File OF-Tolls-Group1-E101-2019-02 02

CANADA ENERGY REGULATOR

IN THE MATTER OF the *Canadian Energy Regulator Act*, SC 2019, c 28, s 10 and the regulations made thereunder;

AND IN THE MATTER OF an application by Enbridge Pipelines Inc. for approval of the Transportation Service and Toll Methodology for the Canadian Mainline;

AND IN THE MATTER OF Hearing Order RH-001-2020.

Written Evidence of Mr. Roland Priddle

December 7, 2020

To: Mr. Jean-Denis Charlebois
Secretary of the Commission
Suite 210, 517 10 Ave SW
Calgary, AB T2R 0A8

Table of Contents

Evidence of Mr. Roland Priddle

I. INTRODUCTION

Q1. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND OCCUPATION.

A1. My name is Roland Priddle of 1150 Normandy Crescent, Ottawa Ontario, K2E 5A6.

I consult on energy economics, policy and regulation.

Q2. PLEASE PROVIDE A SUMMARY OF YOUR PROFESSIONAL BACKGROUND AND EXPERIENCE.

A2. My relevant education and professional experience includes:

- National Energy Board, Chairman and Board Member 1986-97
- Department of Energy Mines and Resources, Senior Adviser 1973-79, Assistant Deputy Minister 1979-85
- National Energy Board, Economics Branch division chief, Oil Branch director 1965-73
- Shell International, management analyst 1956-65
- University of Cambridge UK, BA, MA, University of Ottawa MA, University of California at Berkeley, incomplete MA.

My CV is included as Annex 3 to this written evidence.

Q3. IN WHICH CASES HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE CANADA ENERGY REGULATOR'S PREDECESSOR, THE NATIONAL ENERGY BOARD?

A3. I have previously provided testimony before the National Energy Board ("NEB" or "Board") in relation to the following matters:

- GH-1-2004, Mackenzie Gas Project, certificate application, 2006
- GH-1-2011, KM LNG Application to Export Liquefied Natural Gas ("LNG"), 2011
- OH-004-2011, Northern Gateway, certificate application, 2012
- GH-001-2012, Nova Gas Transmission Limited ("NGTL") Application for North West Mainline Komie North Extension, 2012

- GH-001-2014, NGTL Application for North Montney Mainline Project, 2014
- OH-002-2016, Energy East Pipeline Ltd., certificate application (evidence filed but not examined because application withdrawn)
- MH-031-2017 NGTL North Montney Mainline Project Application for Variance and Sunset Clause Extension, 2017
- RHW-002-2017 Crescent Point Part IV complaint re Westspur, December 2018 (evidence filed but not examined because applications withdrawn)

Q4. ON WHOSE BEHALF ARE YOU SPONSORING EVIDENCE IN THIS PROCEEDING?

A4. I prepared this evidence on behalf of the Canadian Shippers Group which consists of Canadian Natural Resources Limited ("Canadian Natural" or "CNRL"), TOTAL E&P Canada Ltd., MEG Energy Corp. ("MEG") and Shell Canada Limited.

Q5. WHAT INFORMATION HAVE YOU REVIEWED AS BACKGROUND TO PREPARING YOUR EVIDENCE?

A5. My review of background materials includes, but is not limited to, the following:

- the Canadian Mainline Contracting Application (C03823) (the "Application") filed by Enbridge Pipelines Inc. ("Enbridge");
- the Evidence of John J. Reed, filed by Enbridge as Appendix 5 to the Application (A7C1I7);
- the Evidence of Dr. Jeffrey Church, filed by Enbridge as Appendix 6 to the Application (A7C1I8);
- the Evidence of Neil Earnest, filed by Enbridge as Appendix 7 to the Application (A7C1I9);
- the Additional Written Evidence of Concentric Energy Advisors Inc. (Messrs Reed and Kennedy), filed by Enbridge on June 12, 2020 (A7G3D3);
- the Evidence of the Canadian Shipper Group, filed contemporaneously with this evidence;
- the Evidence of Drazen Consulting Group Inc. by Mark Drazen and Ron Mikkelsen, filed contemporaneously with this evidence;
- the Evidence of Dr. Jeff D. Makholm of NERA Economic Consulting, filed contemporaneously with this evidence;

- Relevant parliamentary and regulatory decisions, documents and reports including:
    - House of Commons Debates
    - Acts of Parliament
    - Canadian intergovernmental agreements
    - The (Borden) Royal Commission on Energy (1957-59)
    - The (Gordon) Royal Commission on Canada's Economic Prospects: Dr. Jack Davis, Canada's Energy Prospects (1955)
    - Board of Transport Commissioners' decisions
    - NEB and Canada Energy Regulator ("CER") decisions
    - NEB annual reports ("ARs") 1960-2019
- Other authorities such as Bonbright *Principles of Public Utility Rates*; Daggett *Principles of Inland Transportation*; Makholm *The Political Economy of Pipelines*; Skeet, Paul Frankel: *Common Carrier of Common Sense*; Yergin, *The Prize*.

II. SUMMARY OF EVIDENCE

Q6. WHAT IS THE PURPOSE OF YOUR EVIDENCE?

A6. The general purpose of my evidence is to assess Enbridge's Application to convert the Canadian Mainline ("the Mainline") to contract carriage from common carriage. My evidence focusses on the following aspects of regulation of the Mainline in the Canadian public interest in the context of Enbridge's proposal:

(a) The history of regulation of the Mainline since its inception, and the history of the Mainline's 70+ years' operation as a common carrier.

(b) The appropriate ranking for the Commission of the CER to give to each of the key market participants in the oil market, having regard to the Canadian public interest.

(c) The appropriateness of the proposed switch to contract carriage, and an associated exemption under the Canadian Energy Regulator Act ("CERA").

(d) The appropriateness of the Commission holding a traditional cost-of-service proceeding to determine the appropriate rates on the Mainline.

Q7. WHAT ARE YOUR MAIN CONCLUSIONS AND YOUR REASONING IN ARRIVING AT THEM?

A7. My main conclusions are as follows:

- In the context of this Application, the Canadian public interest is most closely aligned with the interests of Canadian oil producers, along with Canadian-based aggregators and refiners, and Canadian governments who benefit from the taxes and royalties generated by the producing sector.

- The Application may be responsive to supporting shippers' requests and Enbridge's desire to mitigate risk, but it is definitely not in the Canadian public interest and it should be denied.

- Common carriage has worked well throughout the 70-year history of the Mainline, it is required by the CERA, and while there are problems with this system when there is inadequate pipeline capacity from the Western Canadian Sedimentary Basin ("WCSB" or "the Basin"), there is no compelling reason to abandon it at this time.

- After 25 years of negotiated settlements, the last of which has not worked well for Canadian-based crude oil producers, it is time to rebase Enbridge's tolls according to its cost-of-service.

My reasoning in arriving at these conclusions includes consideration of the Mainline's purpose, history, performance, expansions, apportionment, risks, monopoly characteristics, toll regulation, negotiated settlements and evaluation in relation to the public interest of salient elements of the Application and of the expert evidence, partly in the light of previous relevant regulatory decisions. In summary form my reasoning is as follows:

The Enbridge Mainline was conceived, approved, and regulated as a common carrier pipeline (A21) whose purpose was to serve primarily the interests of crude oil producers by providing the major outlet for western Canadian oil resources. It has continued to serve in this function for some 70 years (A9, A12). This is reflected in the central role during the last 25 years played by the Canadian Association of Petroleum Producers ("CAPP") in successive settlements of the Mainline's rates (A13).

The Mainline is a natural monopoly currently controlling some 70% of the pipeline egress capacity from the Western Canadian basin (A11). Enbridge implicitly entered into a "regulatory bargain" with the government of Canada: in exchange for the essential legislatively-conferred right to take land for pipeline use, it has accepted regulation in

matters of rates, service and facilities, as provided by three successive acts of parliament (A9, A10, A21).

For some 15 years the NEB monitored and then for 20 years actively regulated the Mainline's rates and return on equity, specifically recognizing in its awards the greater risk exposure of a common carrier oil pipeline compared to contract carrier gas pipelines (A14).

For the past 25 years the Mainline's rates have resulted from negotiated incentive settlements, primarily with the upstream oil-producing sector. The negotiation of these settlements contributed to the crude oil producers' understanding of the pipeline and did so more effectively than the traditional adversarial regulatory processes which they replaced (A15,16,17,19).

However, these incentive settlements generally had as their starting point tolls based on cost-of-service principles established by the NEB in regulatory proceedings.

The settlement currently in effect through 2021 appears however in recent years to have resulted in an imbalance of economic interests between the producing sector, challenged by extraordinarily low commodity prices, and the pipeline service provider receiving an essentially guaranteed income stream, resulting in the pipeline capturing an increasing share of the revenue available at market locations (A20).

Common carriage on the Mainline has worked well: its status as a common carrier has never been the subject of a formal complaint to the regulator or to the policy side of government, for example to seek a change in the relevant legislation (A22). The Mainline has frequently experienced periods when shippers request transportation of more oil than the pipeline could carry, resulting in a situation under which each of the shippers that requested a volume is "apportioned" a share of the available capacity (A24).

Notwithstanding statements by witnesses Church and Reed that this apportionment is economically inefficient, there have never been complaints to the NEB or the Commission regarding negative effects of Mainline open access on the upstream industry (A33, final paragraph).

Regulatory issues have never significantly impaired capacity expansions to deal with situations of apportionment (A23). Rather, in the 20th century uncertainties about crude oil supply were the most important consideration affecting expansions (A25). In the 21st century, environmental, landowner and indigenous issues have tended to prolong regulatory processes (A23). There has been no direct link between common carriage, apportionment and the ability of Enbridge to provide additional Mainline capacity (A26).

The "upstream industry" royalty owners and crude oil producers and their service providers rank as the group of greatest relevance to this evidence (A27). and the preponderant weight which should be given to their interests in assessing the Application (A28) was reflected in the tolling decisions taken during the era of active rate regulation (A29). As to other actors, while U.S. refiner-buyers are valued customers of Canadian crude oil producers, their economic interests rank below those of Canadian oil producers in relation to the Enbridge application. Canadian integrateds' economic interests tend to balance as between

income generation from crude oil production and from oil refining. Again, the crude oil market the integrateds provide is valuable, but their economic interests should be ranked below those of crude oil producers in terms of the Canadian public interest in this Application (A30).

The support that Enbridge has marshalled for the Application does not represent the Canadian public interest: it is biased in favour of U.S. refiners and against Canadian crude oil producing interests, which had previously been the only (1995, 2000, 2005, 2010) or the dominant counterparty (2011) in settlement negotiations (A31).

The Commission's duty is to see to it that Enbridge's Mainline tolls are just and reasonable (CERA s.230) and not unjustly discriminatory (s.235). The NEB nearly 50 years ago recognized that its responsibilities included on the one hand a duty to prevent undue exploitation of monopolistic opportunity and on the other hand a responsibility to conduct its regulatory function so that the enterprise can recover a fair return on capital employed in providing service. Subordinate interests shared between the pipeline and shippers include incenting efficiencies, managing operational problems such as apportionment, minimizing the cost of regulatory proceedings, and allowing the pipeline freedom to run its business subject of course to parties' right of recourse to the Commission where disputes cannot be resolved by negotiation (A32).

There is absolutely no justification for Enbridge to convert the Mainline from 100% common carriage operation to 90% contract carriage. The "desire of some shippers" is hardly a compelling reason to overturn 70 years of common carriage regulatory certainty (A33).

Enbridge's desire, expressed to its Canadian regulator, is to retain Mainline volumes and reduce its long-term volume risk. This position, supported by witness Reed's references to NEB gas pipeline cases, is at variance with its public advice to the Securities and Exchange Commission and to its investors that the Mainline is cost competitive relative to other alternatives and that this provides a significant measure of protection against volume fluctuations (A33).

The best that Enbridge's witness Earnest can offer Canadian crude oil producers is "the potential" which may exist "for a period of time" of a significant increase in western Canadian crude oil prices, an enigmatic finding which leaves the producer to speculate about the potential for a temporal significant decrease in such prices (A33).

Witness Church helpfully reminds the Commission that an unregulated natural monopoly typically results in inefficiency and/or higher prices and lower output from the exercise of market power. This nicely captures the likely outcome of Enbridge's contract carriage project, whose unregulated participants would enjoy market pricing power over uncontracted shippers left with recourse to a woefully insufficient 10% common carriage reservation (A33).

Contract carriage (85%) was first approved by the NEB 25 years ago for the Express Pipeline in the OH-1-95 proceeding, for an entirely new, modest-sized, probably economically-marginal, new oil pipeline that was assigned Group 2 status in the NEB's

ranking of important pipelines under its jurisdiction. The project enjoyed producer and provincial support, faced transportation alternatives, and for which shipper commitments provided critical financing support. Express was opposed only by Enbridge's predecessor, presumably concerned with retaining its then-monopoly of eastwards transmission of western Canadian crude oil (A34).

Contrasts of Express with the Application are stark: the Mainline is a legacy pipeline, a continental giant, never economically marginal, not needing financing, risks well understood and recognized historically in the regulated revenue requirement, dominant eastwards shipper of western Canadian crude oil, and placed in Group 1 for financial regulation (A36).

The NEB noted seven years ago that oil pipelines are increasingly relying on long-term contracts to support new facility construction. Eleven litigated NEB cases are compared with the Application relative to four criteria for contract carriage: (1) Linkage to new facilities? (2) Related to new markets? (3) Underpinning for new facilities? (4) Unopposed by oil producers? None of these criteria apply to the Application. With two minor exceptions, all of them apply to the eleven cases (A34 and Annex 2). Therefore, there is no relevant precedent under NEB or CER regulation for approving a switch to contract carriage in the absence of a proposal for new facilities or services, along with support from the producing community.

The Application and expert evidence asserts a private interest case for a switch to contract carriage, namely, to mitigate the Mainline's competitive risk and enable it to engage in "fair" pipe on pipe competition, but at the expense of crude oil producers' choice and optionality in seeking refinery markets. The Application elevates the interests of a monopoly pipeline above those of crude oil producers whose interests are most aligned with the overall Canadian public good (A37).

The pending expiry of the 2011 toll settlement provides an opportunity for a comprehensive public review and re-basing of the Mainline's revenue requirements. This should be done on a cost of service basis which respects the long-established standard of a fair return on and of capital invested in the enterprise (A38).

III. EARLY HISTORY OF THE ENBRIDGE MAINLINE

Q8. WHAT SECTOR OF THE CANADIAN OIL INDUSTRY HAS BEEN THE PRINCIPAL FOCUS OF GOVERNMENT POLICY?

A8. Unquestionably, the upstream crude oil producing sector.

