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November 18, 2015

RESS, EMAIL & COURIER

Ontario Energy Board
P.O. Box 2319
27th Floor
2300 Yonge Street
Toronto, ON M4P 1E4

Attention: Ms. K. Walli, Board Secretary

Dear Ms. Walli:

Re: Union Gas Limited – Pre-approval of the Cost Consequences of NEXUS Long Term Contract – EB-2015-0166/EB-2015-0175

We are legal counsel for Union Gas Limited ("Union"), applicant in the above-referenced proceeding. Please find enclosed Union's Argument-in-Chief, which has been filed through RESS and served on all parties in the proceeding.

Yours truly,

[Original Signed By]

Charles Keizer

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cc: Colin Schuch, Board Staff
Mark Kitchen, Union Gas
All Intervenors

11229-2124 20491120.1

ONTARIO ENERGY BOARD

IN THE MATTER OF The Ontario Energy Board Act, 1998, S.O. 1998, c.15, Schedule B, and in particular, S. 36 thereof;

AND IN THE MATTER OF an Application by Union Gas Limited for pre-approval of the cost consequences of long-term natural gas transportation contracts with NEXUS Gas Transmission;

AND IN THE MATTER OF an Application by Enbridge Gas Distribution Inc. for pre-approval of the cost consequences of long-term natural gas transportation contracts with NEXUS Gas Transmission.

ARGUMENT-IN-CHIEF OF UNION GAS LIMITED

1. This is Union Gas Limited's ("Union") Argument-in-Chief in EB-2015-0166/EB-2015-0175.

A. Introduction

2. Union has entered into an agreement to contract, subject to certain conditions precedent, for long-term transportation capacity with the NEXUS project commencing November 1, 2017 (the "NEXUS Contract"). This contract will increase security of supply through diversification, enhance liquidity at Dawn, ensure competitive energy prices for Union's customers and create supply competition and opportunities for all Ontario consumers. The NEXUS project is designed to transport supplies of Appalachian gas production, predominantly Utica shale gas production[1], from the single largest and fastest growing supply basin in North America to customers in Ohio, Michigan, and ultimately the Dawn Hub in Ontario. The NEXUS project would create a direct connection between the largest source of natural gas on the continent and Ontario.[2]

[1] Transcript of Oral Hearing, Vol. 2, page 7.

[2] Exhibit A, page 1; Transcript for Oral Hearing, Vol. 1, page 95.

3. The NEXUS Contract is not representative of the ordinary business arrangements or typical transportation contracts in Union's portfolio and creates significant financial risk for Union, such that Union will not proceed with the contract without cost pre-approval. The transfer of cost responsibility to ratepayers is accompanied by significant corresponding benefits to Union's customers and all of Ontario by tying Ontario to a new supply basin. Without Board pre-approval and the assurance that the NEXUS project will move forward, Ontario ratepayers would miss an imminently available opportunity to gain significant access to the Appalachian basin, in particular, supply from Utica production, as well as the accompanying benefits. In the absence of pre-approval of the NEXUS Contract, ratepayers will be left with the incalculable risk and uncertainty as to whether Appalachian shale gas will be available to Ontario ratepayers at comparable quantity with as favourable contractual terms and pricing in the future.[3] Pre-approval of the costs arising from the NEXUS Contract should be granted because:

- In accordance with the Board's Report[4] and the Filing Guidelines for Pre-Approval of Long-Term Natural Gas Supply and/or Upstream Transportation Contracts (the "Guidelines") approved in EB-2008-0280, the NEXUS Contract "supports the development of new natural gas infrastructure", being a new greenfield pipeline that directly connects Dawn to a new gas supply in the Utica basin.

- Being eligible for pre-approval on the basis above, the NEXUS Contract is needed to replace the declining and more costly flows from the Western Canadian Sedimentary Basin ("WCSB").[5]

- Corresponding to the transfer of cost responsibility to the ratepayers are the significant benefits that arise from the contract if pre-approval is granted. Union is entering into the contract on behalf of customers for the benefit of customers.

- As a prudent counterparty and recognizing the cost consequences of pre-approval, Union has negotiated a very favourable agreement which protects ratepayers by fully mitigating risks related to project capital costs and resulting rate impacts, project delays and potential for more favourable terms being negotiated by similarly situated shippers.

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[3] Exhibit A, page 10; Exhibit B.T2.Union.Staff.17, page 4.

[4] Report of the Board, *Draft Filing Guidelines for the Pre-approval of Long-term Natural Gas Supply and/or Upstream Transportation Contracts*, EB-2008-0280 ("Board's Report").

[5] Given that the NEXUS capacity replaces capacity currently under contract on Alliance/Vector and TransCanada pipelines, the NEXUS capacity is not incremental.

- A denial of pre-approval could leave ratepayers without the benefits arising from the NEXUS pipeline and expose ratepayers to the incalculable risk of whether alternate pipeline arrangements would permit access to Appalachian basin at a comparable quantity or cost.

The Project

4. The proposed path for the NEXUS pipeline will consist of two components, the first being a newly-constructed greenfield pipeline and the second being the use of existing infrastructure in Ontario and Michigan. The greenfield portion of the pipeline will extend approximately 250 miles (400 kilometers) from Kensington in eastern Ohio to interconnects with the existing DTE/Michcon ("DTE") pipeline grid at Willow Run in southeastern Michigan.[6] The facilities will encompass four compressor stations and five meter stations. Shippers on the pipeline include Union, Enbridge Gas Distribution Inc. ("Enbridge") and DTE, as well as three producers. The estimated capital cost is $2.019 billion.[7]

5. Although most of the capacity held by shippers will flow on the greenfield portion of NEXUS to the facilities of DTE, Vector, and then to Dawn, Union's arrangement will take a different path.[8] For Union, the volumes contracted on NEXUS will still flow on the same greenfield portion of NEXUS from Ohio to DTE at Willow Run. However, instead of supplies then flowing on DTE facilities to Vector, NEXUS has contracted with DTE to provide transportation on the DTE system to the International Border to complete the NEXUS path. Union will then transport their volumes on the St. Clair pipeline to reach Dawn. This path offers an advantage as it will allow the efficient use of St. Clair to Dawn facilities that already exist and reduce the requirement to construct new pipeline infrastructure in Ontario.[9] Furthermore, it is a lower cost option than the Vector route.[10] The anticipated in-service date for the NEXUS project is November 1, 2017.

