File OF-Tolls-Group1-T260-2023-03 01

September 6, 2023

To: Canada Energy Regulator
210-517 Tenth Ave SW Calgary, Alberta
T2R 0A8
Via CER Online Portal

Attention: Ms. Ramona Sladic, Secretary of the Commission

Dear Ms. Sladic,

RE: Trans Mountain Pipeline ULC Application pursuant to Section 67 and the Traffic, Tolls and Tariffs provisions in Part 3 of the Canadian Energy Regulator Act for Approval of Interim Commencement Date Tolls and Other Matters related to the Transportation of Petroleum on the Expanded Trans Mountain Pipeline System (Application)
File OF-Tolls-Group1-T260-2023-03 01
Letter of comment on IRR1 from Tsleil-Waututh Nation

Tsleil-Waututh Nation (TWN) submits the following comments regarding Trans Mountain's responses to Commission IR1 (C25905) pursuant to Canadian Energy Regulator (CER) Process Letter No.2 (C25730) and CER Ruling No. 1 (C25996-1).

As set out in Process Letter No. 2, the CER is preparing to issue a preliminary decision within the interim toll hearing which will "focus on a narrower set of issues that can support an initial ruling with respect to just and reasonable interim tolls, on a timeline that is intended to avoid delaying the commencement date of the expanded Trans Mountain system."

It is not clear whether the issues raised in TWN's letter of comment (C25110), including whether the interim tolls are just and reasonable, will be included in the scope of the subsequent hearing process, yet to be determined by the CER. As a result, TWN submits the following comments in support of TWN's position that the proposed tolls are not just and reasonable, and that any preliminary decision on interim tolls should not be determinative of whether the tolls are just and reasonable moving forward. These comments are primarily focused on Trans Mountain's responses to IR 1.4, however silence on other issues should not be taken as agreement.

It is unfortunate that intervenors were not provided with the opportunity to ask information requests of Trans Mountain during this preliminary round, as the single round of IRs from the CER resulted in Trans Mountain providing incomplete or misleading responses, without opportunity for follow up.

In particular, the responses to IR1.4 (IRR1.4) relating to the company meeting its financial obligations only provide a partial and distorted glimpse into Trans Mountain's full financial picture to the CER. As a result, TWN has conducted further analysis on more realistic scenarios, as discussed below.

TWN submits that despite the lack of complete information, the interim tolls that Trans Mountain applied for are not just and reasonable. TWN's position is that the CER should revisit the toll methodology because of the unique and unprecedented circumstances related to this application which result in tolls that cover less than half of the cost of construction, requiring the proponent to absorb $16.2 billion of the estimated $30.9 billion construction budget. In terms of losses, the amount will be much greater than $16.2 billion due to the debt that has been incurred for Canada's purchase of Trans Mountain, along with interest expense for the purchase and expansion not included in the financing estimate of the construction budget.

TWN notes that this application would not be before the CER if Trans Mountain were still owned by Kinder Morgan Inc. The six Crown Corporations that comprise Trans Mountain are not acting on a commercial basis by filing this application without direct accountability to the Government of Canada and by extension, the Canadian public.

TWN's submission can be summarized as follows:

1. Trans Mountain's IRR 1.4 does not provide a full picture of Trans Mountain's financial picture and should not be relied upon to determine whether tolls are just and reasonable;
2. Trans Mountain cannot meet its financial obligations;
3. The Fair Return Standard is no longer met;
4. The capitalization of Trans Mountain is 100% debt;
5. Trans Mountain's recapitalization scenario is not credible;
6. Trans Mountain cannot service debt obligations (principal and interest); and
7. Trans Mountain has embellished its revenue stream.

Even with Trans Mountain's distorted numbers - unlikely and overly optimistic, Trans Mountain Corporation (TMC) claims a forecast return on equity of 1-4% - a far cry from the 12-15% hurdle set by Kinder Morgan, which is consistent with the industry norms that the Commission is supposed to uphold. As a result, TWN submits that the CER must revisit the toll methodology as it relates to the current budget, and provide further opportunity for the Commission and intervenors to test the reasonableness of the proposed tolls and tolling methodology before making a preliminary determination.

1. Trans Mountain's IRR 1.4 does not provide a full picture of Trans Mountain's financial picture and should not be relied upon to determine whether financial obligations can be met

Trans Mountain's IRR1.4 presents scenarios based on a picture of the company as represented by a consolidation of TMC and its subsidiaries.[1] TMC is an arbitrary cut off point since the Application has been filed by Trans Mountain Pipeline ULC, a subsidiary of TMC, while TMC is 100% owned by Canada TMP Finance Ltd. (TMP Finance), which in turn is 100% owned by Canada Development Investment Corporation (CDEV) as set out in the CDEV Organization chart, below. The relevant Trans Mountain entities are highlighted in red and must be considered as a whole when evaluating Trans Mountain's financial picture, including TMP Finance.

A complete picture of Trans Mountain's financial status that includes TMP Finance would more clearly illustrate the issues obfuscated by Trans Mountain's IR Responses. Unfortunately, Trans Mountain's response does not fully or accurately address the Commission's information request because Trans Mountain only provides information from Trans Mountain Corporation (TMC), and not TMP Finance, TMC's parent company which to date has borrowed more than $16 billion from the Canada Account for the benefit of Trans Mountain.[2] In contrast, TMC reports only $8 billion as having been borrowed from TMP Finance with $7.4 billion reported as equity.[3]