As between the principal industry sectors—upstream exploration and production and related service providers, pipeline transmission, refining and marketing—the upstream sector has been the continuing focus and policy concern of the Government of Canada and of the governments of the producing provinces. This is primarily because of its exceptional revenue contribution from sales of mineral rights and from taxes and royalties, its enormous net export contribution to Canada's balance of visible trade and because of its role in helping to ensure national energy security. In this regard, I draw attention to Section

III of the evidence of the Canadian Shippers' Group. By contrast, refining and marketing, commonly referred to as the downstream sector, are made up of competitive margin businesses, one of many which function in an environment of generic government fiscal and other policies. The Canadian refining sector of course provides a valued domestic market for WCSB and Atlantic Basin crude oil and the refinery market west of Ontario is essentially captive to WCSB supply.

Q9. PLEASE DESCRIBE THE EARLY HISTORY OF THE MAINLINE, INCLUDING THE CIRCUMSTANCES UNDER WHICH IT WAS BUILT AND INITIALLY REGULATED FOR TOLLS AND TARIFFS.

A9. The modern era of Canadian petroleum development began with the discovery of light crude oil by Imperial Oil at Leduc, Alberta on February 13, 1947, which was succeeded by a second and larger Leduc discovery (May 1947) and by subsequent finds at Redwater (1948), Golden Spike (1948), Bonnie Glen (1951), Wizard Lake (1951) and elsewhere.[1] [2] [3]

The early history of the Mainline

The Mainline was an initiative of Imperial Oil following these spectacular discoveries.

Like all other pipelines of that era, the Mainline, properly the Interprovincial Pipe Line Company ("IPL"), was created by Special Act of the Parliament of Canada by a private member's bill, namely Bill 238 in the 20th Parliament. This bill received third reading and was passed by the House of Commons on April 30, 1949 immediately before Parliament was prorogued and the general election called.

Significantly, Bill 238's sponsor Mr. W.A. Robinson M.P. (Simcoe) stated on second reading:

> *I feel that every hon. Member believes that this is an important national development which deserves the favourable consideration of the house.*

[1] *The Imperial discoveries were dramatic and by the end of 1947 the Leduc area boasted 28 producing wells, with 17 more at the drilling stage…The real boom that a generation of Albertans had dreamed of was under way. Leduc aroused the interest of international capital in Alberta's potential, and long-awaited development funds poured into the province.* Source: David H. Breen: Alberta's Petroleum Industry and the Conservation Board. Edmonton: University of Alberta Press, 1993, pages 245-6.

[2] *Imperial Leduc No.1…was the most important economic event in Alberta's oil history when it came on production that wintry February afternoon in 1947.* Source: Aubrey Kerr: Leduc: S.A.Kerr: Calgary AB, 1991. Mr. Kerr was for a time the chief geologist of the National Energy Board.

[3] These and other fields were members of the Woodbend geological group. Source: https://ags.aer.ca/publications/3739.htm

And Mr. R.R. Harkness (Calgary East) opined that:

> *…oil lines in particular which are absolutely essential to the development of our industry in Alberta…the development in that province which is so essential to us and to the dominion.*[4]

Strikingly, the very last words in the debate on third reading, by Mr. R.R. Knight M.P. (Saskatoon), in fact the very last words in debate in Canada's 20th Parliament (1945-49), were as follows:

> *Before I resume my seat, I want to express the view that, in my opinion, this line should be a common carrier, and that it should have to accept, just as our transportation companies have to accept, any freight which is offered to it for transportation at a proper price.*[5]

IPL's construction was enabled by the authority of the *Pipe Lines Act 1949* ("PLA"), which gave interprovincial pipe line companies the essential authority to take land, which, in the United States, is known as the power of eminent domain. The PLA also provided authority for the regulation of traffic, tolls and tariffs and to declare a company to be a common carrier. This authority was never used. Instead, the Mainline declared itself to be a common carrier and acted as such without regulatory compulsion.

The circumstances under which the Mainline was built

Mr. Lionel Chevrier, Minister of Transport, during the debate on second reading of the PLA, stated as follows in the House of Commons on April 8, 1949 [6]:

> *The first of these* (private companies seeking to get special enactments for the purpose of proceeding almost immediately with the construction of these lines--Priddle[7]) *the Interprovincial Pipe Lines* (sic), *is a company sponsored by Imperial Oil Limited. It seeks authority to build pipe lines within or outside Canada. The company proposes to build a pipe line from Edmonton to Regina as the first stage of its construction. During 1949, if the legislation which they seek is approved…As the company's plans develop, other lines will be built including a line to a point on the international boundary for the purpose of exporting oil to the United States.*

[4] House of Commons Debates, 20th Parliament, 5th Session, Vol. 4, both Robinson and Harkness at page 2776.

[5] op.cit., page 2808.

[6] House of Commons Debates, 20th Parliament, 5th Session: Vol. 3, page 2510.

[7] Special acts to incorporate four other pipelines were passed by parliament on April 30, 1949: British American Pipe Line Company, Trans-Northern Pipe Line Company, Westcoast Transmission Company Limited and Western Pipe Lines. 20th Parliament, 5th Session, Vol. 4, page 2809.

The construction of IPL was therefore contingent on the passage of the PLA.

This construction to Regina was subsequently authorized under the PLA by the Board of Transport Commissioners for Canada ("BTC"), by a judgment dated June 10, 1949 (File No. 45371.2).

The BTC approved further construction of the Mainline by IPL: from Regina to the international boundary at Gretna, MB, on September 15, 1949 (File No. 45371.2.1), from the international boundary in the St Clair River to Sarnia, ON, on March 17, 1953 (File No. 45371.2.42) and from Sarnia to Port Credit, ON, on June 8, 1956 (File No. 45371.2.46). These approvals essentially completed the geography of the Mainline in Canada as it exists today.

The circumstances under which the Mainline was initially regulated for traffic, tolls and tariffs

The PLA, 1949 and 1953, provided that the BTC could make orders and regulations with respect to all matters relating to traffic, tolls or tariffs (s. 40). Tolls had to be filed with the BTC (s. 42), were to be just and reasonable (s. 43), could be disallowed by the BTC and a tariff satisfactory to the BTC substituted, and the BTC could suspend any tariff (s. 44). Pipelines under the BTC's jurisdiction were seemingly not subject to "active" regulation of traffic tolls and tariffs.

As to common carriage, in the debate on second reading of the PLA, Minister Chevrier stated as follows:

> *In the United States, where they have had more experience with pipe lines than we have had in Canada, interstate oil pipe lines are regarded as public transportation agencies and they were placed in the category of common carriers by the Hepburn amendment to the Interstate Commerce Act for the purposes of regulating rates and services.*[8] *This was done to promote competition in the oil industry by requiring major oil companies to permit other shippers the use of their lines. Economic superiority of the pipe line as a means of transporting oil over long distances by land routes affords great competitive advantage to an oil company owning a pipe line, but if independent oil companies can use the pipe line as a common carrier this advantage is much lessened.*[9]

[8] The Hepburn Amendment has been characterized by one authority as "the world's first pipeline regulations", see Makholm, Jeff D, *The Political Economy of Pipelines*. Chicago: University of Chicago Press, 2012, page 19.

[9] The same observation was made by the British oil economist Paul Frankel. In 1946 he wrote: *As pipe-line transportation is economically feasible only if there is a continuous flow on a considerable scale, discrimination is inevitable against those competitors whose turnover or financial resources do not allow them to build a pipeline. This factor was fully realized in the United States by about 1910 when the status of a Common Carrier was imposed on company-run pipelines, making them bound to accept any oil tendered to them.* Frankel, Paul, *Essentials of Petroleum*, London: Chapman & Hall, 1946, cited in Skeet, Ian (editor). *Paul Frankel, Common Carrier of Common Sense*. Oxford: Oxford University Press for the Oxford Institute for Energy Studies, 1989, at page 17.

The PLA, section 41 provided in part that:

> *The Board may, by order, declare a company to be a common carrier whether the company has or has not acted or held itself out as a common carrier.*

Mr. Gordon Churchill, Minister of Trade and Commerce, during the debate on second reading of the NEB Act, stated as follows to the House of Commons on May 22, 1959.

> *The Pipe Lines Act provided for the control of the traffic, tolls and tariffs of oil pipe line companies once such companies had been declared by the Board of Transport Commissioners to be common carriers. However, although the major oil pipe lines have acted as common carriers they were never declared by the Board of Transport Commissioners to be common carriers.* [10]

Q10. WHAT WAS THE RATIONALE FOR THE ECONOMIC REGULATION OF OIL PIPELINES AT THE TIME THE NEB WAS CREATED IN 1959?

A10. The rationale was to regulate pipeline natural monopolies in the public interest. The natural-monopoly rationale of public utility regulation reflects a longstanding and accepted point of view.[11]

Thus, in committee of the House in discussion of a resolution to provide for a national energy board, Mr. Gordon Churchill, Minister of Trade and Commerce, outlined on May 18, 1959, certain points of policy which underlie the proposed measure and which was intended to guide its administration if approved by Parliament. He stated in part as follows:

> *We recognize the need for and welcome capital whether domestic or foreign for investment in the energy and associated industries, and we believe such capital, wisely invested, should enjoy a fair and reasonable rate of return. As to what is a fair return, it is not our intention to incorporate any fixed formula in the statute. Rather, our first premise is that returns on successful investment must be sufficient to attract capital for replacement and expansion, and our second premise is that the public interest requires that no pipe line company should exploit its monopoly or quasi-monopoly position to secure returns higher than are fair and reasonable.*[12]

Minister Churchill went on to explain:

> …. *The oil pipe line may not have the same sort of captive market* (as the gas pipe line). *However, for some refineries one oil pipe line may be the only practical source of supply, and for many oil producers one oil pipe line is the only practical*

[10] House of Commons Debates, 24th Parliament, 2nd Session, Vol. 4, page 3927.

[11] Bonbright, James D. et al. *Principles of Public Utility Rates.* Arlington VA: Public Utilities Reports, 1988, Pages 17-25, NATURAL MONOPOLY AND PUBLIC UTILITY STATUS. Bonbright has been approvingly cited by the National Energy Board.

[12] House of Commons Debates, 24th Parliament, 2nd Session, Vol. 3, page 3767.

> *outlet to market. Therefore, for practical purposes, an oil pipe line is in a monopoly or quasi-monopoly position, and should be regulated as such.*[13]

The resolution was reported and concurred in and Mr. Churchill obtained leave of the House to introduce Bill C-49, to provide for the establishment of a national energy board.

In the debate on second reading of C-49 on May 22, 1959, he stated as follows regarding the economic regulation of pipelines:

> *The part of the bill which has to do with traffic, tolls and tariffs lies at the heart of the legislation and is perhaps the most important single new feature.*[14]

Mr. Churchill later repeated the rationale for economic regulation of oil pipelines as follows:

> *Some oil producers can find an outlet to market through only one pipe line, and some refineries are similarly dependent on one pipe line. Oil pipe lines therefore have some of the characteristics of monopoly and the argument for some regulation in the public interest therefore applies.* [15]

Q11. DO YOU CONSIDER THAT THE MAINLINE CURRENTLY EXHIBITS MONOPOLY OR QUASI MONOPOLY CHARACTERISTICS?

A11. Yes.

It is sufficient to note, as did the CER on page 2, point 1 of its September 27, 2019 letter, that Enbridge controls over 70% of crude oil transportation capacity out of the WCSB, via pipeline or rail. Dr. Makholm's evidence corroborates and enlarges on this view in his A28 and his Figure 1 showing that the Mainline enjoys a dominant market position with respect to the WCSB. Regionally within the Basin, the degree of concentration is greater. Thus, the Mainline provides the only interprovincial pipeline receipt service available to some producing areas and the only pipeline delivery service to the regionally important Regina plant of Consumers' Cooperative Refineries Ltd. ("CCRL"). This position of market power is acknowledged by Enbridge. However, under the current form of common carrier regulation of the Mainline by the CER, Enbridge's ability to exercise market power is

[13] Ibid.

[14] House of Commons Debates, 24th Parliament, 2nd Session: Vol. 4, page 3927.

[15] Ibid.

greatly constrained.[16] The CER must ensure that this regulatory constraint is maintained by continuance of the 100% common carrier status.

Q12. FOR WHOSE BENEFIT WAS THE PIPELINE ORIGINALLY CONSTRUCTED?

A12. The Mainline was originally constructed for the benefit of the royalty owners and producers of Alberta crude oil and its subsequent operation up to today has had that same purpose in respect of the whole WCSB.

The first annual report of IPL, which was for 1949, states at page 4 as follows:

> *On April 30, 1949, by special Act of the Parliament of Canada, Interprovincial Pipe Line Company was incorporated for purposes of constructing, owning and operating a crude oil pipeline system to provide an outlet for the extensive crude oil reserves discovered in the Province of Alberta.*

The BTC, in approving the extension from Regina to the international boundary at Gretna MB, stated:

> *The Board is satisfied that the construction of the pipe line from Regina to Gretna on the route proposed will enable the applicant to get its* (sic) *oil to a market in the most economical and practical manner and with the least delay.*[17]

Clearly, IPL, now the Enbridge Mainline, was constructed for the benefit of the royalty owners and producers of Alberta oil. Without that pipeline connection to interprovincial refinery markets, it would not have been possible to successfully monetize for the benefit of the producers, royalty owners, the provincial and federal treasuries, the oil reserves discovered at Leduc, Redwater and elsewhere.

Up to that point, Canadian oil products markets had been adequately supplied by the output of regional refineries which used crude oil imported by rail (Regina, Winnipeg) and pipeline (Sarnia) and by oil products imports.

The Canadian oil refining industry did not "need" Alberta oil: on the Prairies and in Ontario it was doing fine without Alberta oil and in Québec and the Atlantic Provinces it continued to thrive on imported feedstock. Alberta and, later, Saskatchewan oil needed the markets that IPL was built to connect.

Minister Chevrier (see also A9 above) told the House of Commons:

> *The attention of all Canada is now focussed on the oil discoveries in Alberta which we hope will exceed our most optimistic expectations.…The new oil field discovered in Alberta will require the construction of trunk pipelines to carry the*

[16] Enbridge Response to CCRL and FCL IR No. 2.12, page 27 of 55.

[17] BTC, Hearing of June 8 and 12, 1949, Judgement September 12, 1949.

> *crude oil to refineries and the finished products from the refineries to the markets.*[18]

The Royal Commission on Energy summarized the import-displacement effect as follows:

> *Until the discovery of the Leduc field in 1947 Canada was almost wholly dependent upon imported oil. This dependence was recognized as a serious weakness in our economic fabric. Indeed, the Leduc and subsequent discoveries of crude oil contributed greatly to the reduction of expenditures on oil imports and stimulated the investment of large sums of foreign capital.*[19]

This review of the historical evidence makes it clear that the IPL system, now the Mainline, plus the Lakehead Pipeline Company ("Lakehead") connection from the Gretna MB border crossing to the international boundary near Sarnia ON, and then onwards to the Sarnia and Port Credit oil refineries, was built and operated to serve primarily the interests of Western Canadian oil producers from the outset.