[6] Exhibit A, page 14.

[7] Exhibit K1.1, page 2.

[8] See map in Exhibit A, page 16, Figure 3-2.

[9] Exhibit A, page 15; Transcript of Oral Hearing, Vol. 1, page 29.

[10] Exhibit B.T1.Union.LPMA.5, page 1.

6. Attracting more supplies to Dawn is critical to enhancing Dawn's liquidity and overall competitiveness in the surrounding market.[11] To this end, the new physical supplies and additional active market participants brought to Dawn by the NEXUS project will benefit not only Union's sales service customers, but all customers who transact at Dawn including Union's direct purchase customers who rely on arranging their natural gas supply at the Dawn Hub.[12]

The Contract

7. Union participated in a NEXUS non-binding open season which was held between October 15, 2012 and November 30, 2012. Union analyzed its future transportation requirements and chose to bid for an amount of 150,000 Dth/d (158,258 GJ/d), which provided Union with anchor shipper status. Anchor shippers generally receive a rate that is $.015 to $.03 US/Dth lower than other shippers.[13]

8. Union negotiated with NEXUS on an arm's-length basis and in the same manner and with the same individuals as other potential shippers. As a result, Union has negotiated a rate that is known for 15 years and capped by the capital cost tracker, discounted to that of non-anchor shippers, and competitive with the rate received by other anchor shippers on the project. As an anchor shipper, Union's negotiated rate on the greenfield portion is $0.015 US/Dth lower than the greenfield rate offered to Enbridge who is not an anchor shipper.[14] Further, Union notes that the pricing Union will pay to NEXUS for the transportation contract service will be less than regulated posted tolls (which will be approved by FERC).[15]

9. As an anchor shipper, Union has negotiated with NEXUS a rate of $0.77 US/Dth plus fuel, which consists of $0.635 US/Dth for the greenfield portion of the pipeline and $0.135 US/Dth for transportation on the DTE system. Service on the DTE system will be contracted directly by NEXUS to complete the NEXUS path. This rate is subject to a

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[11] Exhibit A, page 4..

[12] Exhibit A, pages 10-12.

[13] Exhibit A, page 28.

[14] Exhibit B.T1.Union.VECC.4, page 1.

[15] Exhibit A, page 45.

capital cost tracker adjustment that will be calculated based on a capital budget of $2.019 billion[16], as compared to the actual costs upon completion of the project. This will result in a maximum adjustment of +/- 15% applied only to the portion of the rate ($0.635 US/Dth) related to the greenfield pipeline construction or related expansion facilities. This will cap the range of the final NEXUS negotiated rate between Kensington and Union St. Clair to be between approximately $0.67 US/Dth[17] and $0.87 US/Dth[18] (plus fuel). These clauses ensure that the rate is defined for the 15 year term as well as provide certainty to the parties should costs be higher than expected and share the benefit should the actual costs be lower than expected.[19]

10. As an anchor shipper, Union has also obtained a Most Favoured Nations ("MFN") clause which provides Union with the ability to amend the Precedent Agreement should another similar shipper negotiate more favourable terms than what Union has received. This ensures Union will be treated fairly and equitably, and that Union is guaranteed the best possible contracting terms available to similar shippers. More specifically, if other similarly situated shippers obtain from NEXUS rate provisions and other terms of service that are more favourable to such other shippers than Union's negotiated rate provisions, Union will be entitled to receive those same rate provisions and terms of service from NEXUS.[20]

11. The NEXUS Contract also contains a number of provisions that are favourable to and that mitigate risks of the ratepayer should the ratepayer assume the responsibility for the costs of the NEXUS Contract through the Board's pre-approval of costs. The mitigation of risks are set out in Section "E" below.

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[16] Exhibit A, Schedule 1, page 67.

[17] The lower end of the toll is calculated by reducing the greenfield toll of $0.635 US/Dth by 15%, and then adding the $0.135 US/Dth to transport supplies on the DTE system ($0.635 * 0.85 + $0.135 = $0.67).

[18] The upper end of the toll is calculated by increasing the greenfield toll of $0.635 US/Dth by 15%, and then adding the $0.135 US/Dth to transport supplies on the DTE system ($0.635 * 1.15 + $0.135 = $0.87).

[19] Exhibit A, page 43.

[20] Exhibit A, Schedule 1, Sections 3(e).

The Cost

12. The annual cost for the NEXUS project tolls is $47.7 million US resulting in a commitment of $715 million in total NEXUS project tolls.[21] This represents approximately 31% of Union's 2017 total projected transportation portfolio costs.[22] The total cost of $715 million is calculated based on the upper end of the NEXUS toll of $0.87 US/Dth over the 15 year term, and could be less depending on the outcome of the capital cost tracker adjustment.[23]

B. The Request for Pre-Approval

13. It is Union's view that the Guidelines issued by the Board in EB-2008-0280 apply to the NEXUS Contract, and that Union's application meets the filing requirements according to the Guidelines.

14. The ambit of the Board's review in this matter is found within the approach set out by the Board's Report and framed by the evidence required by the Guidelines. Together the Board's Report and Guidelines provide the basis on which an application is to be considered in the public interest. In assessing pre-approval, the Board, pursuant to its Guidelines, must balance the opportunity to facilitate new infrastructure and the transfer of associated costs to the ratepayer relative to the need and associated benefits, together with mitigated risks.

15. The Board has previously recognized the role that a LDC plays in encouraging these new, large-scale infrastructure projects:

> "The Board recognized that the enrolment of regulated utilities for such long term arrangements would be a necessary and desirable element in new infrastructure development."[24]

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[21] The total landed cost of gas to Dawn will also include costs for transportation from St. Clair to Dawn at the rate of $0.028 US/Dth/d. Union is not seeking pre-approval of these costs as they are not part of the cost consequences of the NEXUS Contract.

