Day 11 - September 22, 2012 - Edmonton

International Reporting Inc. - Vol.79-SatSep22.12 - A3A3Q8

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27118

Review of methods to cover major spill costs

In yesterday's questioning, Northern Gateway Pipelines (NGP) said that raising tolls was one option to raising capital to cover losses due to a spill. Ms. Hales confirmed that tolls could only be raised subject to National Energy Board (NEB) approval.

NGP had also stated that Enbridge arranged a "facility" with lenders to provide immediate cash for costs with the Michigan spill, and recovered these funds later from insurance. Ms. Hales asked, "So … Enbridge accepted responsibility for the spill in that case?" Mr. Carruthers said, "Correct." 27144

Ms. Hales reviewed these and other resources that would be available for covering a loss from a spill. Mr. Carruthers responded. Insurance is anticipated to be around $250 million. Cash flow, around $400 million. Financing has no amount assigned to it. Raising tolls also has no quantification. Pausing dividends of $220-$330 million.

On the question as to Enbridge guaranteeing costs, Mr. Carruthers reiterated that it does not intend to do that and would not be a last resort. "What's the appropriate amount of insurance?" is the question, he said. "Do you put up a $500 million guarantee or do you invest 500 million to even further enhance the reliability of the system? And that's the approach that Enbridge took." 27212

Ms. Hales asked about the Aboriginal Equity arrangement, whereby the loan to acquire the equity is recovered over 30 years, before any net dividends are paid to the participating Aboriginal groups. If dividends are halted to recover spill costs, asked Ms. Hales, how will that work on repaying the equity loan? Mr. Carruthers was certain that the Aboriginal equity would be secure, but was uncertain about the financial aspects of that question. 27219

Aboriginal Equity: 26 First Nations out of 45

Ms. Hales explored the statements in previous days that 60% of Aboriginal communities have signed on for equity participation. Mr. Carruthers stated that in fact it is 26 First Nations out of 45 have "excecuted equity agreements," and that it would "represent a bigger number in terms of population."

Toll differentials

With respect to the discussion about a 77% difference between the tolls paid by funding participant committed shippers vs uncommitted shippers, Ms. Hales asks Mr. Earnest how common are differences of this magnitude. He would not speak to the Canadian situation, but did note that the Southern Lights diluent import pipeline has a two-to-one toll differential. 27251

Payback period for funding participants

Ms. Hales referred to illustrative tolls in Table 8, IR 11-12(d) (B101-2), and noted that funding participant (FP) term shippers are making a commitment of about a billion dollars when they sign a TSA for 15 years transporting 50,000 barrels a day, or $1.343 billion for 20 years. A non-FP shipper would be committing $1.584 billion over 20 years, a difference of $241 million or about $1 million a month over the 20 years. 27260

TABLE 8

Three Categories of Shippers	Relative Capital Portion	Relative Operating Portion
Funding Participant (FP) Term Shipper	100%	100%
Non FP Term Shipper	125%	100%
Uncommitted Spot Shipper	150%	150%

Actual Costs = Estimate	Capital Portion	Operating Portion*	Total
Funding Participant (FP) Term Shipper	2.64	1.04	3.68
Non FP Term Shipper	3.30	1.04	4.34
Uncommitted Spot Shipper	3.96	1.57	5.52

The FP shippers have invested $14 million towards pre-development costs, although it may be little higher. Ms. Hales stated that that will be recovered in 14 to 16 months because of the preferential toll. 27287

Ms. Hales clarified some details relating to funding participants and the direct owner. There are 10 funding participants, and 10 units. 9 FPs own between them 7 units, and one FP, also the direct owner, owns 3 units. 27338

Ms. Hales said of the direct owner, “Let’s call them MEG.” Mr. Fisher said “I don’t think I said MEG. I said a funding participant.” Ms. Hales said, “I was just inferring that from other evidence.” 27342

Ms. Hales asked about the entity in the ownership structure called Enbridge (Gateway) Holdings Inc. “Is this primarily a tax structure?” Mr. Carruthers replied that you keep them separate so it’s easier to effect a change in ownership. Then he added that there may be a project financing component. 27361

Wright Mansell impact study and cost benefit analysis

Ms. Hales turned to Dr. Mansell and asked him to explain the role of his estimates of economic impacts and the cost benefit analysis. Dr. Mansell's explanation is a good introduction to the two studies. The discussion begins at paragraph 27373.