Q13. DO YOU CONSIDER THAT THE MAINLINE CONTINUES TO SERVE THE PURPOSE YOU DESCRIBE IN THE LAST PARAGRAPH OF A12?

A13. Yes.

In making that affirmation, I have regard to the central role played by the producers' association in toll settlements from 1995 through 2011, and to Enbridge's 2011 statement that it was not aware of any concerns or objections with respect to the 10-year Competitive Toll Settlement ("CTS") and that it believed that all parties having an interest in the Enbridge's traffic, tolls and tariffs were afforded a fair opportunity to participate and have their interests recognized and appropriately weighed during the course of CTS negotiations.[20]

IV. HISTORY OF TOLL REGULATION ON THE MAINLINE

Q14. HOW DID REGULATORY APPROACHES TO RATE REGULATION EVOLVE FROM 1959, WHEN THE NEB WAS CREATED, UNTIL THE EARLY 1990s?

A14. Prefatorily, I would observe that the legislated approach to rate regulation has remained the same since 1959 through numerous other changes to the relevant statutes. Essentially it was and is to leave the matter of traffic, tolls and tariffs to the regulator. Thus, Mr. Gordon Churchill in the debate on second reading in May 1959:

> *The bill* (C-49 to provide for the establishment of a national energy board) *does not specify a formula which the board is to apply in examining and, if need be, in*

[18] House of Commons Debates, 20th Parliament, 5th Session: Vol 3, page 2510.

[19] Royal Commission on Energy (Henry Borden, Chairman). Second Report, July 1959, page 129.

[20] Enbridge, May 2, 2011 letter to the NEB Application of Enbridge filing for approval of the CTS for tolls on the Canadian Mainline for the period of July 1, 2011 to June 30, 2021.

> *setting tolls and tariffs...certainly no single formula would apply to the two industries* (gas transmission and oil pipelines were distinguished in this statement of policy as they subsequently were in the legislation and by the regulator) *where the nature of the business and the inherent risks are so different.…What is needed here is flexibility combined with an understanding of the two industries involved and the public interest affected. We hope to provide this through a board of competent men* (sic), *served by a well trained and experienced staff, appreciative of the public interest and of the needs and problems of the industries concerned.*[21]

The first decade was a period of passive regulation: tolls and tariffs were accepted as filed, financial results were surveyed, and informal contacts were maintained with the regulated companies. In 1969, the major gas transmission company, its costs "squeezed" between contracted gas purchase prices in Alberta and contracted sales prices to eastern utilities, filed for a substantial rate increase. After a three-year process, formal gas transmission rate regulation began. Oil transmission rate regulation was initiated, this time at the regulator's insistence, in 1975 with a decision three years later.

The First Phase-Passive Regulation: from its creation in 1959 until 1973, in terms of its responsibilities under Part IV Traffic, Tolls and Tariffs of its Act, the Board simply accepted filed tariffs, having presumably satisfied itself that the filed tolls were just and reasonable, not contrary to any portion of its act and not unjustly discriminatory.

However, change was adumbrated at page 22 of the NEB's 1967 report:

> *While it has not yet been necessary to hold formal proceedings with respect to regulation of rates, tolls and tariffs, as contemplated under Part IV of the Act, there continue to be frequent discussions on rate matters between the Board and companies under its jurisdiction, and discussions with other interested parties.*

The dam so to speak started to break in 1969, thus the Board at page 22 of its AR under the caption Financial Matters stated:

> *Among the major factors contributing to the expanded activities of the Board was the preparatory work involved in the implementation in late 1969 of Part IV of the National Energy Board Act…there will no longer be any distinction with respect to traffic, tolls and tariffs between those companies which commenced the operation of pipe lines under the Board's jurisdiction since 1959, and hence have been subject to Part IV, and those whose operations predated the coming into force of the NEB Act, which were not hitherto subject to Part IV.*

The Second Phase-Active Cost of Service ("COS") Regulation: The distinction foreseen by Mr. Gordon Churchill in 1959 between what he called the two industries of gas

[21] House of Commons Debates, 24th Parliament, 2nd Session: Vol.4, 3927-3928

transmission and oil pipelines, was maintained in the NEB's practice through the life of that Board.

Thus, TransCanada PipeLines Limited ("TCPL"), the major gas transmission company under the Board's regulation, in August 1969 applied for a substantial increase in its rates which was the first case to come before the Board under Part IV of the NEB Act. It was not finally reported upon until May 1973. Active COS regulation of gas transmission was extended to the other major jurisdictional companies such as Westcoast Transmission and public rate hearings were held almost biennially.

The active regulation of oil pipelines started with the Board advising IPL in April 1975 of its intention to hold a toll hearing and a subsequent three-part process ended with publication in May 1978 of its final reasons for decision. The process had been extended in part because IPL had recourse to the courts, up to the level of the Supreme Court, in matters relating to the filing with the Board of information about the finances and operations of its American subsidiary Lakehead.

After a second major IPL toll hearing and decision in 1980, the Board issued an order[22] [23] providing a procedure that would permit tolls to be adjusted without a public hearing, after consideration by the Board of the views of interested parties. The resulting adjustments to tolls were to reflect routine changes in throughput, rate base and COS, provided there was no change in the principles, or the rate of return established in a previous Board decision. IPL had frequent recourse to this method of adjusting tolls which, initially restricted to IPL and Cochin, was later made available to other oil pipelines. Summary information is provided on page 12 of the AR for 1980.

This adjustment procedure, which was not available to gas transmission pipelines, reduced the frequency of formal public-hearing toll proceedings for IPL.

Q15. WHAT ACTIONS DID THE NEB TAKE IN THE EARLY 1990s TO ENCOURAGE A SHIFT AWAY FROM TRADITIONAL COST OF SERVICE RATE REGULATION TO NEGOTIATED SETTLEMENTS OF TRAFFIC TOLLS AND TARIFFS?

A15. The actions in question were authoritatively summarized in the NEB's ARs to the responsible minister of the crown to be laid before Parliament. Much of what follows comes from that source.

An extended consultative process with interested parties, first referenced in AR 1987, page 19 under "Regulatory Process", culminated in the 1988 publication of the report *Improving the Regulatory Process*, which reviewed suggestions including the feasibility of negotiated settlements (AR 1988, page 73). Subsequently, the NEB published its first *Guidelines for Negotiated Settlements*, which, however, did not get much traction in the regulated

[22] T0-4-80, 4 December 1980.

[23] TO-4-85, 6 June 1985 elaborated the approach to toll adjustments for IPL, classifying adjustments under three heads, only one of which would normally require a public hearing.

community largely because the NEB had reserved to itself the right to amend settlements. The *Guidelines* were updated in August 1994 when the Board stated that it would either accept or reject a settlement package in its entirety.

At the same time, the NEB was giving attention to practical alternatives to the traditional COS method for the toll regulation of pipelines, with emphasis placed on increasing operational efficiency through incentive mechanisms. An Incentive Regulation Workshop was held in January 1993 with a summary of the workshop published in March (AR 1993, page 23).

In the wake of these developments, 1995 marked a turning point in the NEB's economic regulation of pipelines, which had been based for 15 years on a review of uniform accounting data and acceptance of filed tolls and tariffs, and then for more than two decades on a COS basis. The NEB established the cost of capital for major pipelines on a generic basis, with provision for automatic annual adjustments to the rate of return on equity for what it characterized as "an indefinite period" (AR 1995, page 25).

At the start of the generic cost of capital proceeding, IPL indicated that it had reached a comprehensive negotiated settlement with the CAPP respecting an incentive toll methodology and associated tolls and tariffs, which was approved by the NEB in March 1995. The agreed-upon methodology was to form the basis for calculating IPL's revenue requirement and parameters were established to calculate the revenue requirements and the resulting tolls for 1995 to 1999 inclusive. Trans Mountain Pipe Line and TransNorthern Pipelines Inc. followed suit with negotiated incentive settlements approved by the NEB in 1996 (AR 1995, pages 1, 26, 27).

In this context I would note, however, that the evidence of the Drazen Consulting Group states that incentive tolling does not mean abandoning COS. Indeed, Drazen states that COS is an essential test of just and reasonable tolls in situations where effective competition is infeasible.

I consider that negotiated settlements such as Enbridge has enjoyed over the past 25 years are a "looser" approach to cost-based toll regulation. I consider that incentive settlements under the NEB were still tied to COS regulation in that COS normally formed the starting point for a settlement.

The changed approach in the first half of the 1990s was summarized on page 1 of the NEB's AR for 1995 in the following terms:

> *Some 27 years ago, TransCanadaPipeLines applied to the Board to be regulated on a cost of service basis. For more than two decades this approach was applied to major Canadian pipelines. Their costs were litigated before the Board, often annually, in expensive proceedings requiring legal counsel and expert witnesses. The Board prepared the way for an alternative approach by publishing guidelines for negotiated settlements in 1988 (updated in 1994), holding a seminar on incentive regulation in 1993 and establishing in 1995 the cost of capital for major pipelines on a generic basis, with provision for automatic annual adjustments to the rate of return on equity. As a result, starting with Interprovincial Pipeline in*

> *February 1995*[24]*, the Board has received for approval a succession of multi-year negotiated settlements, generally embodying provisions for incentives to reduce costs and share the benefits of such reductions between the pipelines and their shippers.*

The NEB in 1996 informed the minister and Parliament that although reliance on traditional adversarial approaches to toll regulation was waning, it was likely that issues such as pipeline access and toll design for specific services would still require referral to the NEB for resolution (AR 1996, page 4).

Q16. GOING INTO THE ERA OF NEGOTIATED SETTLEMENTS OF TRAFFIC, TOLLS AND TARIFFS, DID THE BOARD HAVE ANY CONCERNS ABOUT THE POSSIBILITY THAT PIPELINES WOULD BE BETTER ABLE TO EXERCISE MARKET POWER THAN THEY WERE WHEN OUTCOMES WERE LITIGATED?

A16. I believe the NEB expected that, as turned out to be the case, a united producing sector would be an effective, counterparty to the pipelines, that producers would be aware of the risk that pipelines would be tempted to misuse quasi-monopoly positions and that on the pipelines' part this temptation would be tempered by their desire to reach multi-year settlements and avoid recourse to the NEB. Broadly speaking, these were the behaviours which generated successive settlements for the Mainline from 1995 through to and including the CTS of 2011.

Certainly, there was no intention by the NEB to allow the pipelines *carte blanche* to shape their service offerings without regulatory restraint. And if the countervailing power of the united producing sector in the negotiating process failed to limit the pipelines' exercise of market power, then I am sure the expectation was that the Board would step in with correctives.

In 1999 I stated as follows:

> *I think these settlements are a wonderful Canadian achievement. They have brought to an end a quarter-century of fractious adversarial public hearings relating to rate matters. They are much more sophisticated instruments of regulation than could have been produced by the traditional processes. They have provided sound incentives for pipelines' managements to optimize the use of their hardware at minimum additional investment. There is significant scope for the pipelines to earn over the generic rates of return which the Board's formula generates. At the same time, they retain sensible limitations on the degree to which these still-quasi-monopolies can exercise market power.* [25]

[24] The five-year Incentive Toll Settlement negotiated between CAPP and IPL filed 16 February 1995 was approved by Board order TO-1-95

[25] Priddle, Roland: *Reflections on National Energy Board Regulation 1959-98: From Persuasion to Prescription and to Partnership.* Alberta Law Review, Volume 37, No.2 (July 1999). Online: http://www.albertalawreview.com/index.php/ALR/article/view/531/524

Those remarks I believe appropriately captured the NEB's views and expectations in the second half of the 1990s.

Q17. WHAT WERE THE MAIN REASONS BEHIND THE NEB'S ENCOURAGEMENT OF NEGOTIATED SETTLEMENTS OF TRAFFIC, TOLLS AND TARIFFS?

A17. In my view, which may or may not be shared by practitioners who were active in the period 1988-1995, the main reasons and the sequence of events were as follows:

1. The NEB (board members and staff) considered that it had by the late 1980s identified and put into practice valuable efficiencies in the traditional oral public hearing process (examples: pre-hearing conferences; lists of issues; encouragement for prior settlements on issues[26]; written information requests and responses; and prior notification of evidence that parties intend to cross-examine on).

2. By the early 1990s, after nearly a quarter-century of dealing with often-biennial rate applications by gas transmission companies in lengthy, adversarial public hearings, the NEB and I believed the interested parties were suffering from "regulatory fatigue". The NEB increasingly recognized the costs for applicants and parties resulting from traditional processes and considered that there were no significant further efficiencies to be harvested in the hearing process.

3. The NEB was aware of the role of negotiated settlements in decision-making in rate cases by the Federal Energy Regulatory Commission and by American state regulatory authorities generally.[27] Staff kept in touch with and reported on USA developments in this field.

4. There was increasing dissatisfaction on the part of shippers with COS regulation. First, shippers were of the view that COS regulation provided perverse signals to pipelines to 'pad' their costs, rather than seeking efficiencies (see p. 7 of the *Summary of Discussion, Incentive Regulation Workshop*, March 1993). Second, public hearings were adversarial, pitting pipelines against their customers (shippers, including producer-shippers), instead of the parties working together to better meet shippers' needs. Lastly, shippers were of the view that they were at a large disadvantage in arguing about a pipeline's costs because of information asymmetries (p. 8 of the Summary of Discussion, Incentive Regulation Workshop, March 1993), and the hearing process was unfair because the shippers ended up

[26] The AR 1994 at page 28 states as follows*: A number of Group 1 pipeline companies have, in some recent years, established task forces on tolls, tariffs and operational matters. These task forces provide a forum for the pipeline companies, producers, shippers, consumers, governments and other interested persons to exchange information, discuss issues, negotiate and ultimately settle issues before the formal hearing process initiated before the Board.*

[27] The NEB had occasional meetings at the level of chairs and members with the FERC and its predecessor the Federal Power Commission (see for example AR 1969, page 15). NEB members and occasionally NEB staff would attend the semi-annual meetings of the National Association of Regulated Utility Commissioners of the USA where the Board was given some recognition.

paying for the costs of their participation and for the pipelines' costs, which found their way into tolls under the 'cost-plus' COS approach (p. 7).

5. All of the above cumulated in the publication of the results of the NEB's incentive regulation workshop (see A15.) and in August 1993 of the Board's second *Guidelines for Negotiated Settlements.* The producers' association and individual pipeline companies seized the opportunity to come together at senior levels and, in March 1995, the NEB accepted the first multi-year negotiated settlement respecting an incentive toll methodology and related tolls and tariffs, which was between IPL and the CAPP (see A14.).

Q18. WHAT WAS YOUR ROLE AT THE NEB WHEN THESE SHIFTS TOOK PLACE?

A18. I was Chairman and Board Member from 1986 to 1997

Q19. WHAT FORM HAS RATE REGULATION ON ENBRIDGE'S MAINLINE TAKEN SINCE THE MID-1990s?