[22] Exhibit B.T1.Union.BOMA.4, page 1.

[23] Exhibit B.T1.Union.VECC.7, page 1.

[24] EB-2010-0300/EB-2010-0333 Decision and Order January 27, 2011, page 7.

16. With respect to the eligibility to seek pre-approval, the Board stated:

> **"**The Board believes that these applications should be limited to those that support the development of new natural gas infrastructure (*e.g.*, new transportation facilities to access new natural gas supply sources). The Board does not believe that the preapproval process for long-term contracts should be used for the utility's normal day-to-day contracting, renewals of existing contracts and other long-term contracts. These contracts should continue to be addressed in the utilities rate application."[25]

17. Furthermore, in considering an application for pre-approval, the Board stated that:

> "The Board also agrees with stakeholders that the process should allow a utility to apply to the Board on a case-by-case basis to pre-approve the cost implications of the long-term contracts (as per section 36(2) of the *Ontario Energy Board Act, 1988*)."[26]

18. In effect, the Board's ambit of review contains two fundamental aspects. First, eligibility criteria related to the nature of the infrastructure and the contract. Second, the consideration once a request is eligible, as to whether the contractual result is needed, does it provide benefits that follow from the cost responsibility assumed by the ratepayer and are the risks mitigated to provide reasonable bounds in respect of those costs. In effect, once establishing eligibility, is the contract in question prudent and appropriate for the ratepayers to accept the cost responsibility.

19. In carrying out such consideration the Board prescribed filing requirements under the Guidelines in the areas of need, benefits, diversity and risk. These elements, together with eligibility, are to be considered on a case-by-case basis. Given the financial obligations resulting from the long-term commitment, Union is requesting contract pre-approval. The Board has recognized the need for utilities to obtain contract pre-approval in this situation, stating that:

> "…regulated utilities whose sourcing decisions are typically and conventionally subject to ex post facto prudence review would be reluctant or unwilling to accept very significant long-term commitments without

[25] Board's Report in EB-2008-0280, page 4.

[26] Board's Report in EB-2008-0280, page 4.

> assurances of costs recovery. The result would be a frustration of demonstrably needed new natural gas infrastructure."[27]

20. Union submits that the NEXUS Contract represents the type of significant long term contract that would warrant pre-approval as the Board has contemplated. In Union's view, its application in the present proceeding meets the filing requirements set out by the Guidelines. The table below highlights certain key requirements in relation to this application.[28]

	NEXUS
Underpins Significant Greenfield Infrastructure	• The required infrastructure is defined. • The NEXUS pipeline project includes 250 miles of NPS 36 greenfield pipe at a cost of approximately $2 billion to provide 1.5 Bcf/d transport to the market.
Volume	• NEXUS represents a more significant volume of 158,258 GJ/d which represents approximately one third of Union's overall gas supply portfolio. • This does not represent typical day to day contracting.
Cost of Contract	• Tolls are known and are fixed in the contract terms, which mitigates the risk of pre-approval to ratepayers.
Infrastructure Project	• Project is defined and the cost to Union (shipper) is known and capped.
Contract or PA	• PA has been signed.
Magnitude of Cost Commitment	• Significant financial commitment of more than $700 million over the 15 year term of the agreement.

21. The NEXUS project is new greenfield natural gas infrastructure that will directly link Dawn to a new natural gas supply basin. That portion of the NEXUS pipeline from Kensington to Willow Run is entirely a greenfield development. For purpose of cost efficiency and reduced environmental impact, the NEXUS project includes transportation on DTE's pipeline from Willow Run to the St. Clair Pipeline.[29] Notwithstanding that there is a contracted portion of existing pipe, the greenfield nature of the NEXUS project

[27] EB-2010-0300/EB-2010-0333 Decision and Order January 27, 2011, page 7.

[28] Exhibit B.T1.Union.Staff.2, page 3. Also see Exhibit B.T1.Union.Energy Probe.1, page 1 for a detailed table showing the information requested in each part of the Guidelines and the corresponding references in Union's evidence.

[29] Transcript of Oral Hearing, Vol. 1, page 29.

is not diminished since the project cannot occur without the greenfield portion of the pipeline.

22. Furthermore, the pipeline enables the direct connection of Dawn to a new source supply. Given that the Kensington gas processing plant is located in the heart of the Utica production area, the primary source for the NEXUS pipeline is from Utica, which is a new supply source that had little to no production when Union bid into the NEXUS open season in 2012. At that time, Utica producers were in the very early stages of development activities, including drilling test wells to assess the appropriate drilling locations.[30] Recent findings in relation to this brand new supply source have far exceeded initial expectations. For instance, some producers in the Utica basin have developed wells with record-breaking productions in their portfolio. In light of this knowledge, placing the start of the NEXUS pipeline at Kensington has proved to be a prudent decision that will provide significant access to a new supply basin and an attractive place to purchase gas.[31]

23. Without the assurance provided by contract pre-approval, Union will not commit to a contract of this magnitude. The NEXUS Contract requires a significant long term commitment by Union (approximately $715 million over a 15 year term) and represents 31% of Union's annual upstream portfolio.[32] The long term commitment required by the NEXUS Contract does not represent typical day-to-day contracting. Without pre-approval of the associated cost consequences, committing to a transportation contract for one-third of Union's overall supply portfolio over 15 years would expose Union to a unusually large financial risk which the shareholders are not willing to bear. This is especially true since Union passes the cost of the gas and transportation on without a return to offset the corresponding risk.[33] Further, Union is entering into this contract on behalf of its customers who will receive the resulting benefits and thus should shoulder the corresponding cost consequences, which are known and defined for the term of the

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[30] Transcript of Oral Hearing, Vol. 2, pages 7, 85 and 112.
[31] Transcript of Oral Hearing, Vol. 2, pages 85 and 86.
[32] Exhibit B.T1.Union.Staff.1, page 1.
[33] Transcript of Oral Hearing, Vol. 2, page 2.