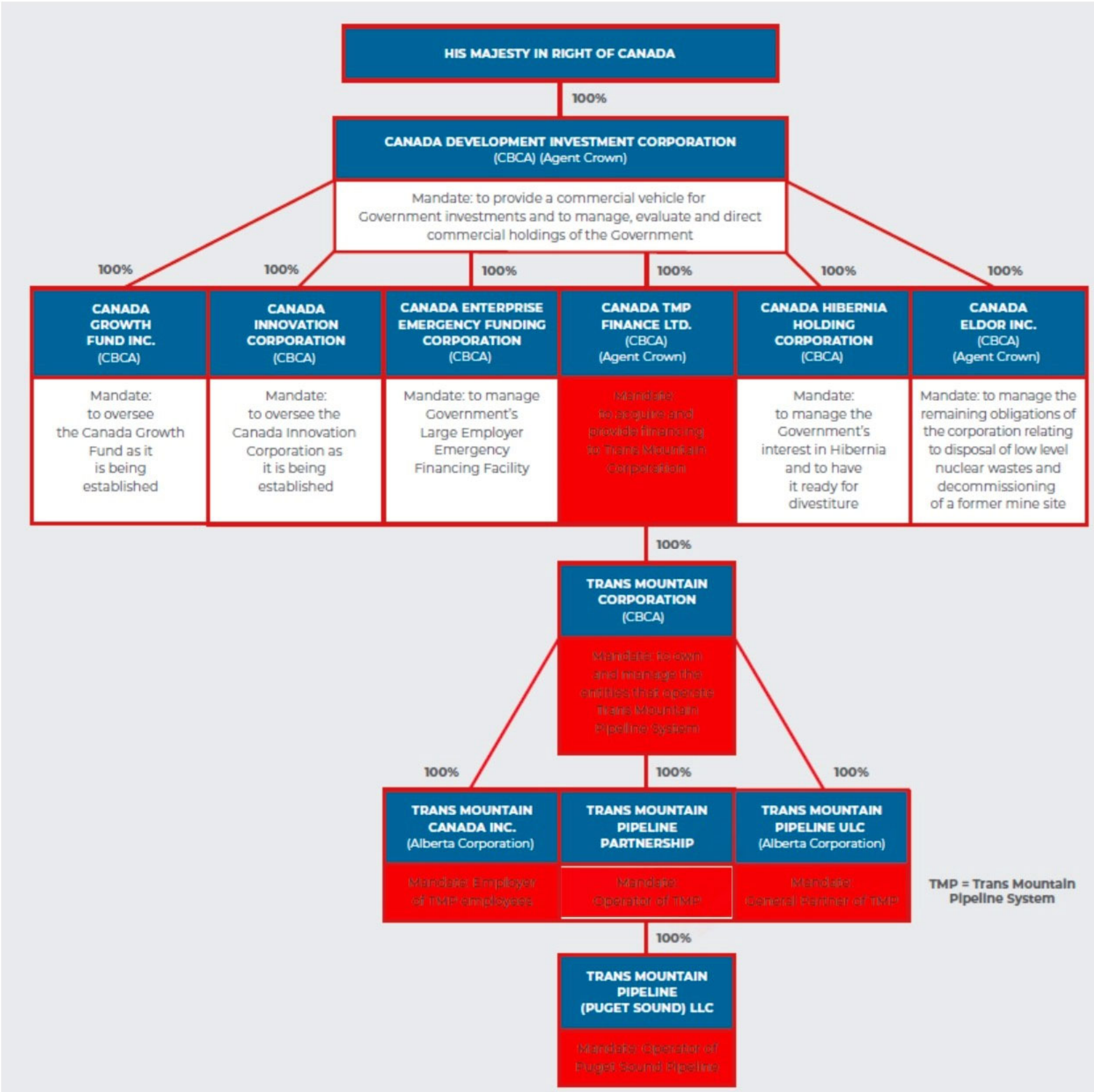
Without corporate shells and accounting wizardry, it would be clear that Trans Mountain is unable to meet its financial obligations under the toll methodology, and as a result, under the applied-for interim tolls that the methodology produces.

This has direct implications on Trans Mountain's responses to the Commission's questions about meeting financial obligations as they relate to Trans Mountain's fictional capital structure, and the implications that flow from that structure. In reality, Trans Mountain, including the expansion, is funded by 100% debt, and questions about meeting financial obligations must consider this reality.

[1] Trans Mountain Pipeline ULC, Responses to CER Information Request No. 1, Application for Approval of Interim Commencement Date Tolls and Related Matters, August 16, 2023, p.23, footnote 6.

[2] Outstanding Amount: $16,501,376,000 as of June 30, 2023, see CDEV Q2 2023 Report: https://cdev.gc.ca/wp-content/uploads/2023/08/Q2-2023-CDEV-Interim-Report.pdf

[3] Outstanding Amount: $8,047,473,000 as of June 30, 2023, see TMC Q2 2023 Report p.7 Note 11 and p.6. https://docs.transmountain.com/Corporate-Reports/TMC-FS-6-30-23-Final.pdf TMP Finance debt is $1.1 billion greater than the debt and equity advanced to TMC because TMP Finance has been incurring ongoing losses due to interest expense that exceeds revenues it receives from TMC. Since interest in kind is added to the debt load as an accommodation for the inability of TMC and TMP Finance to meet their current obligations, debt owed to the Canada Account will continue to mount.



CDEV Organizational Chart, with Trans Mountain entities highlighted in red. Source: CDEV 2022 Annual Report (emphasis added)[4]

[4] CDEV 2022 Annual Report, online: https://cdev.gc.ca/wp-content/uploads/2023/05/FINAL-CDEV-English-Annual-Report-2022.pdf.pdf

2. Trans Mountain cannot meet its financial obligations

Information Request 1.4(d) states "Confirm whether tolls as proposed in Trans Mountain's Application "could cause Trans Mountain to be unable to meet its financial obligations. […] If they could cause this, explain in detail, and discuss how this should factor into the Commission's decision on the Application."

Trans Mountain's response suggests that TMC can meet its financial obligations – albeit, barely – under the applied-for tolls scenario set out in table 1.4-3. However, the table excludes TMP Finance, and relies on 2024 being a full year of operation of the expansion even though Trans Mountain knows this timeline is not achievable. Further, the interim tolls proposed in Trans Mountain's Application are likely to cause Trans Mountain to be unable to meet its financial obligations because the methodology upon which the tolls are based will not generate sufficient revenue for Trans Mountain to be financially viable in the short term, while the interim tolls are in place, nor in the long term while final tolls are in place. The fundamental failure of the toll methodology to enable Trans Mountain to meet its financial obligations should factor heavily in the Commission's decision on the Application.

It is not in the interest of Trans Mountain, Tsleil-Waututh Nation, the shippers, the Commission, any community along the system's route, or the Canadian public for Trans Mountain to fail to meet its financial obligations during the period under which interim tolls are in force.

TWN respectfully submits that the Commission re-visit the approved RH-001-2012 toll methodology when determining whether the applied-for Commencement Date Tolls are just and reasonable, not simply examine whether Trans Mountain has calculated the tolls in accordance with the agreed-upon formula specified in the Facility Support Agreement (FSA).

Trans Mountain defines financial obligations as "the ability for the revenue generated from tolls to pay Trans Mountain's operating expenses, capital projects, service debt (interest and principal), and a reasonable return to equity holders."[5]

Trans Mountain relies on an incomplete financial picture in responses 1.4 (e) and 1.4(f) and in the financial comparisons to conclude that the interim tolls may be sufficient to meet its financial obligations.

Trans Mountain's inability to meet its financial obligations under the interim tolls becomes apparent when a complete and more realistic picture of Trans Mountain's financial situation is presented.