A19. I would term this "the settlements era". Rate regulation of Enbridge's Mainline from April 1, 1995 until June 30, 2011 was effected by the NEB pursuant to successive Incentive Toll Settlements ("ITS"), the first three being each for five years and the fourth for one year, negotiated between Enbridge and the CAPP, "the voice of Canada's upstream oil and natural gas industry". Regulation of Enbridge's Mainline tolls by the Canada Energy Regulator ("CER") is currently carried out pursuant to the 2011 CTS which was approved by NEB order TO-03-2011, came into effect July 1, 2011 and continues until June 30, 2021. The CTS is stated to be a product of an open negotiation process between Enbridge, various Enbridge Mainline shippers and the CAPP, collectively the "2011 Negotiating Team". The CAPP appears to have been Enbridge's principal interlocutor in the CTS settlement negotiations and was the sole interlocutor in Mainline Toll Expansion settlements, such as were listed in the CTS application of May 2, 2011 under heading (e) Canadian Mainline Expansion Components, paragraphs 19-24 at pages 8 and 9. The preponderance of the upstream crude oil interest represented by the CAPP is appropriate and understandable, given that regardless of the identity of the Enbridge Mainline shipper and toll payer, the pipeline toll is reflected in the crude oil price available to the producer and royalty owner at Edmonton and Hardisty. In other words, Canadian crude oil producers

are essentially price takers in the market and the netbacks they receive are net of the pipeline toll.[28]

Q20. IN LOOKING BACK AT THE HISTORY OF THE MOVE TO NEGOTIATED SETTLEMENTS ON IPL/ENBRIDGE, WOULD YOU SAY THAT THEY HAVE BEEN A SUCCESS OR HAVE THERE BEEN MIXED RESULTS?

A20. While I believe that negotiated settlements have generally been a success on NEB/CER-regulated pipelines, there have been mixed results with respect to Enbridge.

On the one hand, I consider that negotiated settlements have lifted the burden on pipelines, interested parties and the regulator of what had become for many companies biennial proceedings. I would judge that the lengthy negotiations of successive Mainline toll settlements, the subsequent provision by Enbridge of comprehensive information as well as continuing meetings to review integrity plans, metrics and its overall operating plan have all deepened producers' and shippers' understandings of the Mainline, and have done so more effectively than would traditional regulatory processes. All of this I consider is to the good of the crude oil sector, and I believe that the settlements up to 2011 generally had positive results for both Enbridge and its shippers.

Under the CTS, however, on a COS comparison Enbridge appears to have been earning extraordinarily high returns for a regulated monopoly at a time when producers have been suffering from inadequate pipeline access and depressed commodity prices. And as Drazen points out, COS is an essential test of just and reasonable tolls in situations where effective competition is infeasible.

Drazen's expert evidence states that Enbridge's existing tolls under the CTS regime greatly exceed COS and, as such, are not the appropriate basis for beginning a new incentive tolling regime. Looking ahead to 2022, Drazen states that Enbridge's proposed "benchmark" International Joint Toll will be about US$5.40,[29] whereas the cost-of-service will be about US$4.23/bbl; clearly, on a COS basis, the proposed contract tolls cannot be considered just and reasonable.

This is exactly opposite to the type of outcome that should be pursued from a public interest perspective. The share of aggregate revenue from the sale at market locations of WCSB crude oil have increasingly been captured by the pipeline, rather than the producers and the owners of the resource, the provinces of Alberta and Saskatchewan. The evidence of the Canadian Shipper Group discusses and quantifies the adverse impact of excessive tolls on Canadian producers and other interested parties. The impact is primarily reflected in reduced netback prices for Canadian producers and, in turn, in reduced revenues for governments and the public. As discussed further in section VII of my evidence, I believe

[28] This fundamental of Canadian crude oil pricing was illustrated more than 60 years ago in the Second Report of the Royal Commission on Energy (1959), Table IV *Changes in the posted field prices for Redwater Crude Oil 1948-1959*, at page 2 - 16

[29] Weighted average of contract and spot tolls.

it is time to return to COS regulation for the Mainline, at least to rebase Enbridge's tolls to an appropriate level, after which further settlements could be pursued.

V. HISTORY OF COMMON CARRIAGE AND EXPANSIONS ON THE MAINLINE

Q21. DURING THE ENTIRE TIME OF ITS OPERATIONS SINCE THE ENBRIDGE MAINLINE WAS FIRST BUILT, WHAT FORM OF CARRIAGE HAS IT OPERATED UNDER?

A21. Common carrier status is encoded in the DNA of the IPL/Enbridge Mainline and of its governing legislation for more than 70 years: it is the default setting of the relevant federal regulatory provisions, of its regulators' understanding and of the service offered by the Mainline.

As to government policy, successive acts of the Parliament of Canada—the 1949 PLA, the 1959 *National Energy Board Act* ("NEBA") and the 2019 *Canadian Energy Regulator Act* ("CERA")—contain essentially equivalent provisions that require the Mainline to function as a common carrier for the transmission of oil.

The only change of significance since 1949 is that the imperative of the common carriage provision has been strengthened—now, the company "must" in the CERA s. 239 (1) rather than "shall" in the NEBA, *receive, transport and deliver all oil offered for transmission by means of its pipeline*.

As to corporate policy: before the proverbial shovel went into the ground, the Mainline was conceived by its sponsor, Imperial Oil[30], as a common carrier and the Parliament of Canada

[30] Imperial Oil as the dominant producer of Alberta oil and the owner of the refineries in Regina and Sarnia that IPL was to reach, was in a strong position to contract the capacity of the mainline. That it did not do so can hardly be disconnected from the 1911 pipeline-related breakup of the Standard Oil Trust, Imperial being 69% owned by the Standard Oil Company of New Jersey (now Exxon-Mobil).

embodied common carriage in the PLA, the enactment of which was a precondition for the Mainline's construction starting in 1949 (see A9. above).[31]

Therefore, from the day it first invited nominations of crude oil for transmission, the Mainline held itself to be, and acted as, a common carrier.

In 2019, the common carriage provisions were proposed by the government of the day and embodied in the CERA seemingly without debate in the House, the Senate or in Committee, signifying unanimous policy and legislative assent.

In its 70-year history, the common carrier status of the Enbridge Mainline has never been questioned, much less challenged, by the pipeline company, the crude oil producing sector or the refining interests to whom this feedstock is delivered.

Common carriage has provided the producing sector with flexibility and optionality in getting its crude oil and equivalent hydrocarbons to market, a quality that would be largely lost under the contract carriage proposal of the Application.

Q22. HAS THE SYSTEM OF COMMON CARRIAGE ON THE MAINLINE WORKED WELL?

A22. Yes.

As already noted in A21., common carriage has for 70 years been the default setting for the Mainline and one would therefore not expect any routine reporting by the Mainline's operator or its regulator as to the functioning of the Mainline's common carrier status.

I have been unable to find any submission to the Mainline's successive regulatory authorities or reports by those authorities which would cast doubt on the satisfactory functioning of common carriage. Specifically, I note that the Application to the CER does not make any such claim.

In its March 2019 Advice to the Minister of Natural Resources *Optimizing Oil Pipeline and Rail Capacity out of Western Canada,*[32] the NEB responded to the following question:

> *Is the current monthly nomination process to access available capacity on oil pipelines functioning appropriately, consistent with the "common carrier" provisions of the National Energy Board Act and efficient utilization of pipeline infrastructure (for example, by auctioning uncontracted export capacity to smaller producers)?*

[31] As noted in the last paragraph of A8. above, the common carriers (sic) provisions of the PLA were not invoked by the BTC which had Parliament's authority to declare a pipe line company to be a common carrier. This latent possibility was not invoked by the BTC presumably because it found IPL's voluntary provision of common carriage to be satisfactory in the public interest.

[32] Online: https://www.cer-rec.gc.ca/en/data-analysis/energy-commodities/crude-oil-petroleum-products/report/2019-optimizing-capacity/2019ptmzngcpct-eng.pdf

The response in part was:

> *The Board advises that pipelines transporting crude oil out of western Canada are currently operating at their full capacity, after recent optimization efforts from pipelines and their shippers. Any notable increase in pipeline throughput would need to come from new capacity additions, rather than further optimization of existing pipeline systems. Unexpected delays in almost all proposed major pipeline projects in the last decade have resulted in oil production surpassing pipeline capacity, creating an extended period of high levels of pipeline apportionment. In the current circumstances, the existing monthly nomination procedures on the four major crude oil export pipelines do not appear to affect the pipelines' operational efficiency.*

Q23. HAVE THERE BEEN ANY REGULATORY PROBLEMS AFFECTING THE OPERATION OF ENBRIDGE'S SYSTEM UNDER COMMON CARRIAGE? FOR EXAMPLE, HAVE SUCH PROBLEMS EVER SIGNIFICANTLY IMPAIRED SYSTEM EXPANSIONS?

A23. No.

The Mainline's common carrier status and practice has never been a factor in applications to the regulator for system expansions, which are described illustratively in the following paragraphs.

The long history of operation of the Mainline was marked, at least until the coming into effect of the CERA in August 2019, by what might be described as a succession of cycles in which monthly nominations reach or exceed system capacity, the Mainline's management consults with oil producers and shippers, proposes capacity expansions, applies to the NEB for related approvals, the NEB considers-generally in a public hearing process-whether a pipeline expansion exceeding 40 kilometres is required by the present and future public convenience and necessity, and makes its report. In the case of pipelines 40 kilometres or less in length, the NEB may have provided approval more expeditiously by Order. For decades, the NEB ARs record hundreds of Orders granted to IPL for new oil pipeline facilities of various kinds (line pipe, pumps, valves, tankage, control systems).

20th Century: This cyclical process can be illustrated by the NEB's treatment of the Mainline expansion required to accommodate the increase in Alberta crude oil production which occurred after the 1985 Western Accord[33] had released the upstream industry from government controls. Thus:

- **1986:** *(*T*)he (*IPL*) pipeline operated at capacity with apportionment of available capacity among oil shippers being required in many months. Construction is proceeding on a phased program to additional capacity. Phase II of the program*

[33] Properly: *The Western Accord, an agreement between the governments of Canada, Alberta, Saskatchewan and British Columbia on oil and gas pricing and taxation*. June 1985

progressed in 1986 and Phase III commenced, following Board approval. Additional capacity will be made available in stages during 1987 (AR 1986, page 14).

- **1987**: *The most important factor to affect oil pipeline capacity in 1987 was the completion of an expansion program by IPL, which…completed its Phase II and Phase III expansions…. approved by the Board following public hearings in 1985 and 1986, respectively. Since the expansion and the reactivation of an existing line, there has been enough capacity to move essentially all available volumes to market* (AR 1987, page 9).

- **1988:** *In spite of the completion of several construction projects…IPL operated at capacity… (and) was frequently required to apportion pipeline space among shippers as tenders exceeded pumping capacity…pipeline companies are assessing the need to increase capacity. Their decisions as to the need for additional facilities will, of course, depend on their projections of crude oil prices and supply. Such expansions would be subject to Board approval* (AR 1988, page 11).

- **1989:** *IPL operated at or near capacity. Apportionment was necessary in the early part of 1989. However, compared with the previous year, the overall incidence of apportionment was reduced, reflecting the decline in oil production* (AR 1989, page 12).

- **1990:** *IPL… operated at or near capacity on the Edmonton to Sarnia part of its system. Apportionment was necessary in the latter part of 1990 due to maintenance programs. However, because oil productive capacity was lower than in previous years, the overall effect of apportionment was not severe* (AR 1990, page 13).

21st century: In an atmosphere of heightened environmental, landowner and indigenous interest in the effects of pipeline construction and operation, regulatory processes affecting the Mainline have been prolonged compared to the first 50 years of its history. Nevertheless, in its time the NEB dealt expeditiously with Mainline applications. Take for example, the Line 3 Replacement Program, described as the largest project in Enbridge's history:[34]

- Application to the NEB November 2014;

- Dealt with by the NEB under hearing order OH-002-2015;

- Decision and recommendation and Detailed Assessment provided to the Minister of Natural Resources, April 2016;

- Decision of the principal American regulator, the Minnesota Public Utilities Commission ("PUC") June 2018, challenged January 2019, reaffirmed March 2019,

[34] Online: https://www.enbridge.com/Line3ReplacementProgram.aspx

Minnesota Supreme Court declines to hear challenges to the PUC's approval, September 2019.

To conclude on this point, in 55 years' observation of regulation of the Mainline under common carriage, I cannot recall any circumstance in which a major required expansion has been unnecessarily delayed by the regulator, and none have been denied. Similarly, there has never been any indication that necessary Mainline expansions or replacements have been delayed because Enbridge or its predecessor was unable to manage the related financing.

Q24. HAVE THERE BEEN PERIODS OF APPORTIONMENT FROM TIME TO TIME ON THE MAINLINE?

A24. In numerous ARs in the 2000s, the NEB defined apportionment as follows:

> *A lack of adequate oil pipeline capacity occurs when shippers request transportation of more oil or oil products than the pipeline can carry. This normally results in a situation referred to as apportionment, under which each of the shippers that requested a volume is "apportioned" a share of the available capacity.*

To answer the question, yes, there have been periods of apportionment over many decades. A sampling of the NEB's reporting over a period of 40 years is provided in Annex 1.

Q25. IN YOUR VIEW, WHAT HAVE BEEN THE MAIN ISSUES THAT HAVE LED TO INADEQUATE PIPELINE CAPACITY OUT OF THE WCSB?

A25. In the first decade-plus following the liberalization of the Canadian crude oil industry by the Western Accord (see also A23.), the Mainline appears to have operated at or near capacity and under apportionment most of that time, which was indicative that pipeline capacity was inadequate out of the WCSB as a whole.