contract. Recognizing the reluctance of utilities to take on long-term contracts of significant volumes, the Board has established the pre-approval process to provide assurance of recovery of costs that support new infrastructure and new supply, such as the costs at issue in this proceeding. If the Board decides pre-approval is appropriate, then the cost consequences are effectively accepted as being the toll that ratepayers will pay. This treatment is no different than the costs of other upstream transportation contracts in Union's portfolio, which costs are passed onto ratepayers.[34]

C. Demonstration of Need

24. In conjunction with eligibility, the Board must consider prudence as part of the Board's multi-faceted pre-approval guidelines, and assess the need for the contractual commitment. In this regard, at the time of the project announcement, Union recognized NEXUS as an opportunity to benefit from the changing North American supply dynamics and to[35]:

- replace declining flows from the WCSB by gaining access to abundant, economic Appalachian shale supplies,
- increase the diversity and security of supply for Union's customers,
- reduce price volatility of the Dawn Hub, and
- bring major benefits to the rest of Ontario.

Shift in North American Natural Gas Markets

25. North American natural gas markets have experienced and are expected to continue to experience dramatic changes. Production from conventional, mature North American natural gas basins is in decline while production from shale gas formations continues to exceed expectations. While natural gas reserves still exist in mature natural gas basins, the economics of natural gas production favour shale gas and tight gas formations.[36]

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[34] Transcripts of Oral Hearing, Vol. 2, page 22; Vol. 1, page 75.

[35] Exhibit A, page 18.

[36] Exhibit A, page 6; Schedule 3 - NEXUS Market Study Report, Sussex Economic Advisors, LLC, Figure 3.3, page 17.

26. The Appalachian basin is the single largest and fastest growing production region of natural gas in North America.[37] The basin is estimated to grow to production levels of 40 PJ/d by 2035[38], and will exceed the entire WCSB at its peak production of 18 PJ/d by the end of 2015[39]. Ontario is very fortunate to be in close proximity to this supply basin. However, there is currently no direct pipeline route into Dawn from the Appalachian basin. The NEXUS project, if completed, will provide that connection and help to enhance security of supply through diversification, for all Ontario market participants.[40]

27. The majority of Ontario's natural gas supply needs for the past five decades have been met through the large resources of the WCSB. Natural gas from the WCSB was supplied to Ontario on the TransCanada Mainline either from Empress across northern Ontario or from pipelines passing through the northern US and eventually back into Canada to Dawn. In parallel with the emergence of shale gas supplies, there has been a pattern of declining flows from conventional western supply sources, including the WCSB, and corresponding de-contracting of long-haul transportation from these sources. Directionally, these changes result in less supply arriving at Dawn through existing pipeline infrastructure and have impacted the diversity and liquidity of the Dawn Hub. The continuation of these flow changes represents a significant risk to all natural gas consumers and market participants in Ontario.[41]

28. To evaluate various upstream pipeline options, Union has consistently used landed cost analysis combining the impact of commodity costs and cost of transportation to Ontario. Although the landed costs change from year to year, the two paths that continually produce the highest landed cost to Union are the Alliance and TransCanada long haul paths accessing WCSB supplies.[42]

[37] Exhibit A, page 7.
[38] Exhibit A, Schedule 3 - NEXUS Market Study Report, Sussex Economic Advisors, LLC, page 32.
[39] Exhibit A, page 22; Transcript of Oral Hearing, Vol. 1, pages 36-37.
[40] Exhibit A, page 22.
[41] Exhibit A, page 10.
[42] Exhibit B.T1.Union.Energy Probe.5, pages 1-2.

29. Without access to the abundant and affordable supplies in the Appalachian basin, gas prices at Dawn, and therefore energy prices in Ontario, would be disconnected from the continent-wide lower costs resulting from these emerging supplies. In other words, without a significant direct connection to the Appalachian basin, the cost of energy in Ontario would not benefit from the moderating effect of the low-priced natural gas in the Appalachian basin available to neighbouring areas.[43]

Benefits of Supply

30. Having a new greenfield supply option available will enhance diversity and security of supplies to the Dawn Hub, reduce natural gas prices and volatility and bring benefits to all of Ontario.[44]

31. By Union entering into a firm transportation contract, and therefore supporting the NEXUS project, Union customers and all of Ontario will see multiple significant benefits including[45]:

- Providing a direct pipeline route between the Appalachian basin and Ontario that will benefit Union's sales service customers by significantly increasing the security and diversity of Union's transportation and supply portfolio. Access to these basins will greatly reduce Union's reliance on WCSB supplies, and will offset the declining volumes arriving at Dawn from these traditional western sources.

- The NEXUS capacity will allow Union to displace WCSB supplies that are becoming less economic over time. WCSB basis differentials, once they are combined with the cost of transportation to Ontario, have become less favourable than Appalachian supplies due to rise in demands in Western Canada and the abundance of natural gas supplies located in the Appalachian basin. Additional diversity will allow Union to have options as to where it sources natural gas supplies in future market shifts or as prices between supply basins change. Given the location of the NEXUS pipeline, the connections at Kensington and access to other pipelines that are directly connected at the extension of NEXUS at Clarington provide tremendous diversity and security of supply. In addition, the NEXUS pipeline can access multiple supply points between Kensington and Dawn, including those on the DTE system (such as Willow Run).[46]

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[43] Exhibit A, page 10.

[44] Exhibit A, page 23.

[45] Exhibit A, pages 10-12.

[46] Exhibit B.T2.Union.Staff.17, page 3; Exhibit B.T4.Union.FRPO.20, page 1.

- Introducing new pipeline infrastructure and enhancing supply at Dawn will also benefit Ontario and other market participants at Dawn by adding another transportation option and enhancing the liquidity of the Dawn Hub.[47] Dawn liquidity is supported by adding additional physical supplies, as well as additional active market participants. The Board has previously concluded that it "…is in the public interest to maintain and enhance the depth and liquidity of the market at the Dawn Hub as a means of facilitating competition".[48] This will be of benefit to not only Union's sales service customers as noted above, but all direct purchase customers, who rely on arranging their natural gas supply at the Dawn Hub.