To illustrate the impact of the applied-for Commencement Date Tolls, Trans Mountain provides various forecast scenarios. Regrettably, Trans Mountain has not presented an accurate picture

[5] Trans Mountain Pipeline ULC, Responses to CER Information Request No. 1, Application for Approval of Interim Commencement Date Tolls and Related Matters, August 16, 2023, p.20.

of its financial situation or its capitalization. TWN submits that the Commission should direct Trans Mountain to re-file its responses to IR1.4 to include TMP Finance in order to determine whether it can meet its financial obligations, including operating expenses, capital projects, service debt (interest and principal), and a reasonable return to equity holders.

3. The Fair Return Standard

Trans Mountain's response to the Commission's request draws on the Fair Return Standard framework applied during the toll hearing as the basis for establishing the requirements that must be met.

Trans Mountain states that the National Energy Board (NEB) was satisfied that the requirements of the Fair Return Standard had been met in the toll methodology (RH-001-2012) because "Trans Mountain believes that it has a reasonable opportunity to recover its cost of capital under the proposed toll methodology."[6]

Under the Fair Return Standard, the return must (A) be comparable to the return available to other enterprises of like risk; (B) enable the financial integrity of the enterprise to be maintained; and (C) permit incremental capital to be attracted on reasonable terms and conditions. We go into further detail on these components, below.

A. Comparable return & cost of capital
Trans Mountain avoids discussion of expected return measured against comparable investment opportunities in its response. Trans Mountain asserts that the Fair Return Standard has been met because a decade ago, when the methodology for determining interim tolls was approved, Trans Mountain "believed" it had a reasonable opportunity to recover its cost of capital.

Trans Mountain's cost of capital was clearly established in 2012, and therefore any reference to "beliefs" held in 2012 must be put in the context of the expectations those beliefs were based upon, and steps that would be taken if those beliefs became threatened.

Trans Mountain stated in 2012, "KMP (Kinder Morgan Partners) targets its unlevered internal rates of return for pipeline infrastructure investments over their economic life in a typical range of 12% to 15%."[7] The company "would not proceed with a project that did not meet its targeted IRR for pipeline infrastructure".[8] In other words, Kinder Morgan would not have proceeded with Trans Mountain's expansion once it failed to meet its targeted IRR and this application would not be before the CER.

The NEB understood Trans Mountain's 12 – 15% cost of capital to be typical at that time as it stated in its Decision RH-001-2012, "The investment decision criteria included a targeted

[6] Trans Mountain Pipeline ULC, Responses to CER Information Request No. 1, Application for Approval of Interim Commencement Date Tolls and Related Matters, August 16, 2023, p.20.
[7] Trans Mountain Expansion Toll Methodology Hearing, Information Request Response to CAPP IR 3(c), p.5. I
[8] Ibid.

unlevered internal rate of return in the **typical** range of 12 percent (12%) to 15 percent (15%)."[9] (emphasis added)

In its IR response, Trans Mountain does not remind the CER what it believed its cost of capital to be when the toll methodology was approved. Trans Mountain confirmed during the toll methodology hearing that it was an unlevered 12 – 15%. This is the cost of capital Trans Mountain believed it needed to recover for the Fair Return Standard to be met.

In its response Trans Mountain does not indicate that there has been a change to its cost of capital – to its required rate of return—since the toll methodology hearing. In fact, Trans Mountain's response to the CER suggests the opposite: that there has been no change to the benchmark. By referencing Decision RH-001-2012 in support of the satisfying the Fair Return Standard, Trans Mountain is representing that its cost of capital to be recovered is the same now as it was when the toll methodology was approved.

Trans Mountain's unlevered 12 – 15% return would have been achieved in 2012 because the terms of the toll methodology ensured that Trans Mountain's tolls for committed shippers would provide 7 cents for every $100 million invested in the project up to and including the CPCN cost estimate.

When Decision RH-001-2012 was released, the budget for the expansion project was $5.4 billion and the cost was to be fully reflected in tolls charged to committed shippers.[10] When the CPCN Cost Estimate was delivered in 2017, Trans Mountain continued to believe it had a reasonable opportunity to recover its cost of capital since the CPCN Cost Estimate indicative tolls continued to reflect 7 cents for every $100 million invested.

Trans Mountain's 'reasonable' opportunity to recover its cost of capital began to erode in 2017 when the project budget began to exceed $7.4 billion, and Trans Mountain increasingly bore project costs.[11] With the current expected cost having increased by $23.5 billion from the CPCN Cost Estimate to the current $30.9 billion cost estimate announced in March 2023, Trans Mountain now bears 68.84% of the cost overruns with only 31.16% of the cost overruns passed onto shippers in the form of higher tolls.[12]

It is impossible for Trans Mountain to recover its cost of capital—its commercially determined, and commercially comparable required rate of return—when the toll methodology results in tolls that no longer generate sufficient revenue capable of recovering cost of capital.

[9] NEB, Reasons for Decision, RH-001-2012, May 2013,p.23.
[10] Trans Mountain Pipeline ULC, Appendix 9 Final Form of the FSA TSA Schedules, January 10, 2013,
[11] Robyn Allan, Trans Mountain: Compromised viability to cost taxpayers more than $17 billion, West Coast Environmental Law, October 2022, p. 22 – 23.
[12] Trans Mountain Pipeline ULC, Responses to CER Information Request No. 1, Application for Approval of Interim Commencement Date Tolls and Related Matters, August 16, 2023, p.7.

Kinder Morgan, Trans Mountain's owner and source of project financing in 2012,[13] was clear in its representations to the NEB that if the project proceeded to a point where its return—its cost of capital—could not be covered, it would not proceed with the project. Trans Mountain's cost of capital was an unlevered 12 – 15%. This is the rate Trans Mountain thought to be consistent with the Fair Return comparable investment opportunity standard, the rate that would enable it to meet its financial obligations and the rate that would attract capital. This is the rate of return that Kinder Morgan believed it had a reasonable opportunity to recover, and without that belief, the company would have terminated the project.

Not only has Trans Mountain failed to remind the Commission what its cost of capital requirement was at the time its toll methodology was approved in 2012, it has also not provided the Commission with any information on rates of return achieved by "other enterprises of like risk" in the current market. Trans Mountain in its response, including Table 1.4-3, has presented financial information and ratios that do not address the issue at all.

The market currently expects reasonable rates of return to have remained in the "typical range of 12 – 15%." For example, Enbridge Inc. recently announced its tolling agreement in principle for the Mainline system and confirmed that "Mainline will earn 11% to 14.5% returns, on a deemed 50% equity capitalization, throughout the term of the agreement, which is similar to the returns earned on average during the previous tolling agreement."[14]

In summary, setting tolls at the applied-for interim toll rates will result in insufficient revenue for Trans Mountain to cover its cost of capital and therefore, this element of the Fair Return Standard has not been met. The reason the interim tolls generate insufficient revenue is because the toll methodology is fundamentally flawed when applied to the current budget.