From an observer's standpoint, the main issue affecting the provision of additional Mainline capacity during this time, which came in necessarily-lumpy increments, was economic uncertainty. The NEB in OH-2-97 (albeit not having to do with pipeline capacity out of the WCSB) at page 36 stated:

> *The economic feasibility of a pipeline project is a broad concept that is often dependent on a multitude of factors. In the Line 9 proceeding, evidence was introduced on markets, supply, oil prices and differentials, the impact of the project on markets and producer netbacks, tolling and the valuation of Line 9.*

The uncertainties facing the pipeline investor in that decade-plus included the speed of response of the crude oil market to deregulation after 15 years of state interventions; the pricing environment which at times led producers to cut back; and concerns about supply adequacy. Supply concerns had a long history and may have predominated. In the 1970s,

the NEB had projected declining production of light crude oils.[35] This largely reflected the effects of federal government policies which from September 1973 until deregulation in 1985 held Canadian oil prices below international market levels, cut back exports and therefore production and increased the industry's tax burden. These policies had culminated in the National Energy Program of October 1980 and resulted in the abandonment of important oil sands projects (the Shell and Gulf Oil sponsored *Alsands*, developed in the late 70s and cancelled May 1982, the *Other Six Leases Oilsands*, conceived in 1981, cancelled 1992[36]) and, until a special pricing regime was initiated, threatened the operations of Syncrude and Suncor. Welcome federal and provincial governmental initiatives to foster oil sands development announced in the mid-1990s did not in that decade produce results in terms of offsetting declines in light conventional crude oil. This was reflected in some evidence put before the NEB in facilities applications. For example, in the OH-1-93 Reasons at page 4, the NEB noted IPL's forecast that WCSB output would peak at about 1,960,000 barrels daily in 1995 and decline to 1,699,000 by 2005 (for perspective, CAPP projects 2020 WCSB production at 4,640,000 barrels daily).[37]

In this uncertain environment, IPL tended to come forward with relatively modest phased expansions in the order of 20-30,000 cubic metres (125-200,000 barrels) per day, starting with OH-2-85 (reported July 1985) and going on to OH-3-85 (April 1986), OH-1-93 (December 1993), and then the three-step System Expansion Program ("SEP" already referred-to) approved by XO-J1-1-96, OH-1-96 (June 1996) and OH-1-98 (June 1998). Only by about 1999 was the problem of inadequate takeaway capacity out of the WCSB solved.

Some subsequent projects have suffered political execution (Northern Gateway) and regional rejection and regulatory overkill (Energy East). Others have experienced extraordinary attenuation of pre-construction lead times dealing with environmental and indigenous issues with repeated court challenges (Enbridge Line 3, Keystone XL, Trans Mountain Expansion).

[35] An NEB staff preliminary report of December 1972 *Potential Limitations of Canadian Petroleum Supplies* concluded that production of crude oil from all sources in Canada would be unable to meet the potential export and domestic market after 1973. A succession of NEB reports on *Canadian Oil Supply and Requirements* (OHR-1-75, -76 and -78) projected declining productive capacity of WCSB crude oil and therefore of pipeline needs. That reporting was replaced by the *Canadian Energy Supply and Demand* series starting in June 1981, when the NEB projected that WCSB base supply would start to fall short of meeting Ontario requirements by 1987 and that "…by the year 2000 all of Ontario and even part of the prairies and BC requirements for oil would have to be met by imports."

[36] See Energy Now, August 9, 2017 *Canada's Long History of Cancelled Oil and Gas Megaprojects*. Online: https://energynow.ca/2017/08/canadas-long-history-cancelled-oil-gas-megaprojects-david-yager-yager-management/

[37] Even after deregulation in 1985, official oil supply outlooks were negative. Reporting in *Canadian Energy Supply and Demand 1985-2005*, the Board in October 1986 projected WCSB productive capacity of crude oil and equivalent to fall continuously through 2005 in all its cases (low, high and reference price cases).

Q26. HAVING CONSIDERED THIS LONG HISTORY OF COMMON CARRIAGE AND APPORTIONMENT, WHAT ARE YOUR MAIN CONCLUSIONS CONCERNING THE RELATIONSHIP BETWEEN COMMON CARRIAGE AND THE NEED FOR NEW PIPELINE CAPACITY?

A26. In summarizing the evidence of Mr. Reed and Dr. Church at page 20, third bullet, the Application states:

> *Firm service…will also promote more efficient investment in the Enbridge Mainline, including appropriate price signals regarding if, and when, to expand the Enbridge Mainline.*

There is no direct link between common carriage, apportionment and the ability of Enbridge to provide additional capacity. Enbridge (and its predecessor IPL) have been able to efficiently expand capacity for seven decades while operating under a common carriage model. The need for new pipeline capacity has been satisfactorily signaled by analysis of crude oil supply and markets carried out by Enbridge and its predecessor company and by industry associations such as the CAPP. As indicated in A23., the impediments to new pipeline construction in the last decade have mainly arisen due to environmental, regulatory, and political considerations.

VI. THE CANADIAN PUBLIC INTEREST

Q27. WHO ARE THE MAJOR GROUPS OF PARTICIPANTS IN THE CANADIAN OIL INDUSTRY?

A27. I consider the following to be the major groups of participants in the Canadian oil industry for the purposes of this evidence:

- The provinces as owners of the non-renewable petroleum natural resources being exploited;
- Primarily businesses, whether Canadian or foreign owned, which invest in oil exploration, development and production, sometimes termed “the upstream industry” represented by the producer members of the CAPP and the Explorers and Producers Association of Canada (“EPAC”);
- Secondarily, businesses which provide services of all kinds to the upstream industry and which may be represented as associate members of CAPP or as members of specialist groups such as the Canadian Association of Oilwell Drilling Contractors (“CAODC”) and the Petroleum Services Association of Canada (“PSAC”);
- Thirdly, marketers, aggregators and other service providers who assist in the transport and marketing of oil for small to medium-size exploration and production companies who do not have the scale to handle this function in-house. They may be independent businesses, or they may themselves be members of the upstream industry;

- Crude oil pipelines whether provincially or federally regulated and whether their delivery points are entirely within Canada or reach to the international border; and

- Crude oil refiners whether in Canada or in foreign countries, which can receive Canadian crude oil by any means of transport, recognizing that Canadian refiners initially anchored the demand for WCSB crude oil, generally have less supply optionality than their U.S. counterparts and west of Ontario are captive to WCSB supply (see also A6.)**.**

Notwithstanding its size, employment numbers and sales volumes, I do not consider the downstream industry beyond the tailgate of the refinery or the oil products import terminal itself and the downstream beyond it, to be a major group for purposes of this evidence.

Q28. IN YOUR VIEW, WHAT RANKING SHOULD BE GIVEN TO THE INTERESTS OF CANADIAN OIL PRODUCERS WHEN CONSIDERING THE CANADIAN PUBLIC INTEREST?

A28. I consider that preponderant interest should be given to Canadian oil producers and royalty owners (see also A8. and A12. above). I suggest that this is recognized by successive negotiated settlements of the Mainline's tolls. The "settlements era" was initiated at the most senior levels of CAPP (Chair—Mr. Doug Baldwin, president of Esso Resources Canada) and IPL (Mr. Brian McNeill, president and CEO, previously with an oil producer, Home Oil). In the Mainline settlement negotiations of 1995, 2000, 2005 and 2010 the counterparty was the oil producers' association. The 2011 settlement was negotiated between Enbridge, various Enbridge Mainline shippers and the CAPP. These settlements were all submitted for approval by the NEB which, regulating in the public interest, found the resulting filed tolls to be just and reasonable.

Q29. IN YOUR EXPERIENCE, HAS THE NEB'S PREVIOUS TOLLING DECISIONS CORRESPONDED WITH YOUR ANSWER TO Q28 AND Q26 ABOVE?

A29. Yes.

The NEB's decisions tended to significantly diminish the applied-for revenue requirements and therefore the tolls, which was clearly to the producers' advantage in terms of increased netbacks. Take for example the results of the first proceeding RH-2-76 after the NEB in April 1975 had advised IPL of its intention to determine whether the tolls charged were just and reasonable. When the NEB finally reported in December 1977, the 1976 test year revenue requirement was adjusted by the NEB from an applied-for $185 million to some $122 million (or about 66% of the requested amount). Return on equity was adjusted down from an applied-for 22% to an award of 14% (64% of applied-for), both relating to a 43% equity capital structure. In that the revenue requirement determined in RH-2-76 became the base for subsequent adjustments, the Board's decision built continuing substantial annual producer "savings" into the tolls. Having established that baseline, then in

accordance with the regulatory principle of stability and predictability the Board declined to make significant further adjustments to the equity ratio.

Q30. IN YOUR VIEW, WHAT RANKING SHOULD THE CER GIVE TO THE INTERESTS OF US REFINERS AND OF CANADIAN INTEGRATEDS IN CONSIDERING THE CANADIAN PUBLIC INTEREST?

A30. As to U.S. refiners: when evaluating regulatory alternatives, I consider that there is no Canadian public interest in sustaining or enhancing the commercial interests *per se* of U.S. refiners.

Acknowledging that from the time the Lakehead system came onstream, U.S. refiners have been an important market for WCSB crude oil, oil refining is by its nature is a highly competitive margin-business.

Refiners therefore necessarily aggressively and continuously seek to minimize raw material input costs and maximize output values. They owe nothing to the Canadian crude oil producing industry. In this connection, I note the negligible interest shown by non-integrated U.S. refiners in the discussion of options that might exist to further optimize pipeline capacity out of western Canada, as reflected in the list of companies and organizations that met with NEB staff and provided input to its March 2019 advice to Minister Sohi (see A22.). At the same time, I recognize that U.S. refiners are valued long-term customers for Canadian crude oil producers and, as such, I am sure that producers want to maintain positive relations with them.

I therefore consider that the economic interests of U.S. refiners in establishing the Canadian public interest relative to this Application should rank below those of Canadian oil producers.

As to the Canadian integrated companies,[38] their economic interests tend to balance out, which is of course the objective of integrating crude oil production and refining operations.[39,40] On the one hand, they generate income from their crude oil production, and therefore have an interest in obtaining the best available netbacks. On the other hand, they have income generation from their refining business which is driven largely by "spreads"

[38] The Application document at page 14, paragraph 22, refers to "integrated companies that own both production and refining assets".

[39] "*He* (Rockefeller) *took the first steps toward integration, the process of bringing supply and distribution functions inside the organization, in order both to insulate the overall operation from the volatility of the market and to improve its competitive position."* Yergin, Daniel. *The Prize: the epic quest for oil, money and power*. New York: Simon and Schuster, 1991, page 37.

[40] *The tendency of the producer to look for security of disposal by way of captive refiner-customers, and of the refiner to seek the security of outlets by way of direct access to the large number of ultimate customers, makes for what is called forward integration…since the respective profitabilities of the several phases of the industry are not likely to be uniform, the enterprise which is based on the average thereof is more shock-proof than are those which sink or swim with one only*. Skeet, op. cit., pages 262-263.

between feedstock costs and refined products values, and therefore have an interest in obtaining the lowest available crude oil price.

I therefore consider that the economic interests of Canadian integrateds should be ranked below those of Canadian oil producers in establishing the Canadian public interest relative to this Application. The role of the Canadian refiners has been recognized in A6 and A27.

Conclusion: Were the Commission to consider ranking the diverse interests in this case, primary ranking should be given to the Canadian crude oil producers for whom the Mainline was built, expanded and operated for 70+ years (see also A8., A12., and A26.).

Q31. IN ITS RESPONSE TO CER IR 4.5(C), ENBRIDGE STATES THAT:

> **"THE LEVEL OF SUPPORT FOR THE APPLICATION IS BEST JUDGED BY THE VOLUMES REPRESENTED BY THE PARTIES WILLING TO MAKE THE COMMITMENT NECESSARY TO ENTER INTO A LONG-TERM CONTRACT FOR COMMITTED SERVICE. VOLUMES REPRESENTED BY SUPPORTING SHIPPERS, RATHER THAN NUMBER OF INDIVIDUAL SHIPPERS, ARE THE BEST MEASURE OF THE IMPACT THAT THE PROPOSAL CAN HAVE ON THE MARKET, AND THEREFORE ON THE CANADIAN PUBLIC INTEREST."**

GIVEN YOUR KNOWLEDGE OF WHOM THE SUPPORTING SHIPPERS REPRESENT, DO YOU AGREE WITH ENBRIDGE THAT ITS GROUP OF SUPPORTING SHIPPERS REPRESENT THE CANADIAN PUBLIC INTEREST? IF NOT, PLEASE EXPLAIN WHY NOT.

A31. No, I do not agree that the supporting shippers represent the Canadian public interest.

I consider that preponderant public interest is that of Canadian oil producers and royalty owners (A28.). I note that while two of the twelve supporters have significant Canadian crude oil production, together, they account for only a fraction of the total national production.

I consider that there is no Canadian public interest in sustaining or enhancing the commercial interests *per se* of U.S. refiners (A30.). Nine of the twelve supporters are U.S. refiners or affiliates of refiners. Their support was expressed in what appear to be form letters. None of the 30 parties which took part in the early 2019 NEB inquiry on behalf of the Minister of Natural Resources regarding common carrier provisions of the NEBA related to efficient utilization of pipeline infrastructure (see A22.) appear to have advanced long-term contracting as a desirable alternative to common carriage.

The support for the Application marshalled by Enbridge is strikingly deficient in crude oil production interests compared to that for every negotiated Mainline settlement which it has been put before the Board from 1995 onwards. Recall that the only counterparty in the

settlements of 1995, 2000, 2005, and 2010 was the producers' association, the CAPP.[41] The 2011 CTS was the product of a negotiation by Enbridge with certain Mainline shippers and the CAPP. None of the settlements were opposed by a Canadian crude oil producer or a producer association.

Q32. WHAT WEIGHT SHOULD BE GIVEN TO THE PIPELINE COMPANY'S INTERESTS?

A32. The government's policy position on the pipeline company's interests was expressed in the 1959 debate on Bill C-49 (the NEBA). As already cited in A10., the responsible minister stated:

> … *such capital, wisely invested* (in pipe lines), *should enjoy a fair and reasonable rate of return…sufficient to attract capital for replacement and expansion...*[42]

Again, as noted, the government of that day and its successors up until now decided that Parliament should not attempt to predefine a fair and reasonable return, but left that task with the regulator, then the NEB, now the CER.

The NEB first exercised that mandate in the TCPL case already discussed in A14. and summarized its position in its Reasons as follows:

> *The Board recognizes that in the determination of just and reasonable rates its powers and responsibilities include on the one hand a duty to prevent undue exploitation of monopolistic opportunity, and on the other a responsibility so to conduct the regulatory function that the regulated enterprise can recover [i]ts cost of service including a fair return on capital employed in rendering the utility service*[43] [44]

[41] See ENBRIDGE PIPELINES INC. COMPETITIVE TOLL SETTLEMENT APPLICATION May 2, 2011, paragraphs 14 through 18. Online: https://www.enbridge.com/~/media/Enb/Documents/Shippers/Competitive_Toll_Settlement_Application.pdf?la=en.

[42] House of Commons Debates, 24th Parliament, 2nd Session, Vol. 3, page 3767.

[43] NEB, Reasons for Decision, RH-1-72, page 3 - 11

[44] The foundational Canadian statement as to what is a "fair return" was as follows:

In *Northwestern Utilities (1929)* Lamont J. of the Supreme Court of Canada held that:

> *The duty of the Board was to fix fair and reasonable rates; rates which, under the circumstances, would be fair to the consumer on the one hand, and which, on the other hand, would secure to the company a fair return for the capital invested. By a fair return is meant that the company will be allowed as large a return on the capital invested in its enterprise (which will be net to the company) as it would receive if it were investing the same amount in other securities possessing an attractiveness, stability and certainty equal to that of the company's enterprise.* Secondary source for this: Return on Equity: Allowed Returns for Canadian Gas Utilities A Discussion Paper Developed by the Canadian Gas Association May 2007, at page 12

My impression is that successive NEB hearing panels adhered closely to this foundational statement of what might be termed "regulatory policy".

