIBUTION INC.
REPLY ARGUMENT

On January 21, 2011, Enbridge Gas Distribution Inc. (EGD) delivered its Argument in Chief in support of the preapproval of the cost consequences of a long-term transportation contract with TransCanada PipeLines Limited (TCPL) to transport Marcellus shale gas from Niagara to EGD's central delivery area (referred to in these submissions as "the Contract"). In response, oral arguments were made by TCPL, Consumers Council of Canada (CCC) and Canadian Manufacturers & Exporters (CME) and written arguments were filed by Ontario Energy Board Staff (OEB Staff), the Association of Power Producers of Ontario (APPrO), Energy Probe Foundation (Energy Probe), Industrial Gas Users Association (IGUA) and the Federation of Rental Providers of Ontario (FRPO). In accordance with the process established by the Ontario Energy Board (OEB, or the Board) in this case, EGD is now providing its Reply.

Although it has been stated in a number of different ways, the key question raised by this Application is whether the Contract is the type of long-term contract for which preapproval is appropriate under the OEB's Guidelines for the Pre-Approval of Long-Term Natural Gas Supply and/or Upstream Transportation Contracts (the Guidelines). EGD submits, for the reasons set out in evidence and Argument in Chief, that the Contract is the very type of contract that the Guidelines are meant to address.

Energy Probe and TCPL support EGD's application, and FRPO supports approval of the Contract (albeit with conditions).

The reasons cited by Board Staff and other parties as to why the Guidelines ought not to apply to the Contract are not supported by the evidence or by the Guidelines themselves. The Board's Report issued in respect of the Guidelines makes clear that a pre-approval process is appropriate for long-term contracts that "support the development of new natural gas infrastructure (e.g., new transportation facilities to access new natural gas supply sources)"[1]. While the Board's letter that accompanied the Report gave an example of connecting "frontier production"[2] as one of the types of infrastructure it had in mind, it is clear that the Board's focus in the Guidelines is broader than that and is directed at encouraging contracts that support new infrastructure to any new supply sources. This is seen in the comment in the Report that "the Board is of the view that long-term transportation contracts may help to ensure an adequate

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[1] Page 4, Report of the Board – Draft LTC Filing Guidelines, February 11, 2009, EB-2008-0280 - found at Tab 4 of Ex. K1.5.

[2] See also 2 Tr. 66, for CME's characterization of this phrase.

natural gas supply in the Ontario market from a diverse portfolio of sources" as "[t]his may increase supply reliability and reduce price volatility, which would benefit all market participants".[3] A similar point is made in FRPO's submissions which state that "the intent of the Pre-approval process is to enable the utilities to make long-term commitments to underpin the investment in facilities which have a long-term benefit to the market it serves."[4] Contrary to the submissions of APPrO[5] and Board Staff[6], the investment in new facilities contemplated by the Contract to serve EGD is significant – it involves work estimated at $128 million on TCPL's Niagara to Kirkwall line (to reverse the flow), Union's Kirkwall facilities (to reverse flow) and TCPL's Parkway to Maple line (to enhance flow, through compression and looping).[7]

The Contract in this case will enable EGD system gas customers to have access to Marcellus shale gas, which is an important new supply source not currently accessible to available to Ontario customers. The Contract is not, as CCC suggests, a "garden variety" transportation contract.[8] Contrary to Board Staff's submission, the Contract is different from EGD's "normal day-to-day contracting".[9] It is a long-term (ten year) contract that enables supply on a new path directly to EGD's central delivery area (CDA) from an important new supply source. The Contract contemplates that significant new natural gas infrastructure will be built, and it carries not insignificant penalties in the event of cancellation.[10]

Contrary to the assertions of CCC[11] and APPrO[12], this Contract does address security of supply, as well as diversity of supply. This is seen by the fact that the Contract will facilitate the delivery of Marcellus gas (which is a new source of supply) directly to Kirkwall and EGD's CDA, using a new transportation path. The new Marcellus gas supply will displace spot gas purchases (and some peaking supply) that EGD currently acquires to meet its growing system gas customer demands.[13] As such, this supply will be more secure as it will be underpinned by a firm transportation path. With respect, EGD objects to the suggestion by Board Staff that because EGD has no diversity and supply issues now, there is no need for Marcellus supply. EGD points out that this statement is also at odds with the submissions of other parties. As APPrO pointed out, Marcellus shale gas is "a new and significant emerging major supply basin that will impact consumers in Ontario".[14] As FRPO stated, "[o]ne of the points of emphasis by the utilities in this proceeding is the opportunity for supply diversity ..[f]rom a simple economic point of view, diversity in a portfolio of contracts is fundamental .. accessing natural gas supply from a more geographic proximate source would be beneficial … we commend the utilities for their initiative in seeking to contract for firm transport from the developing supply source."[15]

