



LETTER DECISION

File OF-Tolls-Group1-M124-2017-01 01
1 March 2018

To: List of Parties to Proceeding RHW-003-2017

**Maritime & Northeast Pipeline Management Ltd. (M&NP)
Application for Approval of 2017-2019 Toll Settlement (Application)
RHW-003-2017 Reasons for Decision**

1. Background

On 30 June 2017, the National Energy Board (Board) received M&NP's Application pursuant to Part IV of the *National Energy Board Act*, and the *National Energy Board Guidelines for Negotiated Settlements of Traffic, Tolls and Tariffs* ([Guidelines](#)) for approval of a 2017-2019 Toll Settlement (Settlement) for final tolls over the period 1 January 2017 through 30 November 2019 (the Settlement Period). M&NP indicated that the Settlement is the result of negotiations with the M&NP Tolls and Tariff Working Group (TTWG), which is comprised of representatives of M&NP and other parties interested in M&NP's tolls and tariff matters. M&NP stated that the outcome of the TTWG vote was opposed with the majority of votes in favour of the resolution.

M&NP requested that the Board approve the Application in a timely manner. The key terms and conditions of the Settlement are:

- base period Settlement tolls per gigajoule of \$0.7515, \$0.7178, and \$0.7857 for the years 2017, 2018, and the first 11 months of 2019, respectively;
- accelerated depreciation over the Settlement Period;
- a decreased return for M&NP over the Settlement Period;
- abandonment fees charged throughout Settlement Period to be addressed through separate application;
- the end of the Settlement Period coincides with the expiration of the ExxonMobil Backstop Agreement (Backstop Agreement); and
- M&NP is at risk for certain interruptible revenues over the Settlement Period.

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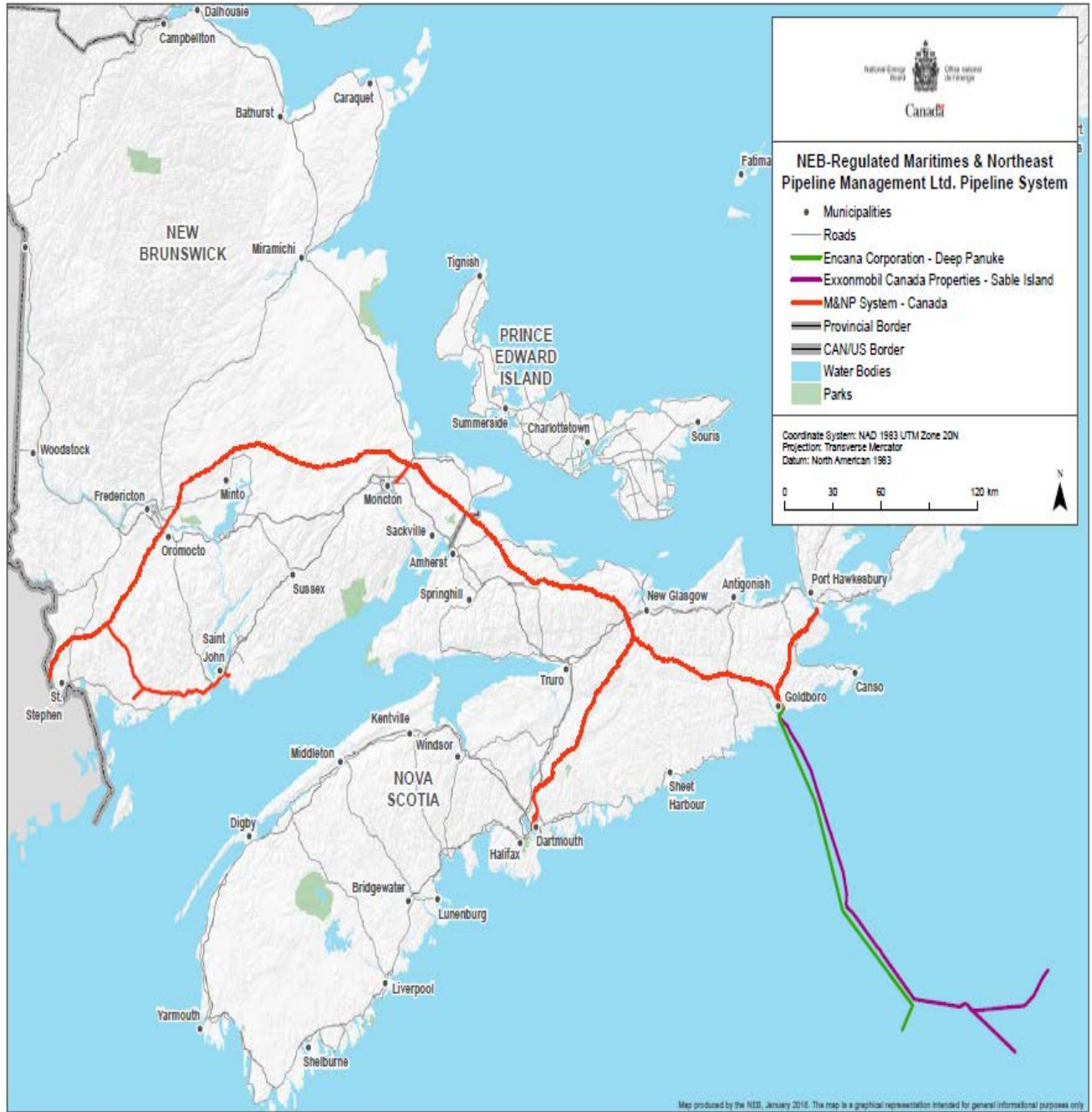
On 11 July 2017, as a result of the opposed TTWG vote, the Board invited comments on the Application. Following receipt of comments from some parties the Board issued Procedural Direction No. 1 on 18 September 2017 granting intervenor status to 16 parties in the RHW-003-2017 proceeding. The comments the Board received indicated the following:

- The Settlement was supported by the following parties
 - Corridor Resources Inc. (Corridor);
 - The East Coast Producers: ExxonMobil Canada Properties (ExxonMobil), Shell Canada Energy (Shell), Imperial Oil Resources Limited (Imperial), Pengrowth Energy Corporation, Mosbacher Operating Ltd., and Encana Corporation;
 - Enbridge Gas New Brunswick (EGNB);
 - Irving Oil Limited (Irving Oil);
 - JD Irving, Limited (JD Irving); and,
 - New Brunswick Power Inc. (New Brunswick Power);
- Heritage Gas Limited (Heritage), and its affiliates AltaGas Ltd. and Alton Natural Gas Storage, opposed the Settlement; and,
- Nova Scotia Power Inc. and Repsol Energy Canada Ltd. did not put forward positions on the Application, but indicated their respective interests in the proceeding.

The Board determined that a written process was appropriate for this Application. Information requests and responses were exchanged between parties from late September to 25 October 2017. On 3 November 2017 the Board issued Procedural Direction No. 2, which resulted in the hearing record being closed on 27 November 2017 following completion of written final and reply argument.

A map of the M&NP system is presented in Figure 1, below.

Figure 1. The M&NP System



2. The Settlement

This section summarizes the views of M&NP and parties on how the negotiated settlement complies with the Board's Guidelines and the extent of the shipper support for the Settlement. Section 3 elaborates on the opposition to the Settlement.

2.1 Compliance with the Board's Guidelines

Views of M&NP

M&NP submitted that all parties having an interest in M&NP's tolls and tariffs had a fair opportunity to participate and have their interests recognized and appropriately weighed in the Settlement. M&NP stated that the outcome of the TTWG vote was "opposed" with the majority of votes in favour of the resolution.

M&NP noted that section IV of the Guidelines states that "...a pipeline company may decide to file an application for approval when it has not obtained an agreement with all of its shippers but, in its judgement, believes it has an agreement which justifies filing the Settlement for Board approval." M&NP stated it believed that it had an agreement which justified filing the Settlement for approval. M&NP indicated that the opposition to the Settlement came from affiliated companies in one corporate family, none of which are primary firm shippers on the M&NP system.

M&NP stated that the Guidelines refer to agreement being obtained from all "shippers." M&NP noted that the Application indicated that no primary shipper is opposing the Settlement. As such, M&NP stated that it considers the Settlement to be supported by all of its shippers. M&NP submitted that the weight to be given to the views of non-primary contract holders is a matter of discretion for the Board. M&NP asserted that to require one hundred percent support from parties who are not primary contract holders would be to essentially provide any such party with veto rights over any settlement.

M&NP submitted that the Settlement and resulting tolls meet the requirements for negotiated settlements as set out in the Guidelines.

Views of Intervenors

Corridor

Corridor did not support M&NP's contention that the position of Heritage and its affiliates deserve less consideration or should be given less weight by the Board because they are not currently firm shippers on M&NP.

The East Coast Producers

ExxonMobil and Imperial stated that the Settlement negotiations were influenced by the views of TTWG members with concerns regarding the system tolls for 2020 and beyond. ExxonMobil and

Imperial also stated that those concerns were taken into account and that the TTWG Members and M&NP had to compromise to achieve a settlement.

The East Coast Producers stated that the settlement process is not contested or alleged to have been unfair in any way. The East Coast Producers said that the Settlement is a result of negotiations at the TTWG in which all interested parties had a fair opportunity to participate and have their interests recognized and appropriately weighed.

EGNB

EGNB stated that negotiations with the TTWG were ongoing from early 2016 and that parties had every opportunity to participate and provide comments.

Heritage

Heritage stated that M&NP attempted to marginalize the interest of Heritage in this proceeding because it does not currently hold firm service directly on the M&NP system. Heritage submitted that, in assessing whether the Application merits approval, the Board should have regard for the interests of all parties that stand to be affected by the tolls charged by M&NP, whether or not they are currently primary firm service shippers and whether or not they support the Application.

Heritage stated that it holds its Nova Scotia natural gas distribution franchise until 2028, at which time it intends to apply to extend its franchise term. Heritage will continue to rely on the M&NP system for its natural gas deliveries long after Encana and the East Coast Producers have departed. Heritage and its customers have a significant enduring interest in the tolls that M&NP charges.

Heritage submitted, with regard to the assertion of broad shipper support, that it bears noting that those voting in favour of the Settlement include producers that will terminate their shipping contracts during the Settlement Period and industrial end users that have a competitive alternative and are seeking load retention rates from M&NP. Heritage added that there are only two gas distribution utilities that are captive to M&NP, of which one is an affiliate of M&NP and the other is Heritage.

Irving Oil

Irving Oil stated that it participated in the TTWG and that the TTWG is a long-established and well-recognized forum that promotes collaboration and the resolution of toll and tariff issues between shippers and M&NP.

Irving Oil said that significant time and effort was taken in the negotiation process and allowed all parties to reach compromises on certain points. Irving Oil stated that the resulting Settlement reflects the gives and takes made during the process by parties.

New Brunswick Power

New Brunswick Power stated that the Settlement was voted on in a fair process.

M&NP's Reply

M&NP said that this process complied with the Board's Guidelines, it was open and all interested parties were invited to participate in the negotiations. M&NP indicated that Heritage, and its affiliates, were among the active participants in the negotiations. M&NP stated that Heritage does not take issue with the process by which the Settlement was arrived at.

M&NP submitted that it at no time asserted that secondary market shippers' positions should be ignored by the Board, only that they should not carry the same weight as the positions of M&NP's primary shippers, who directly bear the risks and consequences associated with the payment of M&NP's tolls.