The impact study was … to quantify some of the economic implications of constructing and operating the project. The cost benefit analysis … was simply in response to the cost benefit analysis submitted by Coastal First Nations. It was not a requirement of the National Energy Board and so it was really just in reply evidence. It was an exercise to put in more detail than was provided in the Coastal First Nations and, actually, better information; we had better information on a lot of the items.

Ms. Hales asked, "Which tool do you consider more reliable for assessing the project's public interest and its potential contribution to the Canadian economy?"

Dr. Mansell: They look at two different things. The impact analysis simply asks: What would be the implications for mostly broad macro variables like employment and labour income and value added and so on? And it really doesn't distinguish among projects in terms of their viability or return on investment. Or, put it differently, their efficiency. In a cost benefit analysis, on the other hand, that's exactly what you're testing. You're asking: What is the rate of return?

So if it was just from a private point of view, it would be a private cost benefit or cash flow analysis and you would simply be testing whether it will produce a return sufficient to justify the investment. In the case of a social cost benefit, we just expand out and cover more things; those things that would not necessarily involve market transactions. Like, we talked about the greenhouse gases, for example.

Market-based regulation

Dr. Mansell noted that the NEB had not required a cost-benefit analysis for a number of years, referring to a change in NEB practice when it shifted to market-based regulation. "Do you really need, for example, the cost-benefit analysis in a situation where you have the market sending a signal as to whether it is viable, required and so on." 27389

Mr. Priddle was Chairman of the NEB during this change in regulatory approach. He stated for the record, "It has been the Board's practice ever since the Express Pipeline proceeding [1996, Mr. Priddle chaired the review] to consider that the presence of completed firm service agreements is the central indication of need for a particular facility and the certificate that would govern it." 27404

Impact of tight labour market

Ms. Hales asked, "What the effect on your model results would be of a very tight labour market in Western Canada if, for example, a couple of other large projects were proceeding simultaneously? Including, for example, the LNG export projects and therefore competing with Gateway for skilled labour." Dr. Mansell replied, "To the extent that you stack more and more project in a very narrow timeframe, the more difficult it is to have those projects completed without dislocations. Which may be in the form of a run-up in wage costs, it may be in the form of delays. In general, things that … may not be in the overall benefit of the region." 27406

Foreign labour to construct project?

Ms. Hales: "How would your assessments of the benefits be affected if foreign labour were used to meet most the construction needs of this project?" Including importing components built in another country. Dr. Mansell replied, "In general, in order to prevent the unemployment rate from rising we have to have about a 2 percent growth in real GDP. So to the extent that these types of projects help maintain that growth you're simply preventing an increase in the unemployment rate. I would keep the Temporary Foreign Worker Program separate. I mean that program will exist with or without these projects." 27411

Diversification and option values

Ms. Hales quoted from Wright Mansell: "Significant diversification, stabilization, and option values [are] associated with the project. These benefits are difficult to quantify but they are nonetheless real and important, and they are in addition to the measurable direct and indirect contributions to Canadian incomes, production, employment and government revenues." She asked if these diversification and option values would help to protect agains adverse pricing impacts associated with market and policy shifts in the U.S. 27431

Dr. Mansell agreed, and provided the example that the analysis assumed no shut in production, and that without NGP that transportation requirements would be met by rail. But if rail could not meet the transportation demand, the consequence could be almost $15 billion of foregone sales because the product would be shut in without the diversification and option value of NGP. 27440

Potential conditions of licence

Ms. Hales said she will finish up with a few questions on some potential conditions that the Panel may place on the project. She noted, "The Panel will be issuing more definitive draft conditions at a later stage prior to final argument." 27466

- Set aside a larger percentage uncommitted capacity, say 20%. Mr. Carruthers suggested there would be concern about this, and it is a question of fairness to the funding participants. Mr. Fisher questions whether there'd be a market interest in that much spot capacity.
- Require long-term TSAs prior to start of construction. Mr. Fisher: We're assuming that will happen.
- Set a minimum volume, term, number of shippers. Mr. Priddle said he would recommend against that as it would impose how the market should function.
- Require a new open season. Mr. Fisher said this would "more or less restart the process" and would not be fair to the funding participants.