B. Maintaining financial integrity

Trans Mountain's reliance on TMC and not TMP Finance's books suggests that they can maintain financial integrity with the applied-for tolls. However, when taking TMP Finance into consideration, including the $33 billion[15] debt owed to the Canada Account and Syndicated bank loan by year end 2023, it is clear that Trans Mountain's financial integrity is compromised by tolls that collect less than half of the cost of construction. The Commission should require Trans Mountain to reproduce table 1.4-3 using TMP Finance's financial obligations.

C. Capital attraction

Trans Mountain avoids discussion about the capital attraction element of the Fair Return Standard. TWN submits that it is evident and obvious that this element is not met simply by the

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[13] National Energy Board, Trans Mountain Report – Reconsideration, MH-052-2018, February 2019, p. 343.

[14] Enbridge Inc., Enbridge announces tolling agreement in principle on Mainline liquids system, Press Release, May 3, 2023.

[15] Outstanding debt as of June 30, 2023 is $28.6 billion including $16.5 billion owed to the Canada Account and $12.1 billion owed to the Bank Syndicate, see CDEV Q2 2023 Report: https://cdev.gc.ca/wp-content/uploads/2023/08/Q2-2023-CDEV-Interim-Report.pdf. In addition, interest in kind will be added to the Canada Account debt in the amount of $400 million by year end and the Syndicated Loan limit has increased from $13 billion to $16 billion. By year end, Trans Mountain anticipates at least $33 billion in debt outstanding ($28.6 + .4 + 4 = $33 billion). Recent reporting in financial statements indicate that $16 billion in syndicated debt will be insufficient and therefore, by year end debt owed will exceed $33 billion.

fact that Trans Mountain has required $16 billion in loan guarantees from the federal government[16] in order to persuade Canadian banks, including RBC, TD, BMO, Scotiabank, CIBC and National Bank to participate in the syndicated loan. TWN notes that loan guarantees are considered subsidies by the World Trade Organization.[17]

In summary, even a cursory review of the Fair Return Standard reveals that the applied for tolls and Trans Mountain's situation as a whole fail all three elements of the Standard.

4. The capitalization of Trans Mountain is 100% debt.

There is no change in the capitalization picture between a consolidation of TMP Finance and a consolidation of its owner CDEV. Thus, an appropriate cut off in the corporate structure when considering capitalization and ability to meet financial obligations is at the level of TMP Finance, not TMC, particularly when TMC's financial reporting presents a contrived financial picture.

For example, in its response to the Commission, Trans Mountain provides Table 1.4-3 "Trans Mountain Financial Ratios Table'." Trans Mountain represents its forecast debt for TMC in 2024 under the column "2024 As Per Corporate Plan" as $23.8 billion. Trans Mountain does not provide any further breakdown as to the components that make up this debt. The $23.8 billion consists of a forecast of $15.1 billion in third-party debt from a syndicate of commercial banks due on March 24, 2025, and $8.7 billion consisting of debt owed to TMP Finance due August 29, 2025.[18]

In its TMC financial reporting and its Table 1.4-3, "2024 As Per Corporate Plan," Trans Mountain represents its equity as $9.4 billion consisting of $7.4 billion as paid in capital from TMP Finance (which is debt TMP Finance owes to the Canada Account) and $2 billion in retained earnings.[19] This breakdown is provided in CDEV's 2023 – 2027 Corporate Plan Summary as Trans Mountain's net earnings in 2023 are added to its equity position in 2024.[20]

However, TMP Finance's forecast debt from the same Corporate Plan Summary is $32.9 billion consisting of $15.1 billion in third-party debt from a syndicate of commercial banks guaranteed

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[16] EDC Canada Account Website: https://www.edc.ca/en/about-us/corporate/disclosure/reporting-transactions/canada-account.html

[17] https://www.wto.org/english/res_e/booksp_e/anrep_e/wtr06-2b_e.pdf

[18] 2023 – 2027 Corporate Plan Summary, Trans Mountain Corporate Plan Summary, p.29. The Syndicate Loan is identified as Short term debt and the debt owed to TMP Finance is listed as Long term debt. Maturity dates for the loans: CDEV, Consolidated Financial Statements, June 30, 2023, p. 24, Note 11 and Trans Mountain Corporation, Condensed Consolidated Financial Statements, June 30, 2023, p. 11-12.

[19] Trans Mountain's inclusion of $2 billion retained earnings in its presentation is inappropriate given that this quantum has resulted primarily from an accounting allowance for equity funds used during construction (AFUDC) allowed under US GAAP. This equity allowance inflates TMC's earnings on paper but does not generate cash flow. At no time has Trans Mountain alerted the CER to the fact that Table 1.4-3 is based on a reliance on US GAAP and the considerations needed when inferring financial performance based on this approach.

[20] 2023 – 2027 Corporate Plan Summary, Trans Mountain Corporate Plan Summary, p.29-30.

by the Canada Account and $17.8 billion owed to the Canada Account for debt incurred to purchase and expand the Trans Mountain system.[21]

Trans Mountain's debt load projected for 2024 in the Corporate Plan Summary is not $23.8 billion as presented in Trans Mountain's IR response. It is $9.1 billion higher at $32.9 billion.

Trans Mountain's financial obligations to service this debt (principal and interest) viewed against the backdrop of its actual debt load reveals that the interim tolls are insufficient to meet these financial obligations.

It is the interest and principal on $32.9 billion that Trans Mountain should have presented as its financial obligation in its response to the CER, not the more favourable truncated picture of $23.8 billion. Trans Mountain, without explanation, has removed approximately $450 million in annual interest expense and over $9 billion in debt principal from the presentation of its financial obligations.

Trans Mountain states that "currently, Trans Mountain's capitalization is largely reliant on debt and equity provided by its owner and a third-party revolving credit facility guaranteed by Trans Mountain's ultimate owner. The current capital structure relies heavily on relatively short-term debt financing with more permanent financing not determined at this time. Given the transitory nature of the current capital structure, a recapitalization of Trans Mountain is also presented."

Trans Mountain's capitalization is 100% reliant on debt while Trans Mountain attempts to characterize its capitalization as "largely reliant on debt and equity…".

The capital structure is, as Trans Mountain states, supported by short term financing since a projected $32.9 billion is due for repayment in 2025 and more permanent financing has not been determined. Trans Mountain recognizes how vulnerable its financial position is (even under the favourable yet false representation of its obligations as presented by TMC), when it concedes that more permanent financing has not been determined.