2.2 The Acceptability of the Settlement

Views of M&NP

M&NP submitted that the Settlement has broad shipper support and its approval will allow for just and reasonable tolls on the M&NP system over the Settlement Period.

M&NP stated that the Settlement's calculation of the revenue requirement, tolls, deferral accounts, and the disposition of the balance of the deferral accounts is unchanged from previous settlements. Further, the toll schedules utilized in the Settlement are identical in structure to those in the nine previous M&NP toll settlement agreements that have been in continuous effect during the past sixteen years.

M&NP stated that the Settlement accelerates depreciation to recognize the probability that, due to depleting gas reserves, producers are not likely to extend their firm service contracts. M&NP stated that this accelerated depreciation is reflected in upward pressure on the toll, a burden borne by the primary firm shippers over the Settlement Period. M&NP said that the shippers have agreed to this as part of the balance reached in the Settlement, with M&NP agreeing to reductions in other key rate determinants, such as return on equity (ROE), and M&NP being at risk for IT (Interruptible Transportation service) and other revenues.

M&NP stated that the above mentioned reduction in ROE is another key element of the Settlement, with M&NP's ROE being significantly reduced during the Settlement from 10.9% in 2017 to 8.50% in 2018 and 8.25% in 2019.

M&NP submitted that approval of the Settlement will not only position M&NP to manage post-2019 tolls but will also allow M&NP and parties with the time to concentrate on such issues. M&NP argued that the broad support from all customer groups for the Settlement is a strong basis on which the Board can reasonably conclude that the Settlement is in the interests of interested parties, M&NP and the public generally.

Views of Intervenors

Corridor

Corridor submitted that M&NP's Application for approval of the Settlement should be approved. Corridor said that the basis for its support was that the Settlement produces tolls that are just and reasonable and take into account the public interest.

East Coast Producers

The East Coast Producers submitted that there is adequate information on the public record for the Board to base an independent assessment of the justness and reasonableness of the tolls. The East Coast Producers also submitted that the negotiated and agreed deemed capital structure, rate of return on equity, debt rates, and depreciation rates are all within the range of reasonableness and result in a revenue requirement that is reasonable.

The East Coast Producers submitted that the Settlement enjoys sufficient support to warrant its approval.

EGNB

EGNB stated that although tolls have increased steadily since 2001, increases have historically been gradual and EGNB hopes this will continue in future tolls. EGNB is sensitive to toll increases as they impact the ability to remain competitive in the Atlantic Canadian market.

EGNB stated that it believes that the Settlement is just, reasonable, and in the public interest.

Heritage

Heritage stated that it and its customers will be directly affected by the outcome of the Application, and they would suffer damage and be prejudiced by the approval of M&NP tolls for 2017-2019 that are not just and reasonable.

Heritage stated that in order to provide service to its customers, it relies solely on natural gas delivered to it by the M&NP system. Heritage said that it is captive to M&NP for its natural gas supply, is directly affected by the tolls charged for service on M&NP, and that increases in the M&NP tolls will increase the delivered cost of gas to Heritage customers in Nova Scotia. Heritage stated that this adversely impacts its ability to develop the natural gas distribution system in Nova Scotia.

Heritage stated that after considering the evidence filed by M&NP in this proceeding, Heritage remains opposed to the Application.

Heritage requested that the Board decline to approve the Application and, instead, initiate a proceeding to deal with the issue raised in its notice of opposition - namely, the determination of the tolling methodology and tolls that would be appropriate for M&NP given its high level of underutilization.

Heritage's opposition to the Settlement is addressed in more detail in section 3 of this decision.

Irving Oil

Irving Oil stated that it fully supports the Settlement. Irving Oil also stated that the resulting tolls and terms of the Settlement Period are just and reasonable. Irving Oil further stated that the level of support from shippers involved in the TTWG is strong and should be viewed as compelling evidence demonstrating the justness and reasonableness of this Settlement.

JD Irving

JD Irving stated that it has been a long-time firm transportation service shipper on the M&NP system and expects to be in the future. JD Irving also stated that it has participated in the TTWG and supports the Settlement.

New Brunswick Power

New Brunswick Power stated it voted in favour of the Settlement, and that the Settlement appears fair and reasonable.

M&NP's Reply

M&NP, in its reply, reiterated its position that the overwhelming support for the Settlement is compelling evidence of tolls that are just, reasonable, and not unduly discriminatory.

3. Opposition to the Settlement

The Board received notices of opposition to the Settlement from Heritage, AltaGas Ltd., and Alton Natural Gas Storage. This section summarizes the views of these parties and their proposed remedies to address these concerns.

3.1 Concerns with the Terms and Conditions of the Settlement

Views of Heritage

Underutilization

Heritage submitted that the tolls prescribed by the Settlement would not be just and reasonable. Heritage argued that there is now significant underutilization of the M&NP system and much of M&NP's capacity is no longer used and useful to provide transportation service and that the reduced throughput and underutilization has already occurred. Heritage submitted that M&NP does not address this reality in its Application.

Heritage stated that as the offshore gas production significantly declined between 2005 and 2015, the utilization and firm service commitments of M&NP have also declined. Heritage argued that the Backstop Agreement does not address the underutilization problem, it only masks it. Heritage indicated the underutilization problem on M&NP could get even worse because of the announced decommissioning of both the Sable Offshore Energy Project in 2018, and Deep Panuke between 2019 and 2021. Heritage added that there is no other offshore or onshore supply on the horizon to replace these lost volumes.

Heritage argued that the fundamental question is whether the Settlement adequately addresses M&NP's underutilization problem in respect of tolls not only for 2017-2019, but also for post-2019.

Heritage submitted that M&NP should not be permitted to wait until 2020 to address the current significant underutilization of its system. Heritage continued that if M&NP believes that changes to its method of regulation or service offerings or tolling methodology should be made, it should now apply to the Board for approval of such changes.