- Connecting Ontario to growing, affordably priced Appalachian basin will help to lower natural gas prices and enhance energy pricing stability in Ontario. Reduced price and reduced long term price volatility is a major benefit to all market participants, including electricity purchasers who rely on supply arrangements made at the Dawn Hub. For example, in the winter of 2013-2014, Dawn Hub and Chicago Hub experienced significant spikes in pricing at around the same time, which was largely due to a lack of pipeline capacity to move gas to those hubs.[49] With additional pipelines connecting Dawn to the Utica basin, the shift in connectivity to a rapidly growing supply source is expected to moderate volatility in price at Dawn.[50] The ability to transact at Kensington in the heart of a robust production area will lessen the extent to which price is driven by constraints in pipeline capacity, and help to mitigate the risk of similar pricing spikes occurring in the future.

32. These benefits are further supported by the Sussex Report, which states:

> "The NEXUS benefits (*e.g.*, reliability, diversity, and price stability) increase the flexibility of the Union and Enbridge natural gas supply portfolios; thus providing additional options to the Ontario LDCs to manage natural gas supply and transportation costs, improve overall reliability, and provide increased priced stability."[51]

33. With the increased diversity of these new supplies and the replacement of the WCSB supplies within the Union portfolio. The resulting savings will help to make Ontario more competitive with neighbouring jurisdictions. Exposure to the Appalachian basin will also provide benefits to the overall stability of natural gas prices in Ontario.[52] As

[47] Based on the Platts ranking, the Dawn Hub price index has been, on average, a Tier 1 price index (*i.e.*, the highest category for traded volumes and number of deals) over the 2009-2015 time period reviewed by Sussex. For comparison purposes, Niagara was ranked as a Tier 2 or Tier 3 price index over the same period (see Exhibit B.T1.Union.APPrO.5, page 5).

[48] EB-2005-0551 NGEIR Decision with Reasons November 7, 2006, page 45.

[49] Transcript of Oral Hearing, Vol. 2, page 128.

[50] Transcript of Oral Hearing, Vol. 1, page 85.

[51] Exhibit A, Schedule 3 - NEXUS Market Study Report, Sussex Economic Advisors, LLC, page 4.

[52] Exhibit A, page 27.

stated in the Sussex Report, "direct access to the Marcellus and Utica supply basins will provide the Ontario LDCs with increased price diversity. Specifically, the Marcellus/Utica gas supply basins will have certain price signals and price indices not previously accessed by the Ontario LDCs, thus increasing overall price diversity and providing more stability with respect to natural gas costs for Ontario LDC customers."[53]

34. The NEXUS project provides the opportunity to introduce new infrastructure that will provide much-needed access to Appalachian shale supplies and will deliver these supplies into Dawn, helping to enhance and grow the diversity and liquidity of the Dawn Hub.[54] This will also allow Ontario to diversify its current reliance on WCSB as a source of natural gas, which is a significant benefit to all natural gas consumers in Ontario. As indicated above and stated in the Sussex Report, the additional transportation infrastructure and supply diversity will benefit all market participants in Ontario. Given the declining Vector volumes and the decrease in natural gas flowing from the WCSB to the Ontario market as well as the increasing take away capacity from Dawn, Ontario needs projects from the growing Appalachian basin, such as NEXUS, to enhance supply and liquidity. [55]

Landed Costs

35. Sussex reviewed the landed costs analysis performed by Union. One of the main conclusions of the Sussex Report is that although the landed cost analysis will be subject to change over time, it is a reasonable analysis that complements the many other benefits of the project.

36. Union has performed two distinct landed cost analyses – one in January 2014 prior to signing the initial Precedent Agreement with NEXUS, and a second in January 2015 prior to signing a renegotiated Precedent Agreement with updated terms. Each of the landed

[53] Exhibit A, Schedule 3 - NEXUS Market Study Report, Sussex Economic Advisors, LLC, page 37.
[54] Transcript of Oral Hearing, Vol. 1, page 53.
[55] Exhibit A, pages 4-5.

cost analyses was performed with different assumptions based on the information known at the time.[56]

37. There is a significant difference between the landed cost of the NEXUS supply compared to the Alliance and TransCanada long-haul supplies that it replaces within Union's supply portfolio.[57] For example, under a conservative comparison of the upper-end of the NEXUS landed cost (assuming the full 15% increase of the capital cost tracker) versus the Alliance supplies, there is a saving of $0.51/GJ over the 15 year term. For the TransCanada-based supplies, the savings on the NEXUS path are $1.18/GJ over the term. Based on the landed cost analysis, and assuming NEXUS supplies replace volumes on the discussed paths, Union estimates potential cost savings of over $700 million[58] over the term of the contract to sales service customers compared to current contracted supplies. When the landed cost differential between NEXUS versus Dawn/St. Clair is considered, the cost savings are about $39 million a year or $589 million over the term of the NEXUS Contract.[59]

38. Overall, the landed cost of NEXUS supplies is very similar to Rover, and is competitive or lower cost than other paths available in Union's portfolio.[60]

D. Demonstration of Contract Diversity

39. In its Decision regarding Union's Parkway Projects and Enbridge's GTA Project, the Board reiterated this position: "[i]t is the Board's view that while uncertainties exist for all supply sources in terms of future cost and availability, it is widely acknowledged, including by this Board in prior decisions, that supply diversification enhances reliability and brings cost benefits through enhanced competition".[61]

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[56] Exhibit A, page 38; Transcript of Oral Hearing, Vol. 2, page 26.

[57] Exhibit A, page 40, Figure 5-5.

[58] (Alliance/Vector vs. NEXUS plus 15%) times by Alliance/Vector volume being reduced plus (TCPL long haul vs. NEXUS plus 15%) times by volume being shifted over 15 years = (($9.00-$8.49) *85,000GJ/day)) + (($9.67-$8.49)*73,000GJ./day)) * 365 *15 years = ($43,000/day * 365 *15) +($86,000/day * 365 *15) = ~$708 million

[59] Transcript of Oral Hearing, Vol. 2, page 67; Undertaking J2.3.