I would however tend to modify that 1972 statement to read "a fair return on and of capital employed". That would more completely characterize the awards which the Board made during the period of active rate regulation.

I consider that this constitutes and continues to be the principal weight that the regulator should give to the pipeline company's ongoing interests respecting already-certificated facilities.

Subordinate interests to which the regulator should give weight tend to be ones shared with shippers, for example: incenting efficiencies by splitting them between the pipeline and shippers; leaving the pipeline to manage operational problems such as apportionment; minimizing the cost of regulatory proceedings; and allowing the pipeline freedom to run its business within the parameters of the Act while recognizing parties' right of recourse to the regulator in the event of disputes which cannot be solved by negotiation.

As to new pipelines and pipeline expansions that require orders and/or certificates, I consider that the CER and the Impact Assessment Agency of Canada should now deal under their respective legislations with certificate applications as expeditiously as all circumstances allow, so as not to unduly restrict pipeline companies' interests in expanding their business in the public interest.

VII. JUSTIFICATION FOR A SHIFT TO CONTRACT CARRIAGE

Q33. IN YOUR VIEW, IS THERE ANY JUSTIFICATION TO CONVERT THE MAINLINE FROM COMMON CARRIAGE TO CONTRACT CARRIAGE AT THIS TIME?

A33. No.

There is absolutely no justification in the operating and regulatory history of the Mainline and in the evidence supporting the Application to overturn 70 years of 100% common carriage and replace it with 90% contract carriage, leaving a 10% token-share for common carriage. Approval of the Application would be a dramatic departure from the tariff stability and predictability long provided by the Mainline to Canadian crude oil producers and royalty owners.[45]

The reasoning for this seismic change given in the 86-page Application document is insufficient. It appears from the Application Overview, page 7, paragraph 3, to consist of

> *…the desire of some shippers for long-term priority access to Canadian Mainline pipeline capacity at reasonable and stable transportation tolls, as well as the*

[45] The NEB's Rfds in successive IPL rate cases are replete with references to the objective of stability in toll-making (examples: RH-3-80, page 7 – 4; RH-3-83, page 27; RH-2-88, page 48; RH-2-91, "simplicity, stability, predictability", page 62. This objective is surely equally important in relation to all tariff matters. In GH-5-89 at

> *desire of Enbridge to retain volumes on the Enbridge Mainline and reduce its long-term volume risk.*

The "desire of some shippers" is hardly a compelling reason to overturn 70 years of common carriage regulatory certainty.

The concomitant desire of Enbridge is to retain Mainline volumes and reduce its long-term volume risk.

Those risks, including whatever may be the risks associated with common carriage versus contract carriage, were long ago drawn to the NEB's attention, the related evidence was not challenged, and the risks were then accounted for in the NEB's equity awards and built into the Mainline's subsequent revenue requirement to this day.[46] Those are the very risks—supply, market and competitive—that Mr. Reed's evidence A36 at his page 27 identifies as "fundamental risks faced by pipelines." In providing for those risks in its equity awards, the NEB was careful to acknowledge that the Mainline of IPL faced greater business risks than gas transmission companies: curiously in view of the NEB's position on oil versus gas pipeline risks, Mr. Reed does not attempt to differentiate gas from oil pipelines in his plentiful references to gas transmission cases (Alliance, Foothills, Nova Gas Transmission, TransCanada, Vector) despite the legislated distinction between a pipeline for the transmission of oil (CERA s. 239(1)) and a pipeline for the transmission of gas (CERA s. 239(2)).

Enbridge's public position on these matter as expressed on page 19 its 10-K report[47] filed with the Securities and Exchange Commission ("SEC") for the fiscal year ending December 31, 2019 is as follows:

> *Notwithstanding the current price environment and Alberta policies, our Mainline System has thus far continued to be highly utilized. Mainline throughput as*

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page 11, the NEB heard that *consistency in regulatory decision-making can add value to Canadian gas exports and…the history of regulatory stability was one of its reasons for seeking a Canadian gas supply*.

[46] The NEB's RfD in RH-3-80, *IPL Tariffs and Tolls*, June 1980, pages 5 – 3 to 5 – 5, reflect the Board's careful examination of IPL's business risks, including those that may be associated with common carriage as opposed to contract carriage. Under Section 5.1.3, *Rate of Return on Common Equity*, page 5 – 3, the RfD summarized the evidence of IPL's expert witnesses who …*contended that IPL faced greater business risks than gas transmission companies because of a threat of competition, lack of long-term contracts or demand charge components in its tariffs, greater supply and demand risks and greater political and regulatory risks… The expert witnesses emphasized the fact that IPL sells its services on a monthly basis without demand charge.* This evidence led the Board to agree that IPL's business risks…*are somewhat greater than those experienced by gas transmission companies* and it made its determination of a fair and reasonable rate of return on common equity on that basis at page 5 - 5. In subsequent rate hearings, the Board found that the level of business risk was not significantly different that in each previous hearing: see for example RfD I RH-3-83 at page 20, RH-4-86 at page 22, RH-2-91 at page 23.

[47] The annual report on Form 10-K provides a comprehensive overview of the company's business and financial condition and includes audited financial statements. Although similarly named, the annual report on Form 10-K is distinct from the "annual report to shareholders," which a company must send to its shareholders when it holds an annual meeting to elect directors. Online: https://www.sec.gov/fast-answers/answers-form10khtm.html

> *measured at the Canada/United States border at Gretna, Manitoba saw record deliveries of 2.845 million bpd in December 2019, slightly higher than our previous record in July 2019. The Mainline System continues to be subject to apportionment, as nominated volumes currently exceed capacity on portions of the system. The impact of a low crude oil price environment on the financial performance of our Liquids Pipelines business is expected to be relatively modest given the cost effectiveness of our Mainline toll and commercial arrangements which underpin many of the pipelines providing a significant measure of protection against volume fluctuations. Our Mainline System is well positioned to continue to provide safe and efficient transportation which will enable western Canadian and Bakken production to reach attractive markets in the United States and eastern Canada at a competitive cost relative to other alternatives.*[48]

Contrast the above statements, certified at the highest level of the company, with Mr. Reed's pessimistic views:

Supply risk?	Record Mainline deliveries.
Market risk?	Impact of low crude oil prices relatively modest.
Competitive risk?	Mainline system well positioned, efficient and cost-competitive relative to alternatives.

The Mainline "low risk" message in Enbridge's 10-K was effectively repeated in a corporate context in the December 2019 Annual Investor Day presentation at page 15 which highlighted "Enbridge's Value Proposition" as featuring a "Superior Low-Risk Business Model". [49]

Of the 12 shipper support letters (Appendix 4 of the Application), nine are from US refiners or their affiliates, two from Canadian integrateds, and one from a Calgary-based international with minor oil production in Canada. With one exception, these expressions of shipper support have the character of form letters, no doubt having been provided by Enbridge. For my view on the ranking that the Commission should give to the interests of US refiners and Canadian integrateds, see A30. Of the twelve supporting shippers, only four were sufficiently interested in options to further optimize pipeline capacity out of

[48] Enbridge Inc., Annual Report Pursuant to Section 13 or 15(d) of the Securities and Exchange Act of 1934 for the fiscal year ended December 31, 2019. Online: https://enbridge.gcs-web.com/node/17971/html#s9305DA4486FE59EAA82ECD33DC408012.

[49] Online: https://www.enbridge.com/~/media/Enb/Documents/Investor%20Relations/2019/2019_ENB_Day_Combined_Presentation_FINAL.pdf

western Canada to take part in the 2019 NEB meetings on this subject and referred-to in my A22.

The evidence of Mr. Neil Earnest consists of a one-time snapshot of the changing relevant U.S. refining scene (his Section 2), some third-party data, lacking conclusions on Canadian crude oil producers (Section 3), some paragraphs on market implications of priority access (Section 4), and an overview of transportation options which again lacks conclusions.

Mr. Earnest's only substantial conclusion regarding potential price impacts of contract carriage appears to be summarized on his pages 24-25 as follows:

> *4.11. Implementation of Mainline Priority Access has the potential to significantly increase Western Canadian crude oil prices for a period of time, because a discounted contract toll will be the price-setting mechanism whenever the total export pipeline contract capacity exceeds the crude oil volume that must be shipped by pipeline.*

In other words, from the perspective of Canadian crude oil producers and royalty owners, the preponderant commercially interested parties, the only justification provided to convert the Mainline from common carriage to contract carriage is "the potential" which may exist "for a period of time" to "significantly increase Western Canadian crude oil prices." Further, this would only occur if contract tolls are discounted when contracted capacity exceeds the oil volume for pipeline shipment.

I would note that, based on information as to historical apportionment, including that provided by Mr. Earnest's Section 4, the opposite condition has generally prevailed: the crude oil volume to be shipped by the Mainline has more often than not over the last 35 years substantially exceeded export pipeline capacity (see A25).

In this connection I consider that if Mr. Earnest's reasoning in 4.11 is correct, then implementation of Mainline Priority Access has the potential to significantly decrease Western Canadian crude oil prices for potentially lengthy periods of time, because in the unregulated secondary market for Mainline capacity a premium over the contract toll will be the price-setting mechanism whenever the total export pipeline contract capacity is less than the crude oil volume that must be shipped by pipeline.

I consider that the principal cause of apportionment on the Mainline during the term of the CTS has been the industry's difficulty in increasing crude oil egress capacity for the WCSB. The outlook on this score, including the threatened re-cancellation of the presidential permit for Keystone XL, is not promising. The potential Mr. Earnest postulates to "…significantly increase Western Canadian crude oil prices for a period of time…" hardly seems to exist in the near-term of a switch to 90% contract carriage.

As to Dr. Jeffrey Church's evidence, I note his paragraph 12. He starts correctly with a statement, surely applicable now and always to the Mainline, that

> *A natural monopoly exists when the costs of providing the service or product are minimized by having a single supplier instead of multiple competing suppliers.*

Again correctly, he goes on to state

> *…an unregulated natural monopoly typically results in inefficiency, either because there are higher industry costs from having multiple suppliers and/or there are higher prices and lower output from insufficient competition and the concomitant exercise of market power.*

The second part of the second statement aptly captures the likely outcome of Enbridge's contract carriage project. It will result in the creation of considerable market power held by unregulated companies. The contract carriage parties who obtain capacity will have considerable ability to exercise market power over uncontracted shippers for whom the 10% common carriage reservation is likely to be totally insufficient. That unconstrained market power will be available to contract carriage participants any time that the Mainline's services have a market value higher than the tolls for uncommitted capacity. It is unacceptable from a public interest standpoint that such a condition could exist in respect of an ostensibly regulated natural monopoly.

Dr. Makholm's evidence in his A58. aptly describes the likely effect of contract carriage as follows:

> If given the opportunity to act opportunistically through the acquisition of contracts on the Mainline, US downstream shipper/refiners have a much greater chance of appropriating quasi-rents from WCSB producers, as the evidence showed in 2018.

The Application at page 18, paragraph 33 advises that companies that currently ship approximately 70% of the crude oil volume on the Canadian Mainline have expressed interest in contracting, in aggregate, for an even greater percentage of the contractible crude oil capacity Enbridge will offer in the open season. These companies can hardly share Mr. Earnest's expectation in his 4.11 regarding contract tolls being discounted for a period of time. Instead they surely see profit opportunities in the unregulated secondary market for Mainline space existing for a greater period of time.

Finally, in regard to any justification to convert the mainline from common to contract carriage, I have been unable to find any complaints by crude oil producers or shippers to the NEB or the CER regarding actual or perceived negative effects on the western Canadian upstream industry of the principle and practice of common carriage on the Enbridge Mainline. Therefore, despite the statements by Dr. Church and Mr. Reed that the current

system of apportionment is economically inefficient, there is no practical evidence to that effect.

Q34. CAN YOU REVIEW THE CIRCUMSTANCES UNDER WHICH THE NEB FIRST APPROVED CONTRACT CARRIAGE ON AN OIL PIPELINE?

A34. The NEB first approved contract carriage on an oil pipeline in Express Pipeline Ltd. OH-1-95, Reasons for Decision June 1996. This was an application for a Certificate of Public Convenience and Necessity and for certain toll and tariff orders.[50]

The circumstances included the following:

1. This was an entirely new pipeline (Reasons, pages 1, 6);

2. This was a pipeline of modest initial capacity-172,000 barrels daily (page 1);

3. This may have been an economically marginal project because the notional cost-of-service toll for the first year of operation was considered by Express to be higher than what the market would bear (page 19);

4. The Alberta Department of Energy ("ADOE") and a ten-member oil producer group supported the application, including the provision for committed long term service at reduced tolls (page 26);

5. Longer term shipper commitments provided critical support for the financing of the pipeline (page 19);

6. Shippers who signed term contracts assumed some of the risks of the Project in return for lower tolls and unapportioned access (page 23);

7. Transportation alternatives were available to prospective shippers at Hardisty. One of those transportation alternatives was IPL (Figure 1-2 page 3 and page 23);

8. The share of contracted capacity following the initial open season was 85%.

9. The Board's view was that complaint-basis regulation as a Group 2 company was appropriate from the start (page 25); and

10. Only one party—IPL – opposed aspects of the proposed tolling methodology (page 22).

[50] In its RfD in GHW-5-90 and RH-3-90 of February 1991, the Board considered the issue raised by parties regarding the compatibility of unapportioned access with the operation of a common carrier pipeline. However, the proposed facilities were for the batch-accumulation and injection of a hydrocarbon defined as a gas under the NEB Act. The hearing panel therefore did not apply the common carrier provisions of the NEB Act s.71.(1) which relate, as does s.239 (1) of the CER Act, to the transmission of oil (Reasons, pages 30-31). GHW-5-90 and RH-3-90 were referenced by the Applicant in OH-1-95 (summarized on page 26 of those Reasons) but those references were not mentioned in the Views of the Board in the matter of Common Carrier Obligations (Reasons page 27).

Q35. WHAT WAS YOUR ROLE AT THAT TIME?

A35. I was the presiding member of a four person NEB hearing panel.

Q36. DO YOU SEE ANY PARALLELS OR DIFFERENCES BETWEEN THE CURRENT PROPOSAL BY ENBRIDGE AND (1) THE CIRCUMSTANCES UNDER WHICH THE NEB FIRST APPROVED CONTRACT CARRIAGE ON AN OIL PIPELINE AND (2) THE OTHER TIMES THE NEB APPROVED CONTRACT CARRIAGE?

A36.