How the Settlement addresses future tolls

Heritage questioned how M&NP expects its domestic market customers to now make decisions about their transportation requirements post-2019. Heritage argued that M&NP has provided no forecast of the system utilization or billing determinants in 2020, and has made assumptions about post-2019 tolling initiatives without any consultation with its shippers. Heritage submitted its view that M&NP has no ascertainable plan for managing tolls on the M&NP system going forward.

Heritage submitted that M&NP points to the increases in depreciation in the Settlement as being key to ensuring that competitive tolls can be maintained on the M&NP system. Heritage argued that the expected \$0.07/million British thermal units/day (MMBtu/d) reduction in the 2020 toll as a result of the accelerated depreciation, though not inconsequential, would not remotely come close to offsetting the adverse toll impacts resulting from the expected reduction in billing determinants.

Heritage submitted that the estimated 2020 revenue requirement put forward by M&NP assumes that the depreciation rate for 2020 is reduced in order to fully depreciate the net assets by 2039. Heritage argued that were it not for this depreciation rate assumption, the 2020 revenue requirement would be more than 150 per cent higher than portrayed by M&NP.

Heritage argued that M&NP's evidence does not demonstrate that the Settlement adequately addresses the problem of underutilization on the M&NP system, particularly as it relates to the management of the tolls going forward. Heritage submitted that while the increases in depreciation from 2017-2019 are a step in the right direction, they are hardly the "major step" that M&NP advertises them to be, and they will not have a "significant impact" on M&NP's post-Settlement tolls.

Suggested Measures

Heritage argued that other measures should be considered at this time in order to mitigate toll increases for the remaining captive shippers at the end of the Settlement Period, when the producer Backstop Agreement expires. Specifically, Heritage suggested:

- further increasing the depreciation rates for 2017-2019; and,
- fixing the toll for some further period post-2019.

Further Increasing Depreciation

Heritage stated that it does not suggest that the entire M&NP system should be fully depreciated by the end of the Settlement Period. However, Heritage argued that consideration should be given to

fully depreciating the 434,000 MMBtu/d of capacity contracted to the East Coast Producers. This would ensure that the remaining captive shippers are not left, at the end of the Settlement Period, to pay depreciation on unutilized capacity that the producers have relinquished.

Setting of Tolls Beyond Settlement Period

Heritage submitted that even if the Board were to act on the above position of Heritage, further accelerating depreciation would not offset the adverse toll impact that will arise from the loss of billing determinants at the end of the Settlement Period. Heritage suggested that consideration should now be given to a multi-year approach to setting tolls that would extend beyond the Settlement Period. Heritage argued, given the significant underutilization and uncertainty regarding the M&NP system, this seems to be the only way to provide toll stability to the enduring market after the Settlement Period.

Heritage submitted - contrary to M&NP's statement that it has no forecast of the utilization rate beyond the Settlement Period as there are too many unknown variables at this time to accurately forecast demand - that the enduring domestic market is well known. Heritage argued that M&NP acknowledged that there is not likely to be any material market developments over the next 24 months. As such, Heritage put forward the revenue requirement estimate provided by M&NP with a resulting \$0.76/MMBtu/d toll, based on throughput of 176,119 MMBtu/d, as an agreeable level for fixing the 2020 tolls.

Disallowance of Return

In the absence of a proceeding regarding changes to the tolling methodology during the Settlement Period, Heritage argued that the Board should consider the appropriateness of allowing M&NP to continue to recover the costs of all its capacity in its tolls. Heritage added that it should not be an option for M&NP to continue to charge tolls that allow the return of and on its investment, irrespective of whether pipeline capacity associated with that investment is used and useful for providing transportation service.

Views of M&NP

M&NP argued that the fundamental question is not, as put forward by Heritage, "whether the Settlement adequately addresses M&NP's underutilization problem in respect of tolls not only for 2017-2019, but also for post 2019". Rather the question is whether the Settlement Period tolls are just, reasonable, and not unduly discriminatory while appropriately taking into account public interest considerations which may extend beyond the immediate concerns of the negotiating parties. M&NP argued that the answer to the fundamental question it put forward, is "Yes."

M&NP stated that the Settlement spans an important period in the evolution of the M&NP system in which changed contractual and economic circumstances are expected post-2019. M&NP argued that the Settlement, through its accelerated depreciation, effectively provides a bridge from the pre-2020 period, in which supply-driven dynamics predominate, to 2020 and beyond, when the system will transition to largely domestic market-driven dynamics.

M&NP stated that the level of post-2019 M&NP system tolls will predominantly depend on the level of billing determinants on the system at that time. M&NP indicated that it intends to make all reasonable commercial efforts during the Settlement Period to actively manage the cost of service parameters impacting post-2019 M&NP system tolls.

Underutilization

M&NP acknowledged the concerns of some of the TTWG members with respect to M&NP tolls post-2019, given the significant changes expected to occur at the end of the Settlement, including a continued decline in domestic gas supplies and the expiration of the Backstop Agreement.

M&NP said that to the extent there is underutilization on the M&NP system, the Settlement deals with this reality, just as settlements over the last decade have dealt with this reality. M&NP stated that the reality of not operating at full rated capacity does not lead to the conclusion that M&NP assets are not being used and useful for service. M&NP submitted that, to the contrary, M&NP has firm contractual commitments, and a corresponding firm contractual service obligation, for 434,000 MMBtu/d through to the end of Settlement Period. M&NP stated that this amounts to the M&NP system being 80 per cent utilized from a contractual, and therefore revenue, perspective, and further, that the system must stand ready to transport the entire 434,000 MMBtu/d that is being contracted and paid for, regardless of the level of projected physical throughput on the system.