- Or require an open season where the negotiated TSA would be subject to comments by potential shippers. Mr. Fisher: "We've spent two and a half years negotiating the P/A, the TSA and the toll principles and we've set the path forward with our partners in this funding participant process. So again, I don't think it would be fair."
- Require Northern Gateway to file, before commencing construction, a fully-developed plan for financial assurances to meet all reasonable costs and liabilities arising from potential catastrophic events? That plan would then need to be updated annually or at some other regular interval. Mr. Carruthers appeared to accept this idea, as long as NGP was not required to develop scenarios which are unreasonable.
- Require that Northern Gateway maintain sufficient financial reserves. Mr. Carruthers replied that he'd rather have the previous condition than this one, which is a very inefficient way to manage your businesses.

Examination by Kenneth Bateman of the Joint Review Panel 27551

"Facility" to cover costs in Kalamazoo

Mr. Bateman asked about the facility Enbridge put together to cover costs related to the Kalamazoo incident. "Was the instrument or the program a legally enforceable program or was it just simply a decision by the corporation to assist?" Mr. Carruthers replied, "It goes primarily to our obligation that we're responsible for those costs and remediation. And whether or not it's insured is secondary. I believe that's relatively voluntary but ultimately it would be enforceable."

Mr. Bateman: "Was it created on an ad hoc basis as a result of the situation?" Mr. Carruthers' reply was ambiguous. Mr. Bateman asked whether "a similar approach is something that Gateway would likewise be willing to consider." Mr. Carruthers: "Yes very much so."

Mr. Bateman asked about the timeframe for assessment and payment. Mr. Carruthers indicated it was relatively quick. Mr. Bateman asked for follow up if there were significant claims that were greater than four months.

Examination by Sheila Leggett, Chairperson of the Joint Review Panel 27576

The Chairperson asked each of Mr. Earnest, Dr. Mansell, Mr. Anielski, and Dr. Ruitenbeek if any of them would make any changes to the methodologies that he used in preparing the technical reports.

Mr. Earnest replied, "I certainly would have included more information than in the original report that more fully and completely describe what I was doing and how I was doing the work. Over and above that, in terms of this price analyses I did, I'm really quite comfortable with the analysis in terms of the breadth and the level of detail." "It's my judgement that the benefit estimates likely would increase, primarily because the current view for Northern American crude production both in Canada and in the United States is higher today than it was even 12 months ago."

Mr. Anielski replied: “This work of value and ecological services is still in an emerging art and science. I would have wanted -- and this applies to any project so this is not just this project -- better biophysical risk assessment, better understanding of the ecological functions and degree to which these lands are currently sequestering carbon or absorbing nitrogen or whatever it is and applying more meaningful qualitative/quantitative baseline information to the valuation.” When I did my work, I'm comfortable with the assessment that the values that we've calculated assume almost a hundred percent loss of those ecological values. Now, that is not going to be the case. There's going to be a marginal change due to a linear disturbance or a physical impact on the land. 27592

Dr. Ruitenbeek replied, “There are actually two parts to this work that I was doing: One had to do with just the science or art, if you will, of environmental economic valuation and I'm quite comfortable with the way that was put forward. I wouldn't make any changes to the methods or to the conclusions.” He said that he would have “done a little bit more” in terms of monitoring.” “Within the risk area, which was the second area which has had some discussion here and which will have some discussion on other panels, I treated risk in a very technical way, taking the probabilities from the various other pieces of work, but I did not comment on individual perceptions of risk or social perceptions of risk.” 27601

Dr. Mansell replied, “I believe that the work we've provided uses fit-for-purpose models, well-established models. I believe the results that we've provided are fair, balanced and err on the side of being conservative. So, in general, I'm very confident in the result but you asked what could we do -- what would we do differently? The diversification and option value that we were discussing I think is really important but we need to find a way to measure it or better convey how one should look at it. I know, in a number of instances, we said it's important but we haven't quantified it.” 27615

He continued, “I probably say this each time after we come out of one of these exercises of: What can we do better? Find a better way to communicate what is often very technical detail to a broader audience.”