(1) Comparing Enbridge's Application and the circumstances under which the NEB first approved contract carriage on an oil pipeline

Referencing the numbering of the text in A34. and as concerns the current Enbridge Mainline:

1. It is a legacy pipeline[51] which has operated for some 70 years;

2. It is a continental giant in terms of capacity and, with Lakehead, length;

3. There is no evidence that it has at any time been economically marginal;

4. There is limited producer support for contract carriage and the position of the ADOE is not yet known;

5. The pipeline does not need financing and there is no credible evidence that contract carriage is needed to secure the Mainline's economic viability;

6. Given its long period of operation, the risks facing the pipeline are well understood and were historically recognized in its approved revenue requirement;

7. It dominates the eastwards shipment of WCSB crude oil to domestic and export refinery markets;

8. The proposed share of contracted capacity is 90%;

9. Because of its great size it is classified as a Group 1 pipeline for financial regulatory purposes; and

[51] By "legacy pipeline" is meant an oil pipeline under the meaning of the CERA, which was built and operated prior to the certification of the Express Pipeline and which has provided and still provides only common carriage service. Geographical location is a natural resource. The legacy pipelines, being first in their field, captured the best geographical locations and became as a result natural monopolies Subsequent oil pipelines serving the WCSB, such as Express, had a less favourable locational resource and required carriage contracts to ensure their economic success.

10. There is widespread opposition to the Enbridge Mainline Application including a large producer base, several integrateds, Canadian refineries, a feeder pipeline and a provincial government**.**

(2) Comparing Enbridge's Application and the circumstances under which the NEB has approved contract carriage for other pipelines

Concerning other times that the NEB approved contract carriage, the matrix which is attached to this evidence as Annex 2 summarize eleven cases, including again Express Pipeline OH-1-95 in A34. and including an earlier oil pipeline case involving gas liquids in GHW-5-90 and RH-3-90. For each case, the salient facts are arranged under four headings:

1. Whether there was a linkage with new facilities;

2. Whether the application was related to new markets or a change in the markets served;

3. Whether contract carriage was required by the applicant to underpin new facilities; and

4. Whether contract carriage was unopposed by oil producers.

The finding in respect of the Application is negative under each of these headings. In respect of the nine cases examined in Annex 2, the finding under each heading is, with two exceptional circumstances, positive.

The 2013 report of the Joint Review Panel for the Enbridge Northern Gateway Project, Volume 2, *Considerations,* concisely summarized its views on contract carriage at hard copy page 347, centre column as follows:

> *Oil pipelines are increasingly relying on long-term contracts to support new facility construction. Under this structure, capacity must be allocated in an appropriate manner among firm shippers and uncommitted shippers to ensure that the pipeline continues to comply with its common carrier obligations.*

I consider that this statement is equally applicable as a summary of the NEB's record regarding applications for contract carriage for a portion of available capacity in the cases discussed above. The limitation in this 2013 report of "long-term contracts" to "new facility construction" therefore eliminates any perceived need to review and discard cases such as OH-1-2007 Keystone, OH-4-2007 Clipper (no contract carriage issue), OH-1-2008 Keystone Expansion, OH-1-2009 Keystone XL, and OH-1-2011 Enbridge Bakken Pipeline Company because they all entailed significant new facility construction. In no case was contract carriage approved in respect of existing pipeline capacity.

Mr. Reed's use, in his A40. at pages 31-32, of the NEB Reasons in RH-2-2011, Trans Mountain Pipeline ("TMPL") *Firm Service to Westridge Marine Terminal* is inappropriate

because the case involved unique circumstances. Thus, the Board at page 25-26 of its Reasons stated:

> *The Board also considered the unique features of the Pipeline including: the distinct allocation and apportionment methodology of Westridge dock and Land capacity; and the unique nature of Westridge dock shipments, including the fact that deliveries to the Westridge dock must be vessel-sized, coordinated with marine transportation schedules and take place on an all or nothing basis.*

The Board's Reasons in RH-2-2011 make multiple use of the term "unique circumstances" and connect that term with the need for a "unique solution". Thus, in its views at page 37:

> *In the Board's view, these unique circumstances, among others, warrant a unique and innovative solution.*

Mr. Reed completely neglects the "unique circumstances" of the Westridge case and he is misleading when he states at his page 31 that:

> *The Westridge decision is informative because many of the facts of the Westridge Application are comparable to the facts in this proceeding.*

None of the "unique circumstances" of the TMPL Westridge Dock case are present in the current Enbridge Mainline and there are no grounds for extrapolating the "unique solution" approved in RH-2-2011 to the Enbridge case.

As an additional consideration, I would note that, contra the Mainline firm service proposal, TMPL applied to have the firm service fee for the Westridge Dock treated as a customer contribution to be reinvested in its existing and future operations. The NEB approved that treatment at page 38 of its Reasons as follows:

> The proposed treatment of the Firm Service Fee will allow Trans Mountain to advance incremental capital projects and conduct preliminary activities in support of a potential expansion of the Pipeline. The Board is persuaded that the advancement of these capital projects and activities have the potential to benefit all shippers by enabling Trans Mountain to develop its system to meet the demand for capacity and transportation.

Again, Mr. Reed's use of RH-2-2011 is inappropriate in that there is no provision in the Mainline Application for the similar use of any element of the revenues from the contract carriage proposal.

In summary, every one of the eleven cases in which the NEB approved contract carriage for a crude oil pipeline contrasts strongly with the circumstances in which Enbridge is applying for contract carriage on the Mainline.

Q37. DO YOU SEE ANY PUBLIC INTEREST REASON IN SUPPORT OF A SWITCH TO CONTRACT CARRIAGE AT THIS TIME?

A37. No, and for the following reasons:

The CER website states the following in regard to the public interest:

> *The Canadian public interest includes all Canadians and refers to a balance of environmental, economic, and social interests that changes as society's values and preferences evolve over time. Before making a decision, the CER works hard to assess the overall public good a project may create and its potential negative aspects, weigh its various impacts, and make a decision or recommendation. Simply put, we need to answer the fundamental question: Would Canada be better or worse off if a particular project were to go ahead?*[52]

In relation to the Application, one considers the public interest as securing a balance of essentially economic interests within the overall economic good. I have already expressed my view in A28. and A30. as to the ranking that should be given to various interests. I consider that the interests of Canadian crude oil producers is preponderant. I also recognize that Canadian refiners on the prairies and at Sarnia are directly connected to the Mainline while Canadian refiners east of Sarnia are served by connecting Enbridge's lines 7, 9, 10 and 11 and by marine from Montreal. The Application claims at paragraphs 39, 58 and 165 that a balance has been struck between various interests and desires, but fails to explain how. Some ten months after filing, the Application remains unamended despite the Commission having cancelled the open season and having expressed concerns about the perception of market power of the Mainline.

The Application itself does not present any public interest case for a switch to contract carriage. The one mention of public interest in the Application document at paragraph 28 on page 17 states:

> *The Board has approved the construction of competitive pipelines on the basis that enhanced pipeline competition and increased customer choice serve the public interest.*

First, the Application has nothing to do with construction of pipelines.

Second, in my judgment, the applied-for service changes would reduce Canadian crude oil producers' choice and optionality in seeking refinery markets, which is the most important element of crude oil sector competition.

In terms of inter-pipeline competition, which I regard as a consideration secondary to the interests of Canadian crude oil producers, no credible market evidence has been provided

[52] Online: https://www.cer-rec.gc.ca/bts/nws/rgltrsnpshts/2016/22rgltrsnpsht-eng.html.

that the Mainline is in any sense vulnerable to competition from other pipelines in the markets that it presently serves.

I have looked for public interest reasons for the applied-for carriage switch in the expert evidence supporting the Application.

Dr. Church asserts as follows:

> *The introduction of firm service to a 100% uncommitted service pipeline has three benefits from leveling the playing field with other firm service pipelines.*[53]

No data are provided to support this statement and, as discussed elsewhere, there has been no evidence filed that demonstrates that Enbridge faces volume risk; i.e. that it requires any 'levelling of the playing field'.

Mr. Reed's summary of his conclusions states that:

> *Canadian mainline contracting is in the public interest…because it allows Enbridge to mitigate the competitive risks the Enbridge Mainline system faces in the foreseeable future, and provides Enbridge with the tools to engage in fair pipe-on-pipe competition in the WCSB.*[54]

Again, no factual data are provided to support this statement. In any event, it would be completely inappropriate to elevate the interests of the monopoly pipeline above the interests of the producers whose interests are most aligned with the Canadian public interest.

As to Mr. Earnest's evidence, he seems not to have been asked to address inter-pipeline competitive considerations. I have commented in my A29 on his muted conclusions as to the potential and temporary crude oil pricing effects of implementation of mainline priority access.

I consider that the Application and the expert evidence supporting it do not provide any public interest reason in support of a switch from common carriage to contract carriage at this time.

[53] Page 30, paragraph 113. The three "benefits" asserted by Dr. Church are: (i) Toll flexibility enhances the benefits of competition.(ii) Enhances incentives for investment.(iii) Deter inefficient entry by pipelines.

[54] Page 4, lines 15-19.

VIII. APPROPRIATENESS OF A TRADITIONAL RATE HEARING

Q38. IN YOUR VIEW, SINCE THE APPLICATION IS NOT PRESENTED AS A NEGOTIATED SETTLEMENT, WHAT IS THE MOST APPROPRIATE METHOD FOR ESTABLISHING THE TOLLS AND TARIFFS FOR THE MAINLINE AFTER THE CTS EXPIRES?

A38. Consideration should be given to a comprehensive re-basing of the revenue requirements of the Enbridge Mainline. As noted in A15., the NEB stated in its AR for 1995 that the methodology in that first negotiated toll settlement was to form the basis for calculating IPL's revenue requirement for an indefinite period. That was 25 years ago, a long time in the life of any business whether a regulated pipeline or a user of that pipeline's services.

The 1995 revenue requirement embodied in the first Incentive Toll Settlement was necessarily based on the results to that date from implementation of successive NEB toll proceedings. Historically the principal variable in establishing the Mainline's revenue requirement was of course the equity ratio and the return on equity. In making its successive awards, the NEB examined expert evidence on risk matters such as inter-pipeline competition, the lack of long-term contracts or demand-charge components in the Mainline's tariffs, oil supply and demand risks, political and regulatory risks. In each of those areas, risks have changed over the decades. After 25 years of settlements founded on a revenue requirement reflecting historical risk assessments the time has come for a thorough review and the expiry of the 2011 CTS provides the opportunity.

The Commission should in my view take that opportunity to consider the Mainline revenue requirement against the long-established standard of a fair return on and of capital invested (A32., and Enbridge response to CER IR No.1, page 2 of 65). The tolls on the Mainline appear to have yielded what must be assessed as a high rate of return for a regulated entity during most of the term of the CTS. They have become divorced from the COS and the fair return principles which should apply to regulated monopolies. In my view, it is time to rebase the tolls according to long-standing principles governing rate regulation of utilities; i.e. it is time to hold a traditional COS hearing under which a reasonable rate base can be identified and against which a fair rate of return can be established. Following a year of rebasing, parties should of course be free to negotiate mutually agreeable settlements if they believe they can produce superior results to COS regulation.

Q39. DO YOU HAVE ANY OTHER CONCLUDING REMARKS CONCERNING THE APPLICATION AND THE CANADIAN PUBLIC INTEREST?

A39. The Application would overturn 70 years of common carrier service. The market for 70% of WCSB crude oil has grown and functioned through the intermediation of that service offering. The Mainline cannot now be allowed to switch from 100% to 10% common carriage just to satisfy the wants of "some shippers" (Application, page 18, paragraph 32), most of whom are not operating in Canada, understood to be refiners and integrateds. What the Application describes as a longstanding and efficient commercial dynamic where producers sell their crude oil to shippers such as refiners and integrateds (Application, page 14, paragraph 22) takes place in the framework of common carriage. Any proposed change in that fundamental requires the most critical regulatory scrutiny to ensure the fair

balancing of competing interests, in which those of Canadian crude oil producers and royalty owners are preponderant.

Q40. DOES THIS CONCLUDE YOUR EVIDENCE?

A40. Yes.

ABBREVIATIONS USED IN THIS EVIDENCE

ADOE	Alberta Department of Energy
AR	Annual Report of the National Energy Board
BTC	Board of Transport Commissioners for Canada
CAODC	Canadian Association of Oilwell Drilling Contractors
CAPP	Canadian Association of Petroleum Producers
CCRL	Consumers Cooperative Refineries Limited
CER	Canadian Energy Regulator
CERA	Canadian Energy Regulator Act
CNRL	Canadian Natural Resources Limited
COS	Cost of Service
CTS	Competitive Toll Settlement
EPAC	Explorers and Producers Association of Canada
IPL	Interprovincial Pipe Line Limited
ITS	Incentive Toll Settlement
Lakehead	Lakehead Pipe Line Limited
NEB	National Energy Board
NEBA	National Energy Board Act
NERA	National Economic Research Associates
NGTL	Nova Gas Transmission Limited
PDD	Priority Destination Designation
PLA	Pipe Lines Act
PSAC	Petroleum Services Association of Canada
PUC	Public Utilities Commission of Minnesota
Reasons	Reasons for Decision of the National Energy Board
RfD	Reasons for Decision of the National Energy Board
SEC	Securities and Exchange Commission
SEP	System Expansion Project
TCPL	TransCanada PipeLines Limited
TMPL	Trans Mountain Pipeline
TNPI	TransNorthern Pipeline Inc.
WCSB	Western Canada Sedimentary Basin

ANNEX 1

A Sampling of NEB reporting of Mainline apportionment from 1979 onward

Apportionment was defined by the NEB as follows (see A24.)

> *A lack of adequate oil pipeline capacity occurs when shippers request transportation of more oil or oil products than the pipeline can carry. This normally results in a situation referred to as apportionment, under which each of the shippers that requested a volume is "apportioned" a share of the available capacity.*

Pre deregulation pursuant to the Western Accord: Apportionment was required briefly in 1979 and again for some months in 1984-85: The issue at that time was IPL's use of a historical (12 months) basis during the period of controlled crude oil prices and movements.[55] Upon a complaint by Northridge Petroleum Marketing, the NEB put the matter down for public hearing in April 1985 by order MH-3-85. In that order, the Board recognized that existing apportionment procedures were developed under market conditions different from those expected to prevail in the deregulated environment. The outcome was that the historical basis was replaced at the NEB's direction by an apportionment system based substantially on current tenders.[56] This is essentially the present design in the Enbridge tariff (see below).