[60] Exhibit A, page 41.

[61] EB-2012-0451/EB-2012-0433/EB-2013-0074 Decision January 30, 2014, pages 23-24.

40. There is currently a lack of pipeline and supply diversity in the 2015 Union North sales service and bundled direct purchase portfolio due to its 100% reliance on WCSB supplies delivered to Ontario via TransCanada long-haul transportation.[62] This lack of diversity introduces risks around security of supply, and leaves customers in Union North exposed to the pricing characteristics and potential volatility of a single basin.[63]

41. In order to address the lack of diversity in the north, Union has worked to facilitate increased diversity of supply options for these customers in future years through the TransCanada Settlement Agreement by converting TransCanada long-haul transportation from Empress into short-haul transportation from Dawn. These conversions from long-haul to short-haul were addressed in Union's 2015 and 2016 Dawn Parkway Expansion applications which were subsequently approved by the Board.[64] Once these conversions are completed, customers in Union North will have the ability to access supplies at Dawn, including those from upstream transportation projects such as NEXUS.[65]

42. The added diversity will result in the reliance on WCSB supplies in the Union North dropping from 100% to 48%.[66] Increased diversity includes the addition of 26% of the portfolio from Appalachian supplies facilitated through the NEXUS pipeline.[67]

43. The Union South supply portfolio is currently much more diverse than Union North; however, there is still a significant reliance on supplies directly from the WCSB. Approximately 36% of Union South is sourced from the WCSB, with an additional 31% sourced from Chicago. As the supplies arriving from these traditional western sources decline, Union needs to find replacement capacity upstream of Dawn to deliver new gas supplies and ensure the continued liquidity and diversity at the Dawn Hub.[68]

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[62] Transcript of Oral Hearing, Vol. 1, page 55.

[63] Exhibit A, page 20.

[64] The 2015 projects include the Brantford-Kirkwall/Parkway D Project (EB-2013-0074) and Parkway West Project (EB-2012-0433). The 2016 project is the Dawn Parkway 2016 System Expansion Project (EB-2014-0261).

[65] Exhibit A, page 20.

[66] Exhibit A, page 29, Figure 5-1; page 20, Figure 4-1; Transcript of Oral Hearing, Vol.1, page 55.

[67] Exhibit A, page 29.

[68] Exhibit A, page 21; Transcript of Oral Hearing, Vol. 1, page 54.

44. The Union South portfolio will benefit from NEXUS capacity as upstream transportation reductions on Alliance/Vector and TransCanada take place. By accessing a portion of the NEXUS capacity, the Union South portfolio will benefit from additional diversity and the potential for cost savings by introducing an abundant, affordably priced source of natural gas in close proximity to Ontario. This increased diversity will result in the reliance on TransCanada WCSB supplies dropping from 21% to 3%, and the portfolio would then source 30% from the Appalachian basin.[69] The diverse Union South portfolio still has 23% sourced from Chicago, as well as 17% from Dawn, both of which would include a level of supplies from the WCSB.[70]

45. In relation to the entire Union transportation portfolio (*i.e.* Union North and Union South), the NEXUS capacity will add Appalachian basin supplies and will reduce the overall reliance on WCSB from 53% in January 2015 down to 19% in January 2018.[71]

E. Risk Assessment

46. If pre-approval is granted, ratepayers not only will be provided the benefits stemming from the contract but also will benefit from measures negotiated by Union to mitigate certain key contract risks. Such mitigation measures include:

- a negotiated toll that is known and defined for the 15 year term, and subject to a capital cost tracker mechanism to cap the toll and realize toll savings where capital costs are less than target;
- the ability to withdraw from the project and not be subject to any pre-service project costs if the NEXUS project is delayed beyond November 1, 2018 or cancelled;
- the ability to choose the reservation rate instead of the negotiated toll after the project has been completed; and
- a MFN clause allowing Union to receive more favourable terms that may be negotiated by a similar shipper.

[69] Exhibit A, page 31, Figure 5-2; page 21, Figure 4-2.

[70] Exhibit A, page 30.

[71] Exhibit A, pages 31-32; page 32, Figures 5-3 and 5-4.

These measures mitigate the risk, limit and define the costs under the contract and represent very favourable commercial terms.

Project Capital Costs

Risk Identification

47. Any major pipeline infrastructure project may experience capital cost variances due to a number of factors. If not considered as part of negotiating a rate, there is risk that these cost overruns will result in a toll that may no longer be economical for the shipper.[72]

Risk Mitigation

48. Union has negotiated a fixed rate with NEXUS that includes a known capital cost tracker adjustment mechanism. Union's rate of $0.77 US/Dth will be adjusted to take into account either higher or lower capital costs than anticipated. Union, and other similarly situated shippers, negotiated a limit of +/-15% on the capital cost tracker adjustment that will only be applied to $0.635 US/Dth of the total rate of $0.77 US/Dth (*i.e.* the greenfield and expansion portion of the rate). The baseline capital budget used to calculate the tracker is $2.019 billion. Having a capital cost tracker allows the ratepayer, if pre-approval is granted, to participate in any cost savings realized while limiting any cost overrun potential. This tracker defines the range of final rates of the service and allows for a landed cost analysis to be performed with certainty. For Union, this tracker will limit the final rate to be within the range of $0.67US/Dth to $0.87 US/Dth.[73] For the purposes of determining the total transportation costs and related gas cost savings over the term of the NEXUS Contract, Union has used the upper end of this range to provide conservative calculations.

[72] Exhibit A, page 46.
[73] Exhibit A, page 47.