The Chairperson cited IR 11.12 (B101-2): “… overriding priority is to construct and operate the [pipeline] safely..." She then asked Mr. Carruthers to “colour that” for her. His lengthy reply began: “Fundamentally, in terms of the principles the project has to be built on … would be the commitment to spending more money. I mean, it started with the commitment of putting the pipelines through tunnels to avoid issues. It started with our extended responsibility to ensure a safe marine in terms of the response capability and the operational limits. Those things all go to that philosophy of trying to reduce the risk to as close to as zero as practicable.” 27629

She then cited from the transcript, “"Northern Gateway's general liability insurance would consider eligible clean-up and environmental costs of an oil spill,” and asked what would be considered eligible. Mr. Carruthers replied, “I'm not aware of costs that were deemed to be ineligible. With respect to Kalamazoo, …if they were the result of the spill, they were paid. I'm not aware of costs that weren't. … Fines and penalties are not covered by insurance, so those things would be outside the insurance policy.”

Introduction of Alberta Federation of Labour Panel by Leanne Chahley
27674

Ms. Chahley introduced the two members of AFL's panel - Gil McGowan, President of the Alberta Federation of Labour, and Robyn Allan, an economist with extensive experience in economics and insurance - then asked that they be sworn in. Following the swearing in, Ms. Chahley asked the witnessess to confirm that exhibits filed as CV's and direct evidence as well as other evidentiary exhibits, if any, were hers and his. Each panellist then reviewed corrections that needed to be introduced into the record.

The witnesses, and the evidence relevant to this particular panel:

Ms. Robyn Allan [D4-18-2 CV], [D4-19-3 Direct Evidence]
- A long list of Ms. Allan's evidence filed on behalf of AFL begins in the transcript at paragraph 27686.

Mr. Gil McGowan [D4-14-2 CV], [D4-19-2 Direct Evidence]
- A list of Mr. McGowan's evidence filed on behalf of AFL begins in the transcript at paragraph 27711.

Ms. Chahley noted that Ms. Allan has not appeared as an expert before the NEB but submitted that her résumé qualifies her to provide expert evidence in the areas of macroeconomics and insurance. She has discussed this Mr. Neufeld from Northern Gateway who accepts the witness, but will test her expertise during questioning. The Panel accepted Ms. Allan.

Examination by Keith Bergner for the Canadian Association of Petroleum Producers (CAPP), 27734

Mr. Bergner began by stating that he had no questions for Ms. Allan, and would question Mr. McGowan on Exhibit D4 zero to 2. He obtained from Mr. McGowan the number of members in the AFL (~150,000 today, ~100,000 in 2005), the number of members (29), that about half of the members work in the public sector and half in the private sector, and that the Communications, Energy and Paperworkers (CEP) are a member union as well as an intervenor in the NGP proceeding.

Mr. McGowan stated that very few of the AFL members work in production, "as in upstream energy." "It's one of the sectors in the economy with the lowest unionization rates."

Mr. Bergner replied that "Given the very low membership in production, is it fair to say that your membership has little to lose if there are policies implemented that have negative impacts on the producing sector?" Mr. McGowan disagreed, stating that AFL does have members who work in the sector and the health of the energy sector has a profound significance to all of the AFL members because the sector is such a large portion of the Alberta economy.

AFL wants bitumen to be upgraded before exporting

Mr. Bergner asked, "You wouldn't be here opposing a pipeline to ship synthetic crude oil that had been upgraded in Alberta or in Canada; correct?" Mr. McGowan replied, "At the very least, we would prefer that bitumen extracted here in Canada be upgraded to synthetic crude before it's exported to any markets, either domestic or foreign." 27818

Mr. Bergner asked, "Does AFL take the position that existing pipelines in Canada that ship what you refer to as unprocessed bitumen should be stopped? Mr. McGowan, "Yes. And we've been on the record as opposing the approval -- the application and approval of all pipelines which have primarily been proposed or built for exporting raw bitumen, including the Keystone Phase 1, Keystone XL, the Alberta Clipper, the Southern Lights. We've been here many times before making similar arguments."

Mr. McGowan continued answering Mr. Bergner's questions, articulating the AFL's concerns: "When we are exporting these very valuable resources -- which I will remind you are owned by the public -- we just want to make sure that we're getting the most value. And that value is realized both in terms of the price that the producers get, but also in the creation of jobs, and especially long-term jobs. We're opposed to the export of raw bitumen, but I won't say that we're opposed to any particular pipeline. If the pipeline is being used to export raw bitumen, then we'll be -- we're opposed to that use." 27836

Today, Alberta upgrades about 60% of raw bitumen to synthetic crude. Mr. McGowan cited a Wood Mackenzie report [Exhibit E8-6-2] prepared for the Province of Alberta which projects that by 2025 only about 26% of bitumen in Alberta will be upgraded. "This is deeply troubling for us in the labour movement because, as our former Premier Peter Lougheed has said, you know, before his recent death, the real jobs in the oil sands are in upgrading." 27847

