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A Spectra Energy Company

Guidelines for the Pre-Approval of Long-Term Supply and/or Upstream Transportation Contracts (“LTC Guidelines”) EB-2008-0280

Union Gas
Stakeholder Consultation
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Two Types of Long-Term Contracts

- 1. Supply Contracts**
- 2. Upstream Transportation Contracts**

1. Supply Contracts

- The Board determined in its' NGF Policy Paper that it “is not in favour of new long-term utility supply contracts at this time”.
- In EB-2007-0606 the Board reviewed Union's Risk Management program and concluded that “there is no material net benefit for customers” to reduce price volatility through hedging.
- Given these comments, it is Union's view that there is currently no support for the LDC to acquire long-term supply.
- Therefore, developing guidelines for pre-approval of long-term supply contracts does not appear to be required.
- It may be practical to establish a common pre-approval process for LTC that includes both transportation and supply, should the supply situation change (eg LNG).

2. Upstream Transportation Contracts

North American Supply Dynamics are Changing...

- Unconventional gas (coal bed methane, shale gas and gas from tight formations) has boosted production in N.A. and will continue to contribute significantly over the coming decades.
- N.A. is in the midst of a surge in pipeline construction that is expanding the transmission grid to connect existing markets to these new sources of gas supply. Long-term contracting is required by shippers to support these projects.
- As a result, gas flows are changing and new supplies are available to move directly to markets in the Eastern United States and into Michigan and Ontario.
- Gas flowing through these new pipelines is projected to offset reduced exports from the WCSB due to declining production and Alberta's increasing demand for gas.

2. Upstream Transportation Contracts (cont'd)

The Impact on the Ontario Market...

Supply

- Historically, the dominant source of Ontario's gas supply has been the WCSB, transported on TCPL's system.
- Increasingly new sources of supply are available to Ontario, transported on alternative pipelines directly connected to south-western Ontario.
- Ontario must continue to be well-connected to the emerging supply basins. The LDCs play an important role in supporting these projects to Ontario.

Demand

- Demand will stay strong.
 - ICF projects that about 2/3 of the growth in Ontario's demand will occur in the power generation sector.
 - ICF predicts continued growth in the residential, commercial and industrial sectors.

2. Upstream Transportation Contracts (cont'd)

Principles to Consider

- A diversified gas transportation portfolio provides value to Ontario consumers through price, term and supply basin diversity.
- LDCs have an important role to play in supporting new long-term transportation infrastructure to Ontario.
- Long-term transportation contracts entered into by LDCs should be reviewed for approval at the time the contractual commitment is made, not at the time of cost recovery.
- Subject to a prudence review, LDC shareholders should bear no risk of cost disallowance given that LDCs make no profit on commodity and associated transportation.

2. Upstream Transportation Contracts (cont'd)

Long-term contracts are required to support new infrastructure to Ontario.

Benefits of new infrastructure:

- Diversity of supply from various basins improves security of supply and decreases price volatility for consumers
- Supports all consumers including those on direct purchase who will also see improved security of supply and reduced price volatility
- Improves competition among rival pipelines and encourages service improvements

2. Upstream Transportation Contracts (cont'd)

Risks to consumers of long-term contracting:

Construction & Operational Risks

- Cost escalations, delays or reliability issues on new construction
- Gas interchangeability and quality issues

Commercial Risks

- Long-term demand-charge obligations viewed as debt on the LDCs books
- Competitive and credit-worthy commodity providers

Long-term Forecasting Risks

- Uncertainty over future demand or actual landed costs
- Underperformance of the basin relative to production forecasts

2. Upstream Transportation Contracts (cont'd)

Why the LDC?

- Credit worthy counter party for pipelines
- Long-term commitment to sales service role
- No impact on customer mobility and market entry for new DP competitors given switching rules (GDAR) and assignment procedures (Vertical Slice)
- A bias to support the Ontario market
- Historically has taken on the role of supporting new infrastructure

Union's Proposal

- Union will include a Condition Precedent in long-term transportation contracts (or supply contracts if deemed necessary) requiring that the OEB approve the contract.
- Upon application by Union, the OEB will carryout a review for pre-approval of the long-term contract prior to the contract taking effect.
- Pre-approval request would be initiated by the LDC based on need to mitigate hind-sight regulatory risk. Long-term contracts would normally be considered 10-years or greater and would apply to new infrastructure.

EB-2005-0520 Settlement Agreement

Union's "Transportation Contracting Analysis"

Current guidelines for shorter-term contract reviews work well. These same guidelines could be used for the LTC process.

Union provides:

- Union's rationale for entering into the new transportation contract.
- All relevant contract parameters including: provider, term, price, receipt and delivery point.
- A quantitative comparison of the landed costs for newly contracted capacity to alternatives reviewed by Union at the time of its decision.
- A quantitative and/or qualitative consideration of additional factors considered relevant by Union that may include, but not be limited to:
 - Overall security of supply
 - Supply basin diversity
 - Contract term diversity
 - Pipeline operator diversity
 - Pipeline terms and conditions, and record of service
 - Monthly demand charge/commodity charge structure.