Without more permanent financing Trans Mountain is at risk of loan default while the interim tolls, if approved, are in place. Instead of addressing this precarious situation, Trans Mountain presents a recapitalization scenario without any approval authority or explanation of how such a transformation of its vulnerable situation might or could occur. Trans Mountain's recapitalization scenario cannot be relied upon.

Trans Mountain understands that it is under threat of ceasing to operate as a going concern—of ceasing to meet its financial obligations—as reflected in the notes to the most recent financial statements for CDEV and TMC. That is, not only is TMC under threat of ceasing to meet its obligations in the next 12 months, its contrived capital structure notwithstanding, the debt load

[21] 2023 – 2027 Corporate Plan Summary, CDEV Corporate Plan Summary, p.26 Recognizing that the figures in the Corporate Plan Summary in turn are too low given the recent increase in debt from third parties.

incurred by TMP Finance on behalf of Trans Mountain threatens to take CDEV with it. In TMC's 2023 Consolidated Financial Statements, TMC writes:

> ***Going Concern***
> *The condensed consolidated financial statements have been prepared on a going concern basis in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"). The going concern basis of presentation assumes that TMC will continue in operation for at least one year after the date the condensed consolidated financial statements are issued and contemplates the realization of assets and settlement of liabilities as they become due in the normal course of business. The Corporation's ability to continue as a going concern is dependent upon its ability to service its existing debt and fund the remaining construction costs of the TMEP. On February 18, 2022, the Deputy Prime Minister and Minister of Finance reaffirmed the government's commitment to complete the TMEP; however, the Minister stated that TMC needed to secure external financing to fund the remaining costs of the project. On April 29, 2022, TMC entered into a credit agreement with a syndicate of lenders (the "Syndicated Credit Agreement") for a one year facility (the "Syndicated Facility") for $10.0 billion. On March 24, 2023, the Syndicated Credit Agreement was amended and restated to increase the total available credit to $11.0 billion, which included a letter of credit facility ("LC Facility") for $100 million, and the maturity date was extended to March 24, 2025. On May 2, 2023, the combined available credit was increased to $13.0 billion. Subsequent to period end, on July 20, 2023, the Syndicated Facility was increased to $15.9 billion for a combined available credit under the Syndicated Credit Agreement of $16.0 billion. In order to meet obligations as they become due, TMC will require additional funding through external financing. TMC expects the external financing will be obtained in a timely manner and on terms satisfactory to TMC. However, there is no assurance that external financing will be obtained.* ***The above factors cause material uncertainty that casts substantial doubt as to TMC's ability to continue as a going concern***.[22] (emphasis added)

Similarly, CDEV's most recent quarterly financial statement includes disclosure of material going concern challenges due to its obligation to service Trans Mountain's existing debt and fund the remaining costs of Trans Mountain's expansion. The inadequacy of the $16 billion limit in external financing is also highlighted. CDEV states that, "As at June 30, 2023, there is material uncertainty that the Corporation (CDEV) has sufficient financial resources to meet its obligations for the next 12 months as they become due."[23]

Trans Mountain is not able to meet the third requirement of the Fair Return Standard—the capital attraction requirement—under the applied-for interim tolls. The external funding that Trans Mountain has sourced (currently a syndicated loan from commercial banks in the amount of $16 billion) required a loan guaranteed from the federal government, which is evidence that

[22] Trans Mountain Corporation, Consolidated Financial Statements, June 30, 2023, p.7.
[23] Canada Development Investment Corporation, Consolidated Financial Statements, June 30, 2023, p.16.

Trans Mountain is unable to attract incremental capital on reasonable terms and conditions. That is, without the full force of the taxpayers of Canada behind it, Trans Mountain would not have been able to attract capital to continue to fund the project.

5. Trans Mountain's recapitalization strategy is not credible

Trans Mountain's recapitalization strategy is not credible because it does not begin with an accurate presentation of Trans Mountain's capitalization which is 100% debt—not 72% debt as presented in Table 1.4-3.

Having recognized that the scenario begins from the wrong position, and therefore is not representative of the obligations Trans Mountain faces, it would also be prudent to consider Trans Mountain's forecasts within the context of Trans Mountain's forecasting track record over the past decade.

Trans Mountain states in its response that a "recapitalization of Trans Mountain is assumed to take place during 2024." Trans Mountain assumed in 2012 that the project would cost $5.4 billion. As recently as February 2022, Trans Mountain assumed the project would cost $21.4 billion. One year later, Trans Mountain released their updated project cost estimate of $30.9 billion. Not only does Trans Mountain suffer from an inability to forecast accurately or reliably, and therefore its pro forma statements need to be viewed with scepticism, but further, the assumptions underlying the generation of the recapitalization scenario are without substance.

Trans Mountain claims that a recapitalization of TMC (not TMP Finance which is the entity that should be included in its scenarios) resulting in 45% equity and 55% debt will allow "existing short-term facilities to be paid off and legacy government funded debt will be replaced with market debt". At the very least, Trans Mountain should have provided more detail as to what short-term facilities would be paid off and what government funded debt would be replaced as this would have assisted in identifying the apparent lack of reliability in this claim.

The Government of Canada is on record as stating no further public funds for the expansion project will be forthcoming, so the only source of funds to recapitalize Trans Mountain would need to come from external parties. Given the risks and uncertainties inherent in Trans Mountain's revenues, expenses, future cost of financing and principal repayment, a recapitalization away from 100% debt financing, based on market realities, is unrealistic.

Trans Mountain's third-party debt is predicted in the Corporate Plan Summary as $15.1 billion in 2024. However, the debt facility has already reached $16 billion[24] and will likely reach or exceed $18 billion by year end 2023.[25]

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[24] Canada Account Transactions, August 7, 2023. And CDEV Q2 2023 report Supra n.2

[25] Canada Development Investment Corporation, 2019-2023 Corporate Plan Summary, p. 36. "Additional funding sources atop those previously contemplated are required to finance the completion of TMEP construction activities. Incremental funding could range between $3 and $5 billion." And, Canada Development Investment Corporation, Consolidated Financial Statements, June 30, 2023, p.16.

With Trans Mountain confirming that project operation is now expected later in quarter one of 2024[26], that debt will likely be higher, even if project costs do not increase beyond $30.9 billion. Canada Account funded debt incurred by TMP Finance, which Trans Mountain says will be replaced with market debt, is forecast to reach $17.8 billion by 2024.[27] This means that by year end 2024, a more reasonable forecast for debt incurred to purchase and expand Trans Mountain is $36 billion ($18 billion in third-party debt plus $18 billion in government funded debt).