Further Increasing Depreciation

M&NP stated that the approval of the Settlement will contribute to lower tolls after the Settlement Period by accelerating the reduction of rate base during the Settlement Period. M&NP added that an appropriate depreciation rate is required to ensure M&NP does not under-collect its capital costs during the Settlement Period, thereby placing an unfair burden on future period shippers.

M&NP asserted that it is cognizant of the Board's assessment of supply risks faced by M&NP in the MH-001-2013 Set-aside and Collection Mechanism proceeding and has taken that, along with consideration of the expected expiry of its major producer contracts and other market developments, into consideration in developing its proposed depreciation rates for the Settlement Period.

M&NP stated that the Settlement accelerates depreciation to recognize the probability that, due to depleting gas reserves, producers are not likely to extend their firm service contracts. M&NP argued that it would not be appropriate to further accelerate depreciation during the Settlement Period. M&NP indicated that the acceleration of depreciation achieved by the Settlement represents an approximate 40% increase from 2016 to 2019. M&NP added that while it can always be argued by differing interests that higher or lower depreciation rates should apply during the Settlement Period, the balance achieved by the Settlement is fair.

M&NP stated that it believes that, based on the market circumstances that are now known, it is paramount that this depreciation adjustment be made while all of the shippers that have been on

the system remain on the system, and to ensure that the transportation toll available to domestic Maritime markets transitions in a reasonable manner to post-2019 levels. M&NP argued that doing so balances the interests of existing and future shippers and will assist parties in continuing to utilize the M&NP system both during the term of the Settlement and beyond.

M&NP stated that the Settlement depreciation methodology (accelerated to reflect depleted gas supply and expected non-renewal of producer contracts) and M&NP's planned depreciation methodology for the post-Settlement Period (decelerated to reflect enduring market and lower utilization rate) are consistent with the goal of intergenerational equity. This methodology minimizes the potential for intergenerational inequity by matching economic use of the pipeline with the prevailing shipper mix. M&NP added that it would not be appropriate to further accelerate depreciation during the Settlement Period.

Setting of Tolls Beyond the Settlement Period

M&NP submitted that there would be no utility to mandating a hearing to deal with post-2019 tolling issues at this time, as it would be largely speculative and likely subject to adjustment.

M&NP submitted that setting tolls today to the end of 2022 at the 2019 Settlement toll level, to provide the enduring market with toll stability post-November 2019, is inconsistent with sound toll-making. M&NP argued that intergenerational equity applies as much to the Settlement Period, involving producers, as to the period beyond, involving Heritage and the enduring market. M&NP also submitted that any suggestion that Heritage is entitled to a degree of toll protection, or a guarantee of toll levels far into the future, based on past system use and absent a contractual right, is contrary to the Board's "no acquired rights" principle.

M&NP submitted that Heritage's suggestion, that significant uncertainty about post-2019 billing determinants is a reason for locking in tolls now for the post-2019 period, is nonsensical. M&NP argued that the appropriate response to the uncertainty in the post-Settlement Period is to achieve what is reasonably possible in the 2017-2019 period to set the table for maintaining tolls as low as possible thereafter. M&NP added that it would be appropriate to prepare the post-Settlement tolls once there is greater clarity around the circumstances that will prevail post-2019.

Disallowance of Return

M&NP submitted that Heritage's assertion that tolls allowing a return of and on capital during the Settlement Period are unjust and unreasonable is entirely unfounded. M&NP argued that the assertion that M&NP is no longer entitled to a return of and on capital equates to a finding that fundamental risk has materialized for the M&NP system. M&NP stated that there is absolutely no evidence to support such a finding. In M&NP's view, the evidence is that tolls during the Settlement Period remain at reasonable levels and that the parties primarily responsible for paying such tolls are overwhelmingly in support of the Settlement and are not asserting that tolls are at a level greater than the market can bear.

Summary

M&NP submitted that Heritage's view (that the mitigation of future toll increases incorporated in the Settlement is not adequate and that the Settlement Period shippers should pay even more) is not evidence of the Settlement ignoring post-2019 circumstances. M&NP argued that it is only evidence of Heritage's opinion that the Settlement has not struck an appropriate balance.

M&NP submitted that the Settlement takes concrete measures to reduce M&NP's revenue requirement to enable M&NP to effectively manage its post-2019 tolls. M&NP argued that the Settlement, as applied for, provides toll stability over the Settlement Period and that it takes into account public interest considerations which may extend beyond the immediate concerns of the negotiating parties by setting the foundation to keep tolls as low as practically possible for the post-Settlement Period.

Views of Intervenors

Corridor

Corridor submitted that Heritage, in its submissions in the proceeding, raised a number of important issues that need to be addressed by M&NP, interested parties and the Board. Corridor encouraged M&NP to begin a process to address those issues, but Corridor submitted that the Board should not address those issues in this proceeding.

East Coast Producers

The East Coast Producers stated that Heritage, in its opposition to the Settlement, does not suggest an alternative toll methodology for M&NP and does not suggest a toll that in its view would be just and reasonable and not unjustly discriminatory. In the East Coast Producers' view, Heritage is seeking an inquiry to consider whether tolls which allow a return on and of capital invested in pipeline capacity that is no longer used and useful are just and reasonable. The East Coast Producers argued that Heritage adduced no evidence to support its belief.

Underutilization

The East Coast Producers submitted that the M&NP system continues to be used and useful in the provision of gas transmission service, and that contracts, including the Backstop Agreement, are in place through to late 2019 in respect of 78% of M&NP's capacity.

Further Increasing Depreciation

The East Coast Producers stated that the negotiated depreciation rates, which are higher than those that would be required to effect return of capital over the economic life of the M&NP facilities, are a cost to current shippers that will benefit toll payers on the system after the expiry of the Settlement Period.