Project Delays or Cancellation

Risk Identification

49. Any major pipeline infrastructure project may experience delays, or, in extreme cases, cancellation, due to a number of factors. If this were to occur, the shipper would experience a shortfall of transportation capacity in their portfolio.[74]

Risk Mitigation

50. Union will mitigate any delays in construction by leveraging the diverse upstream transportation and supply options that exist at Dawn. By entering into short-term transportation and/or supply commitments, Union is able to address any gaps in the portfolio that are due to a delayed in-service date for NEXUS for a short period of time.[75]

51. Should the NEXUS project be delayed beyond November 1, 2018 or cancelled, Union can withdraw from the project and will not be liable for any pre-service project costs. Union would analyze its portfolio and replace the anticipated NEXUS transportation capacity with other upstream transportation options that are available at the time.[76]

Demand Risks

Risk Identification

52. Entering into a transportation contract requires certain assumptions around the demands that will support the requirements for the contracted capacity. This is especially true of long-term commitments required to support a new infrastructure project such as NEXUS. If forecasted demands do not materialize, the shipper is at risk of holding excess capacity within its portfolio.[77]

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[74] Exhibit A, page 47.
[75] Exhibit A, page 47.
[76] Exhibit A, page 47.
[77] Exhibit A, page 48.

Risk Mitigation

53. To ensure that any unplanned changes in demands do not jeopardize the decision to support NEXUS, Union has not deviated from its normal gas supply planning practices that have been validated by the Board in past proceedings.[78]

54. As such, entering into a long-term contract with NEXUS does not increase Union's exposure to decreases in demand. Union's current Gas Supply Plan has identified the need for upstream transportation capacity in excess of 150,000 Dth/d for November 1, 2017. The contracted capacity on the NEXUS pipeline will address this need, while still leaving appropriate flexibility within Union's upstream portfolio should there be any fluctuations in customer demand. Should natural gas demands decline in the Union franchise area, there are multiple opportunities to leverage existing flexibility embedded within the portfolio to rebalance the upstream transportation and gas supply portfolios.[79] Given that the NEXUS capacity is about one-third of Union's overall systems capability requirement, the remaining two-thirds are uncommitted or short-term commitments. This will allow Union to address any change in demand, including as a result of Demand Side Management or Cap and Trade initiatives.[80]

Supply Risks

Risk Identification

55. In order to support an infrastructure build, pipeline projects require customers to contract for capacity for a long period of time. In the case of NEXUS, the requirement for anchor shippers was a 15-year commitment. There is risk that supplies available to be transported through the newly-constructed infrastructure would not be available for the entire length of the term.[81]

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[78] Exhibit A, page 48.

[79] Exhibit A, page 48; Transcript of Oral Hearing, Vol. 1, page 63.

[80] Transcript of Oral Hearing, Vol. 2, pages 99-100.

[81] Exhibit A, page 49.

Risk Mitigation

56. When evaluating the long-term commitment required to support the NEXUS project, Union also evaluated its ability to access adequate supplies for the duration of the contract. Union has accessed various resources including the Sussex Report to gauge the level of supply available in the Appalachian basin and available to the NEXUS project.[82]

57. The production estimates for the Appalachian basin are forecasted to exceed 18 PJ/d in 2015 and will continue to increase steadily for the duration of the 15-year NEXUS Contract period referenced in the Sussex Report. These production levels represent sufficient supply production for the duration of the NEXUS Contract's primary term.[83]

58. Union has also been in discussions with these potential suppliers since early 2013 and has conducted numerous supplier meetings and attended relevant industry conferences. Many of these suppliers are new to Union as they are predominantly sourcing their supply from the Appalachian basin.[84]

59. Union has also issued an Expression of Interest for a portion of the supply necessary once the NEXUS project is completed and in service. The goal of this Expression of Interest and subsequent RFP is to understand and potentially secure up to 50,000 Dth/d (52,753 GJ/d) of supply at Kensington starting November 1, 2017 (or the date when NEXUS is in service, whichever is later). Union will evaluate each and every bid on its own merits and determine the successful bidders within the prescribed timelines that accompany the RFP.[85]

TransCanada Mainline Risk

Risk Identification

60. As mentioned previously, natural gas transported to Dawn via NEXUS will replace supplies that will no longer be transported using TransCanada long-haul transportation

[82] Exhibit A, page 49.
[83] Exhibit A, page 49.
[84] Exhibit A, page 50.
[85] Exhibit A, page 51.

from the WCSB. Historically, the trend of shippers de-contracting TransCanada long-haul transportation resulted in concerns as to the economic viability of the Mainline system, which was the subject of the NEB RH-001-2014 settlement hearing.[86]

Risk Mitigation

61. All impacts resulting from Union (and the other eastern LDCs) turning back TransCanada long-haul transportation have already been contemplated in the RH-001-2014 settlement agreement that was approved by the NEB in December, 2014. The financial impacts of those decisions have been incorporated into TransCanada's approved tolls. The NEXUS capacity will simply replace these supplies that would have otherwise been purchased at Dawn, and have no incremental impact to the TransCanada Mainline system.[87] The rates established pursuant to the settlement agreement have been in place since 2014, so there is no further impact on mainline tolls for Union Northern customers until 2030.[88]

Risk – If No Pre-Approval

62. In a scenario where Union was unable to obtain contract pre-approval and to commit as an anchor shipper under the contract as proposed, there is significant risk that producers, who are also anchor shippers on the NEXUS pipeline, may interpret Union's action as a lack of endorsement of Dawn as an important market hub and an indication of a weak market for their supplies at Dawn.[89] In this regard, it is important to note that the transportation capacity contracted by Union and Enbridge on the NEXUS pipeline to Dawn represents approximately 273 TJ/d out of a total of approximately 800 TJ/d (*i.e.*, one-third). If Union and Enbridge did not contract, the remaining shippers, all or nearly all of whom are expected to be producers or marketers on behalf of producers, would be left to shoulder more of the cost of service of the pipeline, leading to a rise in tolls. This negative economic pressure would create a challenge for the project, the remaining shippers, including anchor shippers, and the markets which the NEXUS pipeline would

[86] Exhibit A, page 52.
[87] Exhibit A, page 52.
[88] Transcript of Oral Hearing, Vol.1, pages 60-61.
[89] Exhibit A, page 4.

serve.[90] Producers could reconsider their participation on the project, or their plans to bring supplies to Dawn, creating the risk that the NEXUS project would not proceed as planned.[91]