Even a rough approximation of the financial challenges this represents exposes the lack of reasonableness in Trans Mountain's recapitalization scenario. A $36 billion debt load under current interest rates would require a cash flow in excess of $2 billion a year for interest expense alone.[28] This burden is reflected in the now outdated Five-Year Corporate Plan Summary as TMP Finance in 2024 is forecasted to pay $1.7 billion in interest expense on a debt load incurred for Trans Mountain of $32.9 billion.[29]

6. Trans Mountain cannot service principal repayment on its debt

Trans Mountain's third-party debt is due for repayment on March 24, 2025, while its debt owed to the Canada Account is due for repayment on August 29, 2025.[30] There is no question that without debt roll-over or restructuring, Trans Mountain faces insolvency since its revenue stream from interim tolls are insufficient to meet approximately $36 billion in debt obligations. Trans Mountain recognizes this and confirms that "continued funding from Canada is not assumed in this (recapitalization scenario) illustration." Absent funding from Canada or full guarantee of its debt, it is unclear how Trans Mountain can recapitalize since the market has indicated an unwillingness to do so on market terms. As a result, TWN submits that the Commission should give little to no weight to this scenario unless Trans Mountain can demonstrate that it is likely and reasonable.

Trans Mountain provides a framework for meeting its debt obligations as illustrated in Table 1.4-3. The first column "2024 as Per Corporate Plan" indicates an intention to repay $1 billion in loan principal. However, this debt repayment is not included in the 2024 Corporate Plan, and therefore would not have been approved by Trans Mountain's owner or Treasury Board as part

[26] Trans Mountain Pipeline ULC, Responses to CER Information Request No. 1, Application for Approval of Interim Commencement Date Tolls and Related Matters, August 16, 2023, p.38.
[27] Canada Development Investment Corporation, 2019-2023 Corporate Plan Summary, p. 26. Trans Mountain's debt obligation continues to mount as, further to a credit facility amendment in 2022, interest expense is paid as interest in kind and added to the loan balance semi-annually on June 30 and December 31.
[28] An effective interest rate of 5.2% is derived from the 2023 Corporate Plan Summary on debt expected by TMP Finance for 2024. However, interest rates have increased since the Plan was produced affecting the interest expense on third-party borrowing given the variable rate feature of the Syndicated Loan tied to the Canadian Prime Rate. In CDEV and TMC's Q2 Financial Reports, the effective interest rate has risen to 5.7% for the first 6 months of 2023 as compared to 5.2% for the first 3 months, and the Prime Rate rose a further 50 basis points in July. An effective interest rate of 5.7% (which is likely conservative) represents an expense in excess of $2 billion per year on $36 billion.
[29] Canada Development Investment Corporation, 2019-2023 Corporate Plan Summary, p. 29.
[30] CDEV, Consolidated Financial Statements, June 30, 2023. Supra, note 18, p. 24

of the process for tabling this plan. There is an issuance of $300 million in additional loans for 2024 included in the Plan, not a repayment of any loan balance. For clarity, all other figures presented in the first column of Trans Mountain's response correspond to amounts presented in the Corporate Plan for TMC; however, there are no financial ratios provided in the Corporate Plan.

Trans Mountain then presents a scenario for 2024 – 2026 of TMC's "existing capitalization" which updates TMC's figures since the Corporate Plan was approved and assumes Trans Mountain's expansion becomes operational on January 1, 2024. As detailed above, TMC's capitalization is not Trans Mountain's capitalization. Trans Mountain's capitalization is 100% debt and the ratios provided in the pro forma statements are effectively meaningless. As also detailed above, Trans Mountain confirms a start-up date later in Q1 2024, not January 1, 2024, as reflected in its pro forma statements.

Unfortunately, Trans Mountain does not provide sufficient information to fully explain what has driven the changes to the figures it presents in the "existing capitalization" scenario. Information that is available suggests that Trans Mountain's "existing capitalization" scenario for TMC overestimates revenue and underestimates expenses and debt load even if a January 1, 2024, start-up date is assumed.

For example, the debt load for TMC is presented as $24.1 billion up from $23.8 billion in the Five-Year Corporate Plan Summary (consisting of $15.1 billion in external and $8.7 billion in TMP Finance debt). The $24.1 billion is an increase in debt of only $400 million while CDEV and TMC have indicated in their most recent quarterly financial report that the current $16 billion loan facility with a syndicate of banks is insufficient to meet funding requirements to complete the project. Third party debt incurred by TMC is already on track to exceed $16 billion, and will likely exceed $18 billion going into 2024, and yet, Trans Mountain is representing it as $15.5 billion in its "existing capitalization" scenario.[31] There are billions missing from TMC's expected debt obligations to third party lenders.

Further, the financial impact of Trans Mountain's realistic start-up date needs to be incorporated into its pro forma statements. All pro forma statements presented assume a full year of operation in 2024 which fundamentally compromises their reliability given that Trans Mountain knows this scenario will not be achieved.

On August 31, 2023, Trans Mountain informed the Commission that "each month of delay in the TMEP in-service date results in roughly $200 million in lost revenues and roughly $190 million in carrying charges for Trans Mountain."[32] Trans Mountain would have been aware of these costs when it filed its reply to the Commission's information request and yet, presents

[31] The debt owed to related parties increases based on interest in kind and therefore is not expected to deviate from the $8.7 billion estimate in the Five-Year Plan, hence any change in the debt from the Plan to the 'existing capitalization' scenario would need to be attributed to external financing.
[32] Trans Mountain Pipeline ULC, Deviation Application filed on August 10, 2023, Reply Evidence, File OF-Fac-Oil-T260-2013-03 61, p.3, para. 15.

scenarios that exclude the revenue and carrying charge impact of a later than January 1 start up.

On August 29, 2023, Trans Mountain stated in a press release that "we are currently planning and targeting the commencement of service on the expanded pipeline system near the end of the first quarter of 2024."[33]

Trans Mountain conceding that it expects up to three months of carrying costs and delayed revenue in 2024 but then providing financial pro forma statements that include 12 months of operation along with the increased revenue and lower carrying costs a full year's operation represents is misleading and materially obfuscates a reliable picture of its financial prospects.

Assuming Trans Mountain's in service date is "near the end of the first quarter", a reduction of as much as $600 million in revenue and $570 million in increased carrying costs should have been reflected in the financial pro formas. Doing so would have clearly indicated that Trans Mountain is unable to meet its financial obligations in 2024, even under its contrived capital structure.