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[3] Ibid, at page 3.
[4] Reply Argument of FRPO, dated January 24, 2011, at page 3.
[5] Reply Argument of APPrO, dated January 24, 2011, at page 3.
[6] OEB Staff Submission, dated January 24, 2011, at page 5.
[7] Exhibit K2.1 and 2 Tr. 3-5 and 48-49.
[8] 2 Tr. 60.
[9] OEB Staff Submission, dated January 24, 2011, at p. 8.
[10] As an aside, EGD rejects CME's characterization (2 Tr. 64) of the potential $17 million penalty as "not unusual in any respect" for a company of EGD's size.
[11] 2 Tr. 57.
[12] Reply Argument of APPrO, dated January 24, 2001, at page 4.
[13] 1 Tr. 142,165 and 175-176.
[14] Reply Argument of APPrO, dated January 24, 2001, at page 3.
[15] Reply Argument of FRPO, dated January 24, 2001, at page 4.

Some intervenors, as well as Board Staff, suggest that rather than applying the Guidelines and pre-approving the cost consequences of the Contract at this time, the Board should instead leave it to EGD to continue with the Contract and then seek approval of the cost consequences as they are incurred each year.[16] It is suggested that EGD must have concerns about the Contract if it needs to get pre-approval of the costs, and that in itself supports the view that no pre-approval should be issued.[17] EGD disagrees.

First, the fact that a utility chooses to make use of the pre-approval option that the Board has established and implemented is in no way an admission that the contract is question is imprudent or unduly risky. It is instead a proper approach for a responsible utility to follow. EGD should not be penalized or questioned for seeking approval under Guidelines that the Board has approved, and with which "stakeholders generally agreed".[18]

Second, the annual approval of transportation costs in a rate proceeding only deals with costs for the one year in issue – that does not establish the same relief as what is sought here. Once EGD commits to the Contract, it is committed for ten years. A rate case review of the 2011 cost consequences of the Contract would not address that fact, nor provide relief for cost consequences in future years.

Third, as noted by intervenors in argument, the "prudence review" that the Board undertakes when examining incurred costs in rate proceedings is to be done based on information known at the time that the decision to incur those costs is made. The prudence review is not intended to be done using the benefit of hindsight, which would apply subsequent facts to assess an earlier decision. In EGD's submission, this means that the Board is in position to make an assessment of the costs associated with the Contract now. As explained in evidence, EGD faces risk of cancellation costs of $10 million or more as of January 31st. It can only avoid exposure to that risk by providing notice of cancellation in advance of that date. As a result, the threshold decision of whether to proceed with the Contract must be made now. That decision is to be made in light of all currently available information, which is the same information as has been presented in this proceeding. Therefore, the Board is in the same position now to assess the prudence of entering into the Contract as it will be later.

Finally, EGD submits that the Board has all the information needed to provide the requested pre-approval at this time.[19] The "unknowns" asserted by intervenors ought not to delay a decision.

There is no real or substantial risk that Marcellus supply will not be available.[20]

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[16] See, for example, the submissions of CCC and CME at 2 Tr. 55 and 2 Tr. 62, and OEB Staff Submissions, at page 8.

[17] CME's assertion in this regard is at 2 Tr. 65.

[18] Page 2, Report of the Board – Draft LTC Filing Guidelines, February 11, 2009, EB-2008-0280 - found at Tab 4 of Ex. K1.5.

[19] In response to IGUA's submission that applicants must manage and time their contracts to allow full regulatory review, EGD notes that it filed its application as soon as possible after the Precedent Agreement was signed, and that the January 31, 2011 approval date is driven by third parties, not EGD. In any event, EGD believes that there has been a "full regulatory review" in this case, with participation by a broad range of interest groups.

[20] See, for example, Ex. B-1-1, pages 8 and 9, and Ex. I-1-3. This point is also accepted by APPrO and FRPO in their Reply Arguments.

Moreover, while it is true that the level of TCPL's tolls for future years is unknown, EGD's landed cost analysis establishes that the Marcellus supply that will be transported using the Contract comes at a competitive cost (actually the lowest cost). That is the case regardless of whether one applies: (i) current TCPL tolls; (ii) the new TCPL tolls that have been proposed which shift costs from long-haul to short-haul routes; or (iii) higher TCPL tolls that would use current methodology applied to lower throughput.[21] It is in this light that the Board should consider the position of Board Staff and other intervenors that approval of the cost consequences of the Contract should be rejected, because the costs are uncertain. EGD acknowledges that the cost consequences of the Contract cannot be known for certain at this time, but notes that this is no different from any other long-term contract. What is known, though, is that under any future TCPL toll scenario examined in this proceeding, the landed cost of Marcellus shale gas supply for EGD's system gas customers is competitive with other options (without even taking into account the diversity and security of supply benefits of this new transportation route and supply source).