63. The foregoing is against the back drop that many of the Utica producers have options to go into other markets, and are cautious with respect to entering new markets such as Dawn.[92] Many producers without affiliated Canadian entities or significant Canadian business (such as in the WCSB) have also taken a cautious approach to doing business or initiating business in Canada. Union has worked closely with Utica producers (including the NEXUS shippers) to facilitate their understanding of the Dawn market and the requirements of doing business in Canada. If Union did not remain an anchor shipper then this would undoubtedly be viewed as a negative signal and a lack of endorsement.[93] Without pre-approval and the assurance that the NEXUS project will move forward, the Dawn Hub and Ontario consumers would miss an opportunity to gain significant access to Utica production as well as the accompanying benefits of increased choice, market liquidity at Dawn, and diversity and security of supply.[94]

64. There is significant market competition for the supply available from the growing Utica Appalachian basin. Numerous projects are already in progress to take these supplies to other markets, including the Gulf Coast, U.S. Midwest, U.S. Northeast, and U.S. Southeast. It is critical for Union and Ontario consumers that contractual commitments to the NEXUS project be made and supported to ensure Ontario and those market participants that access supplies at Dawn are able to gain access to these supplies in a similar fashion to the other markets in the eastern half of North America. This will ensure Ontario and Dawn stay well connected to new affordable and competitively priced North American supplies.[95]

[90] Exhibit B.T1.Union.Energy Probe.3, page 2.
[91] Exhibit A, page 4.
[92] Transcript of Oral Hearing, Vol. 1, page 96.
[93] Exhibit B.T1.Union.Energy Probe.3, page 2.
[94] Exhibit B.T2.Union.Staff.17, page 4.
[95] Exhibit A, page 17.

65. Without the NEXUS Contract there is no assurance that natural gas from the Appalachian basin will be available to Dawn from another source on comparable terms. The ratepayers are then exposed to an incalculable risk as to the nature of such supply and its relative benefits and costs.

F. Other Connections

66. It is Union's understanding that with the current commitments, the upstream pipelines that provide supply to Niagara and that are planned for 2015-2016 are largely sold out[96] and significant incremental infrastructure would be required to import any substantial additional gas from the Appalachian basin into Ontario (beyond 2015/2016) at Niagara or Chippawa. Union expects that significant incremental infrastructure would also be required on the TransCanada system to move natural gas from Niagara further into Ontario (beyond the current 2015/2016 volume of 1.4TJ/d).[97] By 2017, Enbridge and Union will have contracted for approximately 273 TJ/d of NEXUS pipeline capacity into Dawn and will combine to bring over 221 TJ/d from Niagara into Ontario. In this regard, both Marcellus volumes through predominantly Utica volumes through Dawn (via Rover and/or NEXUS) are being supported, which will help offset the decreased volumes from WCSB via TransCanada and Alliance/Vector.[98] This will provide further diversity for Ontario and have some balance in its access to Marcellus and Utica production.

67. Union first committed to NEXUS in 2012 when it entered the open season, and was in the final stages of negotiations when the Rover pipeline project was announced. At the time Rover discussed their project with Union, the Rover project already had sufficient commitment from suppliers to move forward. Relative to NEXUS, Rover's minimum contract term was longer (20 years)[99] and the MFN threshold was much higher[100]. Whereas NEXUS planned to use existing infrastructure on DTE, Vector and Union, Rover required substantially more greenfield pipeline capacity to be built in order to get

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[96] Exhibit K2.2 shows total upstream capacity of 1.2 PJ at Niagara. Undertaking J2.2, Attachment 1 shows that nearly all of that capacity is contracted.

[97] Exhibit B.T2.Union.Staff.17, page 2.

[98] Exhibit B.T2.Union.Staff.17, page 3.

[99] Exhibit B.T1.Union.FRPO.6, page 1.

[100] Exhibit B.T1.Union.FRPO.4, page 1.

to Dawn. Also, the Rover capital cost was over double that of NEXUS. As a result of these factors, Union chose to retain its volumes on the NEXUS project as it meets the needs of its customers and would provide the best chance for success. Had Union split volumes between the projects, this may have put the NEXUS project at risk.[101] While NEXUS and Rover are being developed in parallel, the in-service date for Rover has recently been delayed for six months or more.[102] Moreover, it is Union's understanding that shippers on the Rover pipeline may reduce their contracted Maximum Daily Quantity if the developer fails to meet certain deadlines[103], which may present a further risk to the development of that project as planned.

G. Conclusion

68. For the reasons set out in the application and this argument-in-chief, Union submits that it has established a case for pre-approval of the cost consequences of the NEXUS Contract, which is required to support the development of new greenfield natural gas infrastructure that will directly link Ontario and more specifically, Dawn, to a new natural gas supply basin. Without access to the abundant and affordable supplies in the Appalachian basin, gas prices at Dawn, and therefore energy prices in Ontario, would be disconnected from the continent-wide lower costs resulting from these emerging supplies. In other words, without a significant direct connection to the Appalachian basin, the cost of energy in Ontario would not benefit from the moderating effect of the low-priced natural gas in the Appalachian basin available to neighbouring areas. It is Union's view that it has satisfied the eligibility requirements for contract pre-approval pursuant to the Board's Guidelines in EB-2008-0280. Further, Union has demonstrated the various benefits of the NEXUS Contract, including increasing security of supply through diversification, maintaining liquidity at Dawn, ensuring competitive energy prices for Union's customers, and creating supply competition and opportunities for all Ontario consumers. It has also shown how the NEXUS Contract fits into and complements Union's overall portfolio and how Union has taken diligent steps to mitigate ratepayer risks. Given the significant

[101] Exhibit B.T1.Union.FRPO.6, page 1.
[102] Transcript of Oral Hearing, Vol. 2, page 6.
[103] Transcript of Oral Hearing, Vol. 3, pages 89-90.

magnitude and duration of financial obligations stemming from this contract, Board pre-approval would provide the necessary assurance of cost recovery to ensure that Ontario would gain significant access to Utica production and receive the accompanying benefits.

All of which is respectfully submitted, this 18th day of November, 2015

UNION GAS LIMITED
By its counsel Torys LLP

[Original Signed By]

Charles Keizer