The recent information on the monthly financial impact of continuing construction activity beyond January 1, 2024, as provided by Trans Mountain, leads to the conclusion that Trans Mountain's pro forma statements provided in Table 1.4-3 are highly inaccurate and unreliable simply based on a late Q1 start-up date. The estimation error inherent in providing a full year of operation when none is expected, cascades into ensuing years.

For purposes of further illustrating Trans Mountain's inability to meet its financial obligations, we will use the second column in Table 1.4-3 "Existing Capitalization 2024."

In this scenario, Trans Mountain projects $3.1 billion in total revenue and $1.4 billion in expenses, for an operating income of $1.7 billion. After deducting $1.6 billion in interest expense, net income is forecasted to be $100 million. According to Trans Mountain, its expected start up in late March would reduce revenue by approximately $600 million and increase carrying costs by approximately $570 million. Presumably, some of the carrying cost charges would relate to construction costs and some would relate to further debt and interest expense although the breakdown allocation to expenses and capital are not clear. Regardless, a summary estimate of impact would see revenue fall to $2.5 billion, expenses rise and interest expense rise. A net loss far in excess of $500 million would be expected in 2024.

Trans Mountain presents its cash flow as operating income plus depreciation to arrive at $2.5 billion and uses this cash flow to pay interest expense ($1.6 billion), fund sustaining capital ($0.4 billion)[34] and repay debt ($0.6 billion). However, interest expense on debt incurred for Trans Mountain in 2024 will be at least $2 billion leaving $0.5 billion to fund sustaining capital

[33] Trans Mountain Corporation, Trans Mountain Corporation Releases Second Quarter 2023 Results, August 29, 2023.
[34] It should be noted that Trans Mountain lowered its approved level of anticipated spending on sustaining capital by $0.2 billion from the Corporate Plan but has not explained why it has done so.

and debt principal assuming a full year's operation. As explained below, Trans Mountain's revenue stream, even assuming a full year of operation, is likely overstated leaving Trans Mountain with insufficient funding to cover any debt principal repayment and compromise its ability to fund sustaining capital even if the expansion were to start up by January 1, 2024.

Trans Mountain states that "debt repayment is an important consideration in the scenarios. Before debt repayment is provided in the scenarios, Trans Mountain has assumed working capital deficiencies are corrected by funding construction and contractor retainage accounts payable to contractors in 2024. These payables will need to be addressed during the first year of operations and existing debt will be repaid over 25 years in equal installments beginning in 2025." Twenty-five equal installments beginning in 2025 on $36 billion in debt requires free cash flow of $1.44 billion a year.

It is unclear why Trans Mountain would amortize the debt repayment over a 25-year period when it understands the more appropriate time horizon to be 20 years. This is the time horizon Trans Mountain gave as appropriate at the toll hearing since once the contracts expire the revenue risk is too great to expect loan repayment.[35]

More recently, Trans Mountain relied on the International Energy Agency's (IEA) Announced Pledges Scenario and the CER's Canada's Energy Futures 2021 report to confirm a 20-year time horizon. Supply and demand realities portend significant excess pipeline takeaway capacity by 2045 when Trans Mountain's firm service contracts expire. In its 2022 Environmental, Social and Governance Report, Trans Mountain writes, "by 2045, the Announced Pledges Scenario describes circumstances in which Western Canadian supply is 29 per cent lower than 2021 levels and refinery demand in North America is 45 per cent lower than 2021 levels. While the Announced Pledges Scenario also provides data on oil and carbon prices, we focused on modelling supply and demand because they are more directly linked to demand for pipeline transportation."[36]

Amortizing $36 billion over 20 years requires debt repayment of $1.8 billion a year. What this means is that in 2025, Trans Mountain requires a minimum of $3.8 billion in cash flow ($2 billion in interest expense and $1.8 billion in debt repayment) to meet its interest expense and prudent debt repayment obligations. Trans Mountain's Existing Capitalization scenario fails to meet its financial obligations by $1.2 billion in 2025 and $1.1 billion in 2026 even if its optimistic scenarios, including a January 1, 2024, start-up date, are accepted.[37] The inability to meet its obligations is further compromised when more a realistic estimate of transportation service revenue is considered.

[35] Trans Mountain Expansion Toll Methodology Hearing, February 13, 2013, Volume II Transcripts, Paras 1894 - 1895.
[36] Trans Mountain 2022 ESG Report, p. 62.
[37] Trans Mountain's interest expense under its Existing Capitalization Scenario suggests an effective interest rate of 6.6% (rather than the 5.2% effective rate mentioned in its Q1 Financial Statements. It is unclear how the interest expense net of capitalization has obfuscated Trans Mountain's cash flow interest obligation.

7. Trans Mountain has embellished its revenue stream

During the toll methodology hearing Trans Mountain explained that its projected revenue stream did not include spot capacity revenue as Trans Mountain considered it to be too risky to include this revenue in its projections. The revenue Trans Mountain relied upon was revenue to be generated from firm capacity of 707,500 barrels a day.[38] Trans Mountain did not undertake a forecast for the potential demand of the uncommitted capacity. This was confirmed by two Trans Mountain representatives in the tolling methodology hearing:

> 390. **MR. BERGNER** [for Chevron]**:** In terms of the 20 percent, which is uncommitted capacity, am I correct in understanding Trans Mountain has not undertaken a forecast of the needs of uncommitted capacity over the 15 or 20-year period?
>
> 391. **MR. MacFARLANE** [for Trans Mountain] That's correct.[39]
>
> […]
>
> 411. **MR. BERGNER** …are you suggesting that Trans Mountain was unable to make a forecast or simply felt that a forecast of the needs of uncommitted capacity was simply unnecessary?[40]
>
> […]
>
> 415. **MR. STONESS** [for Trans Mountain]: The current usage of those shippers (Washington State and BC destinations that did not sign on for committed capacity) is less than the 180,000 spot that we have available. In addition to that, our pipeline is going from size of 300,000 barrels to 890,000 barrels. We consider that, in a likely scenario where those shippers (uncommitted shippers) have more usage in the future, they will likely get that from the contracted shippers.[41]

Trans Mountain's scenarios in Table 1.4-3 assume 96% capacity utilization, not the 80% capacity utilization Trans Mountain relied on for financial representations made during the toll methodology hearing. There is no indication to the CER in its response that the basis upon which Trans Mountain is now projecting its financial resources has fundamentally changed. Trans Mountain acknowledges that "if only the contract volumes were to move, the resulting financial performance and coverage of interest and debt repayment would be weaker in each of the scenarios."[42]

Trans Mountain should have included scenarios that reflect the revenue stream generated by firm commitments since this is the only revenue that can be reasonably relied on. Estimates based on firm contracts would better serve the CER in its understanding of the financial risks

[38] Trans Mountain ULC, Toll Methodology Hearing, Appendix to CAPP IR 1.3, January 10, 2013.
[39] Toll Methodology, Transcript 1, para. 390-391.
[40] Toll Methodology, Transcript 1, para. 411.
[41] Toll Methodology, Transcript 1, para. 415.
[42] Trans Mountain Pipeline ULC, Responses to CER Information Request No. 1, Application for Approval of Interim Commencement Date Tolls and Related Matters, August 16, 2023 at p. 21 Supra, n. 1

Trans Mountain faces because of the toll methodology, should the interim tolls be approved as applied for.

