Ontario Energy Board

Commission de l'énergie de l'Ontario

Long-Term Natural Gas Supply and Transportation Contracts

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Overview

- Purpose, Process and Timelines
- North American Background
- Jurisdictional Review
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Purpose, Process, and Timelines

Purpose, Process and Timelines

- Input to the Board on what needs to be considered when determining the appropriateness of pre-approving long-term contracts (LTC)

- Issues for discussion will include:
  - What are the needs, benefits, and risks of entering into LTC?
  - What are the implications of not entering into LTC?

Process and Timelines

- Consultation
  - Stakeholder consultation — Oct. 08
  - Staff discussion paper — Nov. 08
  - Stakeholder comments — Dec. 08

- If the Board concludes that there are circumstances where the pre-approval of LTC may be appropriate, the Board will develop guidelines

- Development of guidelines (If applicable)
  - Issuance of draft guidelines — Jan. 09
  - Stakeholder comments on draft guidelines — Feb. 09
  - Issuance of final guidelines — Mar. 09

North American Background

Background

- Until the mid-1980's, transportation and supply contracts of 20 to 25 years were the norm
- Short-term gas supply contracts is now the norm
  - Contracts > 1 year now considered "long-term"
- Factors that have contributed to shorter gas supply contracts include:
  - Growth of competitive markets with multiple buyers and sellers
  - Retail competition
  - Regulatory uncertainty associated with prudence reviews
  - Reduced transaction costs

Background (cont'd)

- Upstream transportation contracts have also shortened but LT contracts
  - still often form part of a diversified portfolio
  - may be required to secure capacity in open seasons, especially for new capacity
  - may be present when the associated assets are more dedicated to particular customers
  - may arise when capacity constraints exist

Background (cont'd)

- A utility with an oversupply of gas may successfully recover the cost by selling it in the open market
  - May be more difficult for pipeline capacity since it only has value in the markets that it connects

- In the last 5 years, interest in LT contracts has increased
  - On-going debate as to whether LT gas supply and/or upstream transportation contracts are required to support capital investment in transportation and frontier supply
    - E.g., The Alaska pipeline and LNG import facilities

Jurisdictional Review

Jurisdictions

- Ontario
- British Columbia
- Alberta
- Manitoba
- Georgia
- Massachusetts
- New York
- United Kingdom
- Germany

Ontario

- In its Natural Gas Forum report (the “Report”), the Board concluded that it will:

  1. “offer utilities the opportunity to apply for pre-approval of long-term supply and/or transportation contracts”

  2. “consult on the development of guidelines that will inform all stakeholders of the principles and issues the Board will consider when evaluating an application for contract pre-approval”

Ontario (cont'd)

- Gas utilities may enter into LT gas supply and upstream transportation contracts but cost recovery could be denied in a rate hearing
- Enbridge and Union have LT upstream transportation contracts in their portfolios
- Enbridge and Union do not have LT supply contracts
  - Short-term gas supply with indexed prices is the norm
  - Union however has 20% of its supply portfolio in rolling 2-year fixed price contracts
    - Union applied for pre-approval of these contracts, but the Board determined they did not require nor warrant pre-approval, as contemplated in the Report

British Columbia

- Terasen Gas offers regulated gas supply and provides upstream transportation and storage for both bundled and unbundled customers
- Long-term Resource Plan filed every two years
- Annual Contracting Plan approved by the BC Utilities Commission (BCUC)
  - Plan applies to commodity and midstream resources
  - Portfolio to include a mix of terms, including contracts one year and longer, appropriate for customers' security needs
- Contracts >1 month must be approved by the BCUC
  - Approval to occur before contract begins
  - Must be consistent with the annual contracting plan
  - BCUC approves buying procedures for contracts ≤1 month

Alberta

- System supply gas offered by the Default Supply Provider (DSP) under a regulated tariff
- DSP need not be the distributor
  - Direct Energy Regulated Services acquired commodity business from Atco
  - Atco now a “pipes-only” company
- Default supply portfolio includes only daily and monthly index contracts and spot purchases
  - Exclusive use of short term contracts provides accurate market pricing and operational flexibility
- No requirement for gas supply plan or contract pre-approval