The East Coast Producers submitted that Heritage's position on depreciation is inconsistent with existing regulatory principles governing depreciation. The East Coast Producers stated that it is well accepted that depreciation is recovered over the economic life of the facilities and that there

is no evidence whatsoever that the economic life of the facilities will end at the conclusion of the Settlement Period. The East Coast Producers argued that, to the contrary, the evidence is that parties like Heritage will continue to use the M&NP system for the foreseeable future.

The East Coast Producers stated that shippers on the M&NP system, including the East Coast Producers, entered into contracts for service under the regulatory paradigm which governed the reasonable expectations of those parties at the time. The East Coast Producers submitted that full depreciation prior to the end of the economic life of the facilities could not have been anticipated and, if allowed, would result in unfairness and prejudice. The East Coast Producers argued that it would be highly inappropriate, unfair, and entirely premature to change the toll methodology that underpinned the contracts held by the East Coast Producers prior to expiry of those contracts.

The East Coast Producers stated that Heritage began to expand its franchise for the distribution of natural gas in Nova Scotia in 2003. The East Coast Producers argued that it must be taken that, at that time, Heritage was well aware that the pipeline would not be fully depreciated by the time contracts on the pipeline expired. The East Coast Producers stated that Heritage's franchise does not expire until at least 2028, and Heritage has plans to seek an extension. The East Coast Producers argued that it would be entirely inappropriate to now change the toll methodology that existed when Heritage embarked on its franchise.

Setting of Tolls Beyond the Settlement Period

Shell stated that the objections identified by Heritage, and its affiliated companies, relate to issues beyond the Settlement Period. Shell further stated that Heritage's future concerns regarding contracting and utilization should not be addressed by the Board in this Application and should be raised and considered in future proceedings.

EGNB

EGNB stated that it is confident in the regulatory process and the ability of the Board to make fair and just decisions regarding current and future tolls on the M&NP system, but that it did not feel it reasonable to speculate on future tolls at this time.

Irving Oil

Irving Oil stated its observation that the concerns raised by Heritage relate to issues anticipated to arise after 2019. Irving Oil said that these issues are by no means definitive or absolute and it is unclear how they can or should have bearing on a Settlement applicable to the 2017-2019 time period. In addition, Irving Oil stated that approval of the applied-for Settlement has not been shown to have any prospect of prejudice or preventing such issues from being raised and considered in the future.

4. Abandonment Funding

Views of Heritage

Heritage argued that increasing M&NP's abandonment cost toll surcharge during the Settlement Period should be considered. Heritage suggested that given the circumstances on M&NP where the producers are terminating their contracts and there is no reasonable prospect that the capacity associated with providing the service to them will be recontracted to others, it would be appropriate for the producers to bear responsibility for all abandonment costs associated with the use of that capacity. It would be contrary to the goal of economic efficiency to require the remaining captive shippers to pay abandonment costs on unutilized capacity that the producers have relinquished.

Views of M&NP

M&NP submitted that although abandonment fees will be charged throughout the duration of the 2017-2019 Toll Settlement, those fees are separate from and are not included in the 2017-2019 Toll Settlement. M&NP added that it does not plan to make any changes to its abandonment cost toll surcharge over the Settlement Period.

M&NP submitted that the risk its abandonment fund faces is related to an increase in the abandonment cost toll surcharge (ACTS) to compensate for the expected decline in billing determinants. According to M&NP, following the Settlement Period, it plans to file for an extended abandonment cost recovery period, to reflect the enduring domestic market. By extending the recovery period coincident with the decline in billing determinants, M&NP submitted that it will be able to maintain the ACTS at a more reasonable level.

5. Views of the Board

Settlement's Compliance with the Guidelines

As noted in the Guidelines, negotiated settlements are regarded by the Board as an opportunity for interested parties to resolve issues without resorting to a hearing process. The Guidelines set out that:

- all parties having an interest in a pipeline company's traffic, tolls and tariffs should have a fair opportunity to participate and have their interests recognized and appropriately weighed;
- a settlement must not fetter the Board's ability and discretion to take into account any public interest considerations which may extend beyond the immediate concerns of the negotiating parties; and,
- the settlement process must produce adequate information on the public record for the Board to understand the basis for the agreement, assess its reasonableness, and to be able to determine that the resulting tolls are just and reasonable and not unjustly discriminatory.

In the case of a contested settlement, the company shall provide to the Board a submission as to why the settlement should be accepted by the Board. The Board will invite comments on the application, and following any process set out by the Board, the Board will consider all the evidence before it, including the expected benefits to be gained by the consenting parties and the expected costs to the dissenting parties.

The Board notes that no interested party raised concerns with the manner in which the negotiations and subsequent TTWG vote occurred.

M&NP stated that secondary market shippers' positions should not carry the same weight as the positions of M&NP's primary shippers, who directly bear the risks and consequences associated with the payment of M&NP's tolls. Heritage, its affiliates, and Corridor disagreed with this position. Heritage stated that it has a significant enduring interest in M&NP tolls and will continue to rely on the M&NP system for its natural gas deliveries long after the East Coast Producers have departed.

The Board notes, that in making its decision with respect to settlements it weighs the evidence of parties on a number of different factors, depending on the circumstances surrounding the application. Further, the Board also considers the impact on parties that may not be party to the negotiations such as possible future shippers and the development of domestic markets in keeping with the principles of intergenerational equity and cost causation. Each pipeline, application, and set of market circumstances are unique and require appropriate weighing of the evidence by the Board.

M&NP brought the Application before the Board referencing section (iv) of the Guidelines, regarding Contested Settlements. The Board agrees with the appropriateness of presenting the Application as contested, given the TTWG vote was opposed. The Board finds that the Settlement complied with the Guidelines and provided interested parties with a fair opportunity to participate and have their interests recognized and weighed in the Settlement.