Post Western Accord: a record of apportionment (possibly not entirely complete) can be traced using NEB's ARs:

- 1985: two months (AR, page 13)
- 1986: many months (AR, page 15)
- 1987: prior to the Phase III expansion coming on stream in October—see A22. above (AR, page 9)
- 1988: frequent requirement (AR, page 11)
- 1989: During 1989, IPL operated at or near capacity. Apportionment was necessary in the early part of 1989. However, compared with the previous year, the overall incidence of apportionment was reduced, reflecting the decline in oil production (AR page 12)
- 1990: late 1990 due to maintenance (AR, page 12)

[55] The issue was summarized as follows on page 1 of the MH-3-85 RfD of July 1985: *In 1979, there was a bottleneck on the IPL-Lakehead system, which raised serious doubt as to IPL's ability to make deliveries of all crude oil likely to be tendered to it. At that time, IPL introduced apportionment of capacity…Subsequently, the bottleneck was removed, and no further apportionment of IPL's capacity occurred until recent months.*

[56] Reasons for Decision, MH-3-85, July 1985: *IPL Apportionment of Pipeline Space*, Summary and Conclusions and Disposition, pages 9-12. Online: file:///C:/Users/Roland%20Priddle/Documents/Canadian%20Natural/Enbridge%20IPL%20RfDs%20etc/MH-3-85%20Apportionment.pdf

- 1992: New procedures developed by IPL and the industry to reduce apportionment were implemented on a trial basis in early 1992. While these procedures were partially successful, the volumes nominated for shipment on the system exceeded capacity in all months except for April, resulting in monthly apportionment (AR, page 13)

- 1993: The volumes nominated on the (IPL) system exceeded capacity throughout 1993, resulting in monthly apportionment ranging from a low of 13 percent in March to a high of 42 percent in December. In response to this capacity shortfall, IPL applied to the Board in June 1993 to increase its capacity…The application was subsequently revised to 27 100 cubic metres (170 000 barrels) per day in November 1993 (AR, pages 13-14).

- 1994: The volumes nominated on the (IPL) system exceeded capacity throughout 1994, resulting in monthly apportionment ranging from a low of 18 percent in April to a high of 55 percent in November and December. Pursuant to a certificate issued by the Board in December 1993, IPL expanded its system by 27 100 cubic metres (170 000 barrels) per day. A portion of this new capacity became available in late 1994 with the remainder in January 1995 (AR, page 11).

- 1995: In January 1995, the company (IPL) completed an expansion of its system by increasing capacity by 27100 cubic metres (170 000 barrels) per day. Despite the expansion, IPL's capacity was inadequate to meet the demand of producers to ship oil to the Chicago market. This resulted in apportionment on the system for most of the year (AR, page 17). In MH-1-95, an inquiry into IPL apportionment, reported in April 1995, the NEB stated at page 1:

  > *Apportionment levels on the IPL pipeline system have increased dramatically in recent years and in April 1995 reached 71 percent on IPL's crude oil lines.*

- 1996: (T)he Edmonton-Sarnia portion of the IPL system operated at capacity. For the last nine months of 1996, nominations to ship…consistently exceeded capacity, resulting in monthly apportionment. By year-end, IPL had completed about 85 percent of its 19000 cubic metres (120 thousand barrels) per day of its System Expansion Program. This expansion, along with the construction of the new Express Pipeline which will enter service in 1997, and completion of phase two of IPL's expansion program, should alleviate pipeline constraints (AR, page 12). In OH-1-96 dealing with facilities and tolls, reported in June 1996, the NEB stated at page 21:

  > *The Board acknowledges that current apportionment on IPL indicates that there is a need for additional capacity and that these facilities will help to reduce this apportionment*

- 1997: (T)he IPL system operated at capacity. For the last four months of 1997, nominations to ship on IPL's crude oil lines consistently exceeded capacity, resulting in monthly apportionment (AR, pages 21-22).

- 1998: In its Reasons in OH-1-98, a facilities expansion proceeding reported in June, the NEB stated at page 16:

> *The Board recognizes that the IPL system is currently under apportionment and that it may remain so even after the SEP II1[57] facilities are in service.*

Apportionment was therefore at times required in some 10 of the 13 years 1985 through 1997.

The NEB reported that in 1998 IPL operated at capacity in the first half of the year but had spare capacity in the second half as producers shut in production due to low field prices.

In 1999, the NEB reported that IPL was at capacity. The following data on IPL capacity utilization is taken from six succeeding NEB ARs:

- 2000: 77%; 2001: 76%; 2002: 77%; 2003: 75%; 2004: 80%; 2005: 74%.

- 2006: Enbridge…operated at about 85 per cent of capacity, with the actual throughput averaging 245 000 cubic metres (1.5 million barrels) per day…Capacity was adequate in the first half 2006; however, in the third and fourth quarters of 2006, Enbridge experienced apportionment on many of its lines (AR, page 32).

- 2007: …Enbridge…operated at about 87 per cent of capacity, with the actual throughput averaging 245 000 cubic metres (1.5 million barrels) per day. Capacity was adequate throughout…and no apportionment was required; many of the lines which comprise the Enbridge system were, however, fully subscribed throughout the year (AR, page 37-38).

- 2007 through 2011: the NEB ARs did not identify any capacity or apportionment matters for the Enbridge Mainline.

- In 2012 the NEB observed at page 47 "…a pipeline system essentially operating at capacity…" but its ARs for 2013, 2014, 2015, 2016/17, 2017/18 and 2018/19 seem not to identify issues of Mainline capacity utilization or apportionment, although apportionment was taking place. For example, the NEB's *Market Snapshot What is Pipeline Apportionment*? dated 2018-08-15 includes a bar chart indicating high first quarter 2018 apportionment percentages on Enbridge Lines 2/3 (~10-25%) and 4/67 (~35-55%).

It is reasonable to conclude that, whatever may have been the levels of Enbridge Mainline common carrier apportionment in the 2010s, the issue was handled to the satisfaction of the Enbridge and its shippers using established procedures approved by the NEB[58] and without the need for further recourse to the Board. In turn the NEB, in contrast to the 1985-1997 period, did not consider it necessary to advise Parliament about apportionment through its annual reporting to the Minister.

Inadequate capacity because of apportionment?

[57] "SEP I, II and III" refers to successive steps in IPL's System Expansion Program.

[58] Example: *Enbridge Pipelines Inc., Rules and Regulations Governing the Transportation of Crude Petroleum by Pipeline*, NEB No.443, effective April 1, 2019. Online: https://www.enbridge.com/Projects-and-Infrastructure/For-Shippers/Tariffs/Enbridge-Pipelines-Inc-Canadian-Mainline-Tariffs.aspx

High capacity utilization ratios have been indicative of the need for capacity expansions resulting in appropriate applications to the NEB, (see A23.). At times, the existence of apportionment and its outlook were given and accepted by the NEB as reasons supporting capacity expansion applications (see above with reference to OH-1-96 and OH-1-98). Apportionment may be just one among several indicators of the extent to which capacity additions are required. There is no evidence from public sources or Enbridge Mainline filings that the existence, degree or duration of apportionment has in any way impaired Enbridge management's provision, with regulatory approval, of pipeline capacity to adequately and efficiently meet the takeaway requirements of the crude oil producing sector.

ANNEX 2

Matrix of Contract Carriage Cases in which the NEB has approved contract carriage differentiated from the Enbridge Mainline Application
Reference A34., item (2)

NEB Hearing Order Number and Applicant	Facilities/Traffic Tolls and Tariffs linkage?	Access new markets/change markets served?	Contract carriage underpinning facilities?	Unopposed by crude oil producers?
RH-001-2020 Enbridge Mainline Contracting Application	No	No	No	No
GHW-5-90 & RH-3-90 IPL NGLs accumulation and injection	Yes: *NEB Act ("NEBA") Parts III and IV Orders*	Yes: *incremental volumes of C3+propane plus for shipment to eastern markets via the applied-for facilities.*	Yes: *IPL would not proceed with the project without the FSA*	Not applicable: *Pursuant to NEBA definition, this is a gas project*
OH-1-95 Express Pipeline	Yes: *NEBA Part III certificate and Part IV Orders*	Yes: *Reasons for Decision* ("RfD"): *Chapter 6, pages 33-46 multiple references to new markets*	Yes: *RfD page 19*: *…longer term shipper commitments provide critical support for the financing of the pipeline*	Yes: *10-company producer group ("Friends of Express") plus ADOE support*
OH-3-96 Federated Pipe Lines	Yes: *NEBA Part III certificate and Part IV Order*	Yes: *RfD Chapter 3, page 6: Will make available new markets*	Yes: *RfD 4.1 pages 10-11: PTAs justified by the support those shippers provide for the financing of the pipeline*	Yes: *RfD 3.2 Transportation Agreements, page 7: producer interest warrants construction of a pipeline.*
OH-2-97 IPL Line 9 Reversal	Yes: *NEBA Parts III and IV Orders*	Yes: *RfD page 43:* *…the project has the potential to cause a reconfiguration of North*	Yes: *RfD page 62: (IPL) would not be prepared to proceed with Line 9 reversal without*	Yes: RfD page 44: *CAPP indicated…reversal …would represent a*

NEB Hearing Order Number and Applicant	Facilities/Traffic Tolls and Tariffs linkage?	Access new markets/change markets served?	Contract carriage underpinning facilities?	Unopposed by crude oil producers?
		American crude oil markets.	*the support of the Firm Service Agreements*	*significant change in the market but…western Canadian producers could adjust*
OH-1-2003 Trans Northern ("TNPL") Reversal	Yes: *NEBA Parts III and IV Orders*	Yes: *RfD pages 1 and 4: Change in direction and increase in volume of oil product flows*	Yes: *RfD page 10: … to secure adequate financing and to ensure the long-term viability of the Project (TNPL) required firm ship-or-pay commitments…*	Not applicable: *this is a refined petroleum products pipeline*
OH-1-2007 Keystone	Yes: *NEBA Part III Certificate, Part IV Order*	Yes: *RfD pages 11-13 multiple references to target market*	Yes: *RfD page 12*: *Keystone stated that it had obtained binding transportation contracts that underpinned the Project.*	Yes: *RfD page 54: no opposition…by petroleum producers…or by governments of producing…provinces.*
OH-1-2009 Keystone XL	Yes: *NEBA Part III Certificate, Part IV Order*	Yes: *RfD page 17: The opening of new markets for Canadian crude oil would alleviate economic risk…*	Yes: *RfD page* 28: *Keystone stated that the Keystone XL Pipeline is underpinned by long-term contracts.*	Yes: *RfD page 38*: *(no)…evidence expressing concern that the approval would have an adverse impact on the producing industry…*
OH-3-2011 Vantage Pipeline Canada ULC	Yes: *NEBA Part III Certificate, Part IV Order*	Yes: *New market for U.S.-origin ethane. RfD page 14, indicates Board agrees AB industry experiencing ethane shortage, pipeline*	Yes: *RfD page 16, NOVA signed long-term TSA for ¾ of capacity. Page 18, Vantage estimated approximately 90% of capital cost recovered*	Yes: *RfD page 80, Vantage application for confidentiality of TSA was unopposed (*NEB treated Vantage*

NEB Hearing Order Number and Applicant	Facilities/Traffic Tolls and Tariffs linkage?	Access new markets/change markets served?	Contract carriage underpinning facilities?	Unopposed by crude oil producers?
		supplies would reduce supply/demand gap	*during the first 10 years of the TSA.*	*as an oil pipeline. The product transported is ethane which meets the definition of gas in the NEBA)*
OH-4-2011 Enbridge Northern Gateway Project	Yes: *NEBA Part IV order subsequent to Part III certificate*	Yes: *expanding and diversifying the markets available for western Canadian crude oil exports.*	Yes: *shipper commitments are central to the Enbridge Northern Gateway Project application*	Yes: *the evidence of CAPP and the Government of Alberta was that pipeline capacity is not keeping pace with growing supply and additional pipeline capacity is required.*
RH-001-2012 Trans Mountain Expansion	Yes: *NEBA Part IV order in the event of a future expansion (requiring Part III certificate*)	Yes: *capacity expansion for improving access to the west coast and offshore markets*	Yes: *RfD page* 22: *Trans Mountain sought (by means of the committed toll) to reduce the financial risk in the investment required for the Expanded System*	Yes: *there is no indication of producer opposition in the RfD. CAPP was represented in the proceeding.*
OH-002-2013 Enbridge Line 9B Reversal & Line 9 Capacity Expansion	Yes: *NEBA Parts III and IV Orders*	Yes: *RfD page 103*: *… the reversal… would provide refineries in Quebec with access to the growing…supplies of crude oil from western Canada*	Unclear: *RfD page 117*: *Bd considers… existence of long-term TSAs to be strong evidence of the need for the Project*	Yes: *no indication of producer opposition. TSA signatory Suncor is major crude oil producer*

Terminology: The applications which led the NEB to accept contract carriage provisions in respect of new or reconfigured pipelines used a variety of terms to describe the agreements which required the Board's approval in relation to the provisions of s.71 (1) of the

NEBA. The terms included: Facilities Support Agreements ("FSA"); Priority Access Agreements ("PAA"); Ship-or-Pay Agreements; and Transportation Service Agreements ("TSA"), the term used in the Enbridge application for Canadian Mainline Contracting in RH-001-2020. All of these provisions would, with regulatory approval, confer unapportioned access to a corresponding part of the pipeline's capacity.

ANNEX 3

CV of Mr. Roland Priddle

RH-001-2020 Priddle Witness Qualifications, December 2020

Name: Roland Priddle

Academic Credentials:

MA University of Cambridge (Economic Geography), MA University of Ottawa (Economics), Graduate student, teaching assistant, Department of Earth Sciences, University of California, Berkeley

Relevant Experience:

- 1956 - 64: Royal Dutch/Shell Group of Companies: Management Analyst
- 1965 - 73: National Energy Board: Staff, Division Chief, Director
- 1974 - 85: Canada Department of Energy, Mines and Resources (now Natural Resources Canada): Director-General, Assistant Deputy Minister (Petroleum)
- 1986 - 1997: National Energy Board: Member and Chairman
- 1997 - present: Consulting nationally and internationally on energy economics, policy and regulation

Qualified as an expert witness in the following proceedings:

- Régie de l'Énergie du Québec: Dossier R-3401-98, Hydro-Québec, April 2000
- Superintendent of Hydrocarbons of Bolivia (Tariffs Applicable to Pipeline System Expansions) May 2002
- National Energy Board: GH-1-2004, Mackenzie Gas Project, November 2006
- United States Bankruptcy Court, District of Maryland (Case No. 03-30465-30 PM), 22 April 2008
- Arbitration Panel in a private arbitration pursuant to the *Commercial Arbitration Act* (Canada), November 2010
- National Energy Board: GH-1-2011, KM LNG Application to Export Liquefied Natural Gas ("LNG"), June 2011
- (Provided evidence, accepted and considered by the National Energy Board in support of applications for licences for the export of LNG and propane, 2012-2019)
- National Energy Board: GH-001-2012, NGTL Application for North West Mainline Komie North Extension, May 2012
- Joint Review Panel for the Enbridge Northern Gateway Project, OH-4-2001, 2013
- National Energy Board: GH-001-2014, NGTL Application for North Montney Mainline Project, July 2014
- National Energy Board: MH-031-2017, North Montney Mainline Variance Application and Sunset Clause Extension Request, May 2018