Manitoba

- Centra offers default sales service, and is responsible for upstream transportation and balancing

- Gas supply, transportation, and storage contracts are filed with the Manitoba Public Utilities Board (MPUB)

- MPUB approves the "rate implications" of contracts in rate case or gas cost proceedings, but does not specifically pre-approve the contracts

Georgia

- Atlanta Gas Light (AGL) no longer sells gas, but is still responsible for upstream transportation and storage capacity
- The Georgia PSC approves the Capacity Supply Plan for the next 3-year period
  - AGL must spell out the options, its criteria for entering into contracts
  - Marketers participate in the process
  - PSC does not pre-approve the individual contracts to be executed, just the “array” of capacity assets

Massachusetts

- Retail unbundling with default service from the distributor
- 20-year Resource Plan filed every 2 years
- All gas supply, transportation, or storage contracts >1 year must be pre-approved
- Standard of Review
  - Consistent with portfolio objectives in the approved Resource Plan
  - Compares favourably with other options
  - Non-price objectives (flexibility, reliability, diversity)
  - Fair, open and competitive solicitation process

New York

1997

- Distributors expected to exit merchant business
- Marketers expected to hold upstream capacity
- Distributors told to minimize long-term contracts during transition

2007

- Distributors required to maintain upstream capacity needed for core markets
- Encouraged to hold long-term contracts to facilitate development of upstream transportation and storage
- Mandatory release of capacity to marketers

Europe

European Union

- 2004 Directive lists long-term gas supply contracts (>10 years) as an option for meeting supply security standards
- Will provide guidance on how long-term supply agreements should comply with competition law

United Kingdom

- Distributors do not sell gas
- Suppliers must have sufficient gas supplies to meet peak and annual customer needs (annual requirement)
- Ofgem has allowed long-term transportation capacity auctions to support infrastructure investments

Germany

- Cap on long-term contracts between importers and local utilities to encourage competition

Gas Supply

Options & Considerations

Appropriateness of long-term supply contracts

- How should the Board define LT supply contracts (e.g., longer than 2, 5, 10 years)?
- Is there a need for the natural gas utilities to enter into LT supply contracts?
  - What are the circumstances, benefits, and risks?
  - What are the implications of not entering into a LT contract?

Appropriateness of contracts pre-approval

- Is it appropriate for the Board to consider a pre-approval process?
- Should there be eligibility requirements (e.g., term, value, etc.)?
- Should contracts be reviewed on a stand-alone basis or in a portfolio context (e.g., taking into consideration diversity of sources, services and terms?)

Board considerations when evaluating an application

- What are the considerations the Board should take into account when determining whether to pre-approve a LT supply contract? Examples may include:
  - Need, costs, and benefits
  - Risk mitigation plan and risk allocation
  - Term of contract and effect on overall portfolio
  - Cost effectiveness in comparison to other alternatives
  - Others?

Review Process

- Is there a need to review pre-approved supply contracts ?
  - What should happen if the executed contract varies materially from the pre-approved contract?

Upstream Transportation Options & Considerations

Appropriateness of long-term upstream transportation contracts

- How should the Board define long-term upstream transportation contracts (e.g., longer than 2, 5, 10 years)?
- Is there a need for the natural gas utilities to enter into long-term upstream transportation contracts?
  - What are the circumstances, benefits, and risks?
  - What are the implications of not entering into a long-term contract?

Appropriateness of contracts pre-approval

- Is it appropriate for the Board to consider a pre-approval process?
- Should there be eligibility requirements (e.g., term, value, etc.)?
- Should contracts be reviewed on a stand-alone basis or in a portfolio context (e.g., taking into consideration diversity of sources, services and terms?)

Board considerations when evaluating an application

- What are the considerations the Board should take into account when determining whether to pre-approve a contract? Examples may include:
  - Need, costs, and benefits
  - Risk mitigation plan and risk allocation
  - Term of contract and effect on overall portfolio
  - Cost effectiveness in comparison to other alternatives
  - Others?

Review Process

- Is there a need to review pre-approved contracts ?
  - What should happen if the executed contract varies materially from the pre-approved contract?

Further Questions?