Mr. McGowan stated that the AFL has a different understanding of the problem facing Alberta and its petroleum producers as presented by CAPP and by Enbridge. Their "[Their].argument is that, in order to deal with the price discount, the only solution that is viable is to find new markets abroad, especially in places like China and Asia, more broadly speaking. We at the AFL … argue that … we have an overproduction problem. We've simply flooded the market in the United States and in a sense the discount is something that we're doing to ourselves. Other oil producing jurisdictions around the world, when faced with similar problems -- and I'm talking most notably about OPEC nations like Saudi Arabia -- will put the brakes on production. So that's the first part of the problem. The second part of the problem, as we see it, is that we are actually not selling the right product, and in particular, we will make the argument -- and this may seem a little bit contentious, we make the argument that bitumen is not oil," 27892

The Chairperson advised Mr. McGowan to answer Mr. Bergner's questions.

Restricting exports and the National Energy Program

Mr. Bergner said that Canada has had experience with the policy of restricting exports with the National Energy Program and that it wasn't a terribly successful policy. Mr. McGowan pointed in reply to "another Alberta-based example of export restrictions that, instead of being a catastrophe, as you characterize it, was a roaring success." In 1971, Alberta was confronted with a situation which, in many respects, is similar to the one that we're dealing with, with bitumen. The resource was natural gas and the Lougheed government introduced export restrictions. They had a regulation which basically said that the natural gas liquids had to be stripped off and made available to Alberta-based producers before being exported to other markets.As a result of this export restriction policy, the Lougheed government created a petrochemical industry, which, for about 20 years, was the second largest industry in the province and still generates about $19 billion of revenue every year and employs thousands of people. 27927

The Chairperson again: "Mr. McGowan, speaking quickly, first of all, is a real problem for the record. So trying to speak quickly to get as much information on the record as possible is not helpful to the Panel." 27943

"Who makes the decision about building upgraders? Is that a government decision or is that a private sector decision?" Mr. Bergner asked. Mr. McGowan replied, "It can be a government decision if policymakers decide that upgrading is a priority. So in the same way that the Alberta government in the seventies decided that creating a homegrown petrochemical industry was a priority." 27956

Mr. Bergner asked, "Do you agree that well-functioning markets tend to produce outcomes that are in the public interest?" Mr. McGowan: "I would agree that where markets function well, they produce outcomes that are in the public interest. But it's clear to us, based on the evidence, that the global market for oil is not a freely functioning market as envisioned by classical economic theory." 28007

Examination by Don Davies for Cenovus Energy, Nexen, Suncor Energy Marketing, and Total E&P (Cenovus et al), 28027

Mr. Davies asked, In its "Lost Down the Pipeline Report" (Exhibit D4-2-12), the AFL wants the Alberta Government to reject what it calls "Free-market fundamentalism" and instead use a mix of regulation and public ownership to jump-start investment in upgrading and refining facilities in Alberta; right? Mr. McGowan replied, "Yes." 28048

NAFTA and upgrading

Mr. Davies asked about NAFTA. Mr. McGowan replied, "We in the labour movement feel that the energy section of NAFTA is a straightjacket on Canadian policymakers, making it difficult if not impossible for them to pursue the public interest and give Canadians, who own the resource, what they want, which is more upgrading and more refining." 28061

NGP and upgrading

“but that if Northern Gateway does not proceed, new upgraders will be built in Alberta?” Mr. Davies asked. Mr. McGowan replied, “If the pipeline is built it will undermine the chances of building upgraders. If it’s not built, that’s not a guarantee that they’ll be built, but it improves the chances that they will.” 28117

Mr. Davies asked the same question a number of times, seeking a yes or no answer from Mr. McGowan, which he refused to give. After his final iteration of the question, ending with, “Say ‘no’ and we can all go home,” Mr. McGowan replied, “Yeah, well, you know, you talk about politician tricks and, in this regard, I'm going to have to talk about lawyer tricks because you're trying to get me to say something on the record that is not an accurate characterization of our position.” The Chairperson stepped in again, “Mr. McGowan, again, I would ask you to answer the question that has been posed to you.”

Mr. McGowan: “No, it is not an accurate characterization of our position.”