



Case & Project Experience

NERA's Role in TransCanada Ltd.'s 2011–2012 Restructuring Case

Overview

On 28 March 2013, Canada's National Energy Board (NEB) issued an important decision in the restructuring case of TransCanada Ltd, Canada's (and North America's) largest gas pipeline. The case was unusual not only for the issues involved but because it was the first time that the three major gas distributors in Eastern Canada acted collectively to oppose major moves proposed by TransCanada.

Background

TransCanada was constructed in the late 1950s primarily to transport gas from Alberta to Canada's eastern provinces. But that role has changed lately, as the abundant shale gas from the giant Marcellus shale field in the eastern United States—one-fourth the distance to those distributors than Alberta—has displaced those traditional Alberta supplies. Such shifting supply patterns have idled much of the capacity on TransCanada's multi-pipeline Mainline. Until 2011, TransCanada had been allowed by the NEB to raise Mainline tolls to recoup its cost of service over smaller Alberta-based volumes. But with an increasing substitution of Marcellus volumes for those in Canada, it has been clear that that practice could not continue. TransCanada's restructuring case involved many costing and toll-making issues emanating from this shift in the sources of gas for eastern Canada.

NERA's Role

Gaz Métro (serving Quebec), and Union Gas Ltd and Enbridge Gas Distribution (serving Ontario) retained NERA Senior Vice President Dr. Jeff D. Makhholm as a witnesses to represent them on a specific costing and toll design issues. Vice President Kurt Strunk served as consulting expert.

TransCanada had asked the NEB for authority to shift much of the book costs for the idled Mainline capacity to components of the pipeline system that the eastern Canadian distributors would use for short-haul services for Marcellus gas, and also to make other changes to toll design that would shift costs to Québec users that formerly were part of an integrated mileage-based toll design for all of TransCanada's costs. NERA opposed such changes as unduly discriminatory for the over three million gas consumers in eastern Canada and also contrary to the way in which the FERC had dealt with the issue years before when US interstate pipeline restructuring had idled certain segments of capacity between Texas and Southern California. The NEB agreed with NERA on these issues, rejecting TransCanada's proposed changes.

The Result

While the NEB permitted TransCanada to implement a number of tariff design changes meant to make its service offering more flexible, it rejected the company's requests meant to shield it from the competitive shift in the supply of gas. Ultimately, the NEB said that "TransCanada must not look to regulation to shield the Mainline from its fundamental business risk." As a result, it capped long haul representative tolls from Alberta to Ontario at \$1.42/gigajoule (GJ), down from the existing \$2.58/GJ, to remain in effect until 2017.

Ultimately, while the NEB permitted TransCanada some flexibility in toll design and cost deferrals, it declined to insulate the company from the broader effects of gas supply competition, saying:

If larger-than-forecast cost deferrals were to occur, they could represent a materialization of the Mainline's fundamental risk and costs could be disallowed. If costs were disallowed, it would not mean that TransCanada did not have a reasonable opportunity to recover costs, but rather that events did not turn out as forecast or that this opportunity was not seized by TransCanada. A potential outcome is that the Mainline would suffer a loss—just like another business that faces competition.

Experts Involved

Dr. Jeff D. Makhholm, Senior Vice President

Dr. Makhholm has extensive expertise and experience in gas supply planning as well as the organization, privatization, and regulation of the natural gas industry. He has advised governments and international governing agencies, regulators, public-owned and investor-owned pipeline companies, and large groups of pipeline users around the world on issues including determining reasonable interstate gas pipeline tariff levels, cost allocation for utility companies, forecasting the net market value for natural gas transportation and storage contracts, and reviewing nations' regulatory frameworks. Dr. Makhholm has provided expert testimony, published extensively, and spoken frequently on these issues. In 2012, Dr. Makhholm's book on the economics and institutions of pipeline regulation, *The Political Economy of Pipelines: A Century of Comparative Institutional Development*, was published by The University of Chicago Press.

Kurt G. Strunk, Vice President

Mr. Strunk has over 15 years of experience working on strategic, regulatory, and corporate financial issues in the energy industry. He has advised energy companies on rate cases, regulatory strategy, resource planning, contract and asset valuation, origination, hedging and risk management, prudence, cost of capital, affiliate transactions, and retail market issues. Mr. Strunk serves as a consulting and testifying expert in regulatory proceedings, commercial litigation, and arbitration proceedings. He has been retained as an expert to testify in US Tax Court, US Federal Court, and US Bankruptcy Court, as well as before public federal and state/provincial utilities boards in the US and Canada.

Stephen Collins, Associate Analyst

Stephen Collins, an analyst at NERA, has consulted in energy economics since 2010 and has on numerous occasions supported expert reports regarding energy and regulatory issues in North America and elsewhere. In Canada, he has consulted on behalf of a variety of energy distributors and stakeholders, including Gaz Métro, Enbridge, Union Gas, FEI, ATCO Gas, the Alberta Utilities Commission, and the Ontario Energy Board. He has worked for clients outside of North America in regions such as Oceania, Europe, and Latin America, and is a fluent speaker of Spanish.

About NERA

NERA Economic Consulting (www.nera.com) is a global firm of experts dedicated to applying economic, finance, and quantitative principles to complex business and legal challenges. For over half a century, NERA's economists have been creating strategies, studies, reports, expert testimony, and policy recommendations for government authorities and the world's leading law firms and corporations. We bring academic rigor, objectivity, and real world industry experience to bear on issues arising from competition, regulation, public policy, strategy, finance, and litigation.

NERA's clients value our ability to apply and communicate state-of-the-art approaches clearly and convincingly, our commitment to deliver unbiased findings, and our reputation for quality and independence. Our clients rely on the integrity and skills of our unparalleled team of economists and other experts backed by the resources and reliability of one of the world's largest economic consultancies. With its main office in New York City, NERA serves clients from more than 20 offices across North America, Europe, and Asia Pacific.

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