Reasonableness of the Settlement

The Board notes the broad support the Settlement received from both the current firm service shippers (who directly bear the financial burdens tied to the Settlement) and shippers in the secondary market for M&NP capacity (who are expected to continue utilizing the pipeline beyond the Settlement Period). The Board also notes the concerns raised by Heritage in relation to underutilization, whether the pipeline is currently used and useful, and toll stability and certainty for the enduring market beyond the Settlement Period. Heritage requested that the Board decline to approve the Application and, instead, initiate a proceeding to determine the tolling methodology and tolls that would be appropriate for M&NP given its high level of underutilization.

The Board is of the view that the impact of the expected drop in billing determinants at the end of the Settlement Period should be addressed by the parties, to the extent possible, during the Settlement Period. In the below sections, the Board examines those steps taken in the Settlement, as well as those proposed by Heritage, to address this reality.

Depreciation, and terms of the Settlement

The Board notes that the M&NP system will be approximately 86 per cent depreciated by the end of the Settlement Period. The Board is persuaded by M&NP that the accelerated depreciation and the reduced return on equity for M&NP contained in the Settlement are in keeping with the toll principle of intergenerational equity and are sufficiently responsive to the current and future realities facing M&NP at this time. As M&NP noted, it can always be argued by differing interests that higher or lower depreciation rates should apply during the Settlement Period, however, the Board was not persuaded that changes to the depreciation rates set out in the Settlement are warranted.

Further, the Board believes that to accelerate depreciation to ensure that the capacity contracted to the East Coast Producers is fully depreciated by the end of the Settlement Period would result in M&NP's current shippers bearing undue burden related to future costs and benefits. The Board views this outcome as unjust and unreasonable, as it would ensure recovery by M&NP of future costs at the expense of current shippers.

The Board agrees with the East Coast Producers that it would be inappropriate to direct a significant change in the tolling methodology that underpins long-term contracts at this time, even if those contracts will expire at the end of the Settlement Period.

The Board finds the Settlement Period appropriate to the conditions and market realities facing M&NP, and further finds that the Settlement proactively takes steps during the Settlement Period to address the ongoing concerns of the enduring market after the expiry of the Backstop Agreement and the Settlement Period.

Setting of Tolls Beyond the Settlement Period

Heritage stated that it considers the setting of tolls beyond the Settlement Period the only way to provide toll stability to the enduring market after the Settlement Period. M&NP and supporters of the Settlement stated that the issues raised by Heritage fall outside of the Settlement Period and that it would be inappropriate for the Board to consider them in this proceeding, and that setting tolls beyond the Settlement Period would be too speculative to be of use.

The Board is not persuaded by M&NP that it is “nonsensical” for Heritage to seek toll stability given significant uncertainty in the future. The setting of tolls results in the allocation of risk between shippers and a pipeline, as well as providing a level of certainty for all parties. Fixing tolls for longer time periods can be difficult, particularly when future circumstances are uncertain, as information deficiencies hamper the ability to accurately predict how the risk and reward balance will play out over time. The Board is of the view that the setting of long-term

fixed tolls is possible through negotiation but, as in any negotiations, parties negotiating toll settlement agreements would be expected to be aware of the risks they accept.

However, the Board is not persuaded by Heritage that a toll hearing to consider setting tolls outside of the Settlement Period is warranted at this time. It is premature, in the Board's view, to pursue long-term fixed tolls without M&NP having the opportunity to explore market-based solutions given the anticipated scale of the shift in markets and the level of uncertainty. Nor is the Board persuaded by Heritage's evidence that such a hearing would be likely to provide the long-term level of toll certainty that is sought by Heritage.

Disallowance of Return

In the absence of a hearing or application from M&NP regarding tolling methodology beyond the Settlement Period, Heritage requested that the Board consider the appropriateness of allowing M&NP to continue to recover the costs of all its capacity in its tolls. Heritage took the position that M&NP should not be able to continue to charge tolls that allow the return of and on its investment, irrespective of whether pipeline capacity associated with that investment is used and useful for providing transportation service. M&NP contended that to disallow a return due to underutilization would be to conclude that fundamental risk has materialized for the pipeline¹.

The Board notes that in proposing this treatment for M&NP's capacity that Heritage considered to be underutilized, Heritage did not address how M&NP should manage the binding transportation contracts and associated revenue collected by M&NP for the capacity under contract during the Settlement Period.

In the Joint Public Review Panel Report GH-6-96 that recommended approval of the Maritime and Northeast Pipeline Project, the Board found that:

The evidence included an examination of the business risks M&NP would be exposed to during the operation, namely the supply risk, the markets the pipeline would serve, the contractual arrangements for gas sales, the Backstop Agreements, political and regulatory circumstances, and pipeline operating conditions. Of the several business risks, the evidence indicates that the greatest distinguishing risk factor is related to the supply of natural gas. However, certain intervenors submitted that the level of business risk was overstated, particularly because of the level of security offered by the Backstop Agreements.²

¹ The Board, in its RH-3-2011 Reasons for Decision, described fundamental risk of the TransCanada Mainline in the following way: "The Board previously characterized the situation where the Mainline's fundamental risk materializes as the point at which Mainline throughput has declined to a level where the resulting tolls exceed what the market could bear. If this were to happen, the Board noted that it would no longer be able to protect the Mainline and the Mainline may not be able to recover all of its costs."

² Joint Public Review Panel Report GH-6-96, PDF page 67 of 168.

The Board is of the view that supply and market risks remain business risks to which M&NP is exposed. The Board notes that the M&NP system is contracted for a significant portion of the pipeline's capacity throughout the Settlement Period, and that at no point during the Settlement Period will captive shippers bear the costs related to physical underutilization on the pipeline. Further, the Board is of the view that there is not sufficient clarity, or evidence on the record in this proceeding, regarding the post-Settlement Period to allow it to make determinations regarding the future utilization of the M&NP system or its tolls. The evidence does not demonstrate that it is appropriate to disallow M&NP the return of and on its investment.