EGD disagrees with the premise of APPrO's submission that EGD should not commit to other sources of supply except increased long haul TCPL mainline service, simply because non system gas customers may benefit more from increased long haul throughput on TCPL's mainline.[22] EGD has demonstrated that Marcellus supply is a lower cost option for system gas supply, and has made clear that Marcellus supply will not displace any current TCPL mainline contracts.[23] EGD urges the Board to disregard the analysis provided by APPrO to suggest that the lower cost associated with Marcellus supply is offset by increased TCPL mainline tolls. APPrO's analysis is premised on incorrect assumptions. For example, APPrO applies the landed cost "premium" associated with TCPL's proposed lower interim tolls to the "benefit" from additional TCPL mainline volumes at TCPL's current tolls. EGD's calculation of the same question (the impact of contracting for TCPL longhaul, rather than Marcellus supply) leads to an assessment of a net cost, not a net benefit, to system gas customers.[24]

More broadly, EGD submits that the Board need not be influenced in its determination of this Application by concerns raised by several parties about the uncertainty of future TCPL tolls caused by ongoing reductions in throughput on the TCPL mainline. That is not a real issue in this case. As EGD's witness stated in evidence[25], and as other parties have acknowledged[26], EGD cannot solve this problem for TCPL. What is clear in this case is that there will be no decontracting or migration away from TCPL mainline service as a result of EGD contracting for transportation to replace spot gas purchases with Marcellus shale gas. Indeed, the amount of

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[21] EGD's argument in chief on this issue is found at 2 Tr. 33-34; see also 1 Tr. 156-158. Evidence is found at Ex. B-1-1, App. F and Ex. I-1-23.

[22] Reply Argument of APPrO, dated January 24, 2011, at pages 5 to 7. Curiously, APPrO itself acknowledges that in future its members may not be TCPL mainline customers as they may instead acquire their supply at Dawn. – Reply Argument at pages 1 and 2.

[23] In its submission, Board Staff implies that there is "potential decontracting" of TCPL contracts that could accommodate the situation where Marcellus gas is not available. The opposite is true; EGD would acquire more TCPL capacity if it needed to replace Marcellus supply.

[24] The appropriate reference is not Ex. I-2-23 yielding a 7 cents/GJ premium; rather it is 45 cents/GJ as shown at Ex. B-1-1, Appendix F. As a result contracting on the TCPL mainline would result in approximately $5M higher landed costs which would be partially offset by savings to system gas customers of $2M, resulting in a net cost to system gas customers of $3M per year.

[25] 1 Tr. 154.

[26] See, for example, Reply Argument of APPrO, dated January 24, 2001, at page 7.

Marcellus shale gas to be delivered under the Contract represents only one quarter of EGD's current spot (Dawn) purchases.[27] As EGD noted in evidence, it will continue to be a significant customer on TCPL's mainline.[28] Moreover, to the extent that EGD's use of the TCPL mainline continues to be an issue for parties, that can be examined in EGD's annual rate proceedings, during which it must present for approval a forecast of all of its gas supply costs for the subject year, including transportation costs and plans associated with that gas supply.

Several intervenors suggest that the Board ought to consider the allocation of risk between EGD and its ratepayers in respect of any preapproval that is granted. EGD disagrees with the assertion that the Guidelines call on the Board to allocate risk as proposed. While it is true that the Natural Gas Forum Report did indicate that the guidelines to be developed for the pre-approval of long-term contracts "could include" considerations such as "risk allocation"[29], the fact is that the Guidelines that the Board ultimately issued (as well as the Board's Report issued in conjunction with the Guidelines) do not address that matter in any detail. There is no requirement that risks must be borne in some part by a utility's shareholder. Instead, the Guidelines simply require the applicant to identify relevant risks, and to provide information about how these risks will be minimized and allocated between ratepayers, contracting parties and shareholders. In this case, EGD has indicated the reasons why it believes the risks associated with the Contract are reasonable. EGD has also explained the reasons why the risks of this Contract properly rest with its system supply ratepayers.[30] EGD makes no profit or return on its system supply activities. It passes the costs of those activities on to system supply customers without markup. It is appropriate, therefore, that costs associated with the Contract be passed on to those customers in the same fashion. EGD disagrees[31] that it is necessary or appropriate to allocate any negative cost consequences of the Contract (which are not currently expected) to its shareholder.

In conclusion, EGD submits that the Contract is prudent and that preapproval of the cost consequences of the Contract is appropriate and consistent with the Board's Guidelines. For the reasons set out in evidence[32], and in Argument in Chief[33], EGD requests that approval be granted on or before January 28, 2011.

All of which is respectfully submitted this 25th day of January 2011

David Stevens, Aird & Berlis LLP
Counsel to EGD

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[27] Ex. B-1-1, page 6.
[28] Ex. I-1-1 and I-1-9.
[29] Natural Gas Forum Report, at p. 73, found at Tab 1 of Ex. K1.5.
[30] See, for example, 1 Tr. 158 and 167.
[31] In response to the positions taken by CCC and FRPO.
[32] Ex. B-1-1, as supplemented by interrogatory responses and Ex. K2.1.
[33] 2 Tr. 22-39.