Trans Mountain confirms that the spot capacity included in the revenue stream is 144,000 barrels per day but has not indicated the revenue this represents in its revenue figure presented in all scenarios for 2024 – 2026. Trans Mountain has not alerted the CER to the fact that after 85% capacity utilization, toll revenues from spot capacity are shared 50/50 with the shippers. It is unclear if Trans Mountain has properly recorded this impact by netting the revenue sharing off before including it in revenue, deducting it in expenses if it is included in revenue, or otherwise making an accommodation for the revenue captured by shippers.

Regardless, a conservative estimate of the annualized impact of spot barrels would put the revenue generation from spot barrels at approximately $440 million in 2024.[43] This amount should be removed from Trans Mountain's revenue stream to better reflect likely revenues.

Trans Mountain knows that capacity demand from shippers who currently use the pipeline can be met by firm shippers who do not require all the capacity they have contracted for but are obligated to pay the fixed toll. Trans Mountain knows that this capacity can be sold at a discount to the posted uncommitted rate and therefore potential spot shippers have an incentive to buy capacity in the secondary market rather than directly from Trans Mountain. Trans Mountain did not include revenue from spot capacity sales in its initial projections of viability because of the uncertainty inherent in this revenue.

Trans Mountain has now presented scenarios as if there is a strong likelihood this capacity will be utilized. Although the applied-for interim tolls are not high enough to cover Trans Mountain's financial obligations, they are considered too be too high to be competitive as evidenced by the representations made by other intervenors to this process. This further compromises the likelihood of uncommitted shippers to seek spot capacity on the expansion. Without addressing any of these issues, Trans Mountain simply asserts an additional $400 million a year, plus, in revenue.

In addition to the opportunity for potential spot capacity shippers to satisfy their demand with capacity allocated to firm barrels, there is also evidence uncommitted shippers are already sourcing alternatives to Trans Mountain for meeting their refinery demand.

HF Sinclair owns the Puget Sound refinery located in Anacortes, Washington. The refinery has a capacity of 149,000 barrels per day. During HF Sinclair's Q1 2023 Investor Call an analyst asked for comment on the Trans Mountain pipeline and how it might impact the economics of the Puget Sound refinery. As discussed at their First Quarter 2023 Earnings Release and Conference webcast (May 4, 2023):

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[43] 144,000 barrel per day x 365 = 52,560,000 barrels x (11.97 uncommitted fixed base rate + .58 variable) = $659,628,000. Netting off cost sharing of 5% capacity to reflect shipper share of revenue ($660 million/3) x 2 = $440 million revenue to Trans Mountain for forecasted spot capacity utilization of 15%.

> …keep in mind that our Puget Sound refinery can also run 100% ANS (Alaska North Slope) crude from the water; that we are one of the few refineries in that area that can do that, so we have the ability to switch back between ANS and these Canadian crudes which gives us extra flexibility to take advantage of this volatility that we'll no doubt see over the next couple of years and so as…as of today it makes more sense to try to bring in as much of the Canadian crude as we can but in the future it may make sense to bring in more ANS and we can do that and optimize our portfolio.[44]

Additional issues

TWN notes that Trans Mountain has applied to the CER for a route deviation around Jacko Lake also known as Pipsell – a sacred site to Secwepemc Peoples. The Stk'emlúpsemc te Secwépemc Nation (SSN) has filed a response opposing this deviation because it reneges on commitments made by Trans Mountain that were conditional to SSN's support for the project.

SSN's submission says "Trans Mountain stated that, due to certain financial obligations, it requires the Project's In-Service Date to be January 1, 2024."[45] It is unclear what these financial obligations might be and whether they have material implications for Trans Mountain on this interim toll application in addition to the implications a later start-up date has for revenue and carrying costs. If so, it is concerning that Trans Mountain has not alerted the CER to these obligations. If not, then it is concerning that Trans Mountain is misrepresenting their position to SSN in order to justify rescinding previous commitments to a First Nation that were essential to their support for the project.

Conclusion

TWN respectfully submits that the CER cannot and should not rely on Trans Mountain's responses to IR 1, and in particular IR 1.4 to determine whether the company can meet its financial obligations.

Trans Mountain provided incomplete information in order to create the impression that the applied for tolls can maintain financial viability. By arbitrarily cutting out TMP Finance from Trans Mountain's financial picture, Trans Mountain fails to account for more than $9 billion in loan obligations by 2024.

Trans Mountain has also embellished its revenue to appear healthier than it is, without explanation, and assumes an unlikely recapitalization scenario in order to bolster the illusion of financial viability. Even with all of these manipulations and optimistic scenarios, Trans Mountain fails all three branches of the Fair Return Standard.

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[44] HF Sinclair Corporation and Holly Energy Partners, First Quarter 2023 Earnings Release and Conference Webcast, May 4, 2023, Response by Timothy Go, CEO, Begin at minute 49:15.

[45] https://docs2.cer-rec.gc.ca/ll-eng/llisapi.dll/fetch/2000/130635/4402542/C25999-2_SSN_Response_to_Trans_Mountain_s_Deviation_Application_-_A8S3E4.pdf?nodeid=4402209&vernum=-2 p.12

A more complete assessment of Trans Mountain's ability to meet its financial obligations under interim tolls must include TMP Finance, and the 100% debt capital structure, financial impact of a start-up date reflective of Trans Mountain's stated expectations, prudent debt repayment scenario, and revenue based on 80% capacity utilization. TWN submits that the CER should require Trans Mountain to refile their responses to IR1.4 using TMP Finance along with the other more realistic assumptions detailed in this submission, where it will be clear and obvious that it cannot meet its financial obligations. This is because the toll methodology does not produce just and reasonable rates at the current budget, which is not only more than 5 times the budget that the toll methodology was based upon, but results in Trans Mountain bearing more than 50% of project costs.

As a result, the toll methodology must be revisited, in TWN's submission.

All of which is respectfully submitted,

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