Conclusion

The Board finds that the Settlement toll methodology is appropriate and results in tolls that are just and reasonable over the Settlement Period. The Settlement appears to strike a fair balance between the pipeline and its current shippers while still taking into account the interests of future users of the system.

The Board notes Heritage's concerns that M&NP has not consulted with the TTWG about M&NP's assumptions regarding post-Settlement tolling initiatives. The Board encourages meaningful consultation and discussions between M&NP and its shippers at an appropriate time, well in advance of the expiration of the Settlement, to provide shippers with a measure of toll certainty and the ability to appropriately plan their business activities and transportation requirements. In the Board's view both M&NP and those shippers that form the enduring market have an obligation to co-operate and share critical information to develop workable transportation services and tolls that fit the post-Settlement circumstances.

The Board expects M&NP to take steps to actively manage its risks going forward, including fundamental risk. Possible steps could include reducing costs, increasing billing determinants, and exploring opportunities to develop new service offerings.

Abandonment Funding

M&NP stated that the Settlement spans an important period in the evolution of the M&NP system and effectively provides a bridge from the pre-2020 period, in which supply-driven dynamics predominate, to 2020 and beyond, when the system will transition to largely domestic market-driven dynamics. The Board notes that in the MH-001-2013 decision, it found:

[...]If there is a change in circumstances between Board-mandated reviews that materially affects the amount required to be collected, then the company must revise their annual contribution amount. The company must not wait until the Board's next review. If there is significant risk that adequate funds will not be set aside, the Board may, on its own initiative, require further coverage of any unfunded future costs through a secondary mechanism (for example, a letter of credit for the unfunded balance).³

³ MH-001-2013 Reasons for Decision – Set-aside and collection mechanism, Section 6.2 - Reviews of Annual Amount Set aside, PDF 122 of 176, A60676-1.

The Board also found:

[...] there is a considerable risk for M&NP to under-collect the cost of abandoning its system because the current supply available to the M&NP system is limited.⁴

The Board also found that for M&NP, a 19.5 year collection period:

[...] more appropriately aligns with current forecasts of the supply available to the M&NP system. M&NP can apply to the Board to vary its collection period if significant supply developments were to occur [...]⁵

The Board believes the current situation may constitute a “significant supply development”. If nothing else, it likely represents a material change in circumstances between Board mandated reviews of the collection period. Due to the aforementioned production declines and anticipated change in use of the system, the Board is of the view that the 19.5 year collection period originally set out in MH-001-2013 should be revisited. The risk of M&NP under-collecting the costs to abandon its system may have increased relative to when the risk was last evaluated by the Board as part of that proceeding.

As noted by the Board in the MH-001-2013 decision, the Board remains of the view that the amount to be set aside for pipeline abandonment should not be subject to negotiation as part of a settlement agreement. Nevertheless, the Board is not satisfied with M&NP’s proposed deferral of this issue to the post-Settlement Period. In the Board’s view, this is not consistent with the direction set out by the Board in MH-001-2013 for M&NP to apply to the Board to vary its collection period should significant supply developments or changes in circumstances occur. It is also inconsistent with M&NP’s proactive approach of accelerating depreciation over the Settlement Period, which contributes to a reduction of risk to itself and its shippers in the post-Settlement Period.

The Board agrees with Heritage’s submission that increasing M&NP’s abandonment cost toll surcharge during the Settlement should be considered. Such an approach could reduce the risk of underfunding in the future, and more appropriately align with the principle of intergenerational equity. However, abandonment funding is outside of the scope of this Settlement and the Board has not solicited extensive evidence on the matter. Therefore, it is premature to determine whether modifying the collection period and/or increasing the surcharge over the Settlement Period is warranted. It is also too early to determine whether M&NP’s proposal to lengthen the abandonment cost recovery period, following the Settlement Period, would be appropriate.

Given the expected reduction in billing determinants following the Settlement, the Board views as time sensitive the setting of appropriate abandonment contribution amounts. Accordingly, the Board directs M&NP to file an application with the Board, by 1 May 2018, proposing an updated collection period and annual collection amount for the Settlement Period and beyond. The Board

⁴ MH-001-2013, Section 4.4.1 – M&NP, PDF 91 of 176, A60676-1.

⁵ MH-001-2013, Section 4.4.1 – M&NP, PDF 92 of 176, A60676-1.

encourages M&NP to request an expedited review process for the application. The application should address, at a minimum:

- whether the collection period remains appropriate, or whether it should be truncated/lengthened;
- whether it may be appropriate to have differing associated contribution amounts during and after the Settlement, based on the expected change in use of the system;
- whether the amount set-aside by M&NP should be accelerated over the Settlement Period;
- whether the abandonment surcharge should be increased over the Settlement Period;
- markets and supply, during both the Settlement and post-Settlement Periods, including supporting evidence using currently available estimates for the post-2019 period;
- the appropriateness of M&NP's abandonment trust's investment policy, as set out in its Statement of Investment Policies and Procedures filed with the Board, during both the Settlement and post-Settlement Period; and,
- how the proposed collection period and contribution amounts respect the principle of intergenerational equity.

Ultimately, M&NP remains responsible for the costs to abandon its system. As noted in MH-001-2013, if the Board is of the view that there is significant risk that adequate funds will not be set aside, the Board may require further coverage of any unfunded future costs through a secondary mechanism such as a letter of credit for the unfunded balance.

6. Disposition

The Board approves the Application as applied for by M&NP subject to the conditions in the accompanying toll order.



R.R. George,
Presiding Member



S.J. Kelly,
Member



A. Scott,
Member