



October 1, 2013

National Energy Board  
444 -7<sup>th</sup> Avenue SW  
Calgary, AB T2P 0X8

By email – [finrespguidelines@neb-one.gc.ca](mailto:finrespguidelines@neb-one.gc.ca)

**RE: Draft Financial Viability and Financial Responsibility Guidelines – COGOA**

The National Energy Board (NEB) has issued for comment "Draft Financial Viability and Financial Responsibility Guidelines" (Draft Guidelines) that would be applicable, if adopted, to all areas and activities regulated under the *Canada Oil and Gas Operations Act* (COGOA). The Canadian Energy Pipeline Association (CEPA) is pleased to provide the following comments on behalf of its member companies. CEPA represents energy transmission companies whose pipelines and related facilities transport 97% of the oil and natural gas produced in Canada to markets throughout North America.

We understand from recent comments by Minister Oliver<sup>1</sup> that it may be the intention of the government to extend these principles of financial responsibility to onshore pipelines regulated under the *National Energy Board Act* (NEB Act). CEPA believes that its members are currently in compliance with the intent of such a decision, but we support the updating of regulation to provide the public with a clear set of enforceable requirements upon which to be confident that the industry is managing this issue effectively.

CEPA agrees with the fundamental principles underlying the Draft Guidelines and believes it is prudent to:

- identify a reasonably well scoped worst case scenario (WCS);
- have assurance that the operator has funds available to contain a spill immediately; and
- ensure that the operator has access to sufficient financial capacity to ensure containment, remediation and appropriate compensation of affected parties.

CEPA-member companies take responsibility for all phases of emergency response, remediation, and reclamation in the event of an incident and will continue to do so, regardless of regulation. Major transmission pipeline companies currently have:

- programs to prevent and manage incidents, as required under the Onshore Pipeline Regulations;
- insurance to manage the costs of incidents; and
- financial capacity to backstop insurance instruments.

Our following comments are not specific to COGOA, but rather relate to the development of parallel guidelines or regulations for the onshore pipeline industry, should the government and the Board consider that course of action in the future.

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<sup>1</sup> <http://www.nrcan.gc.ca/media-room/news-release/2013/7225>

### **Applicability of Financial Responsibility Requirements on a Project-Specific Basis**

The current practice of most major pipeline operators is to acquire insurance at a parent company level, covering and available to all of its pipelines. CEPA believes this is the most appropriate way to ensure maximum financial responsibility without over-insuring assets at excessive cost that degrades capital efficiency. Therefore, application of financial responsibility requirements on a project-by-project basis or an asset-specific basis would not be a viable way to extend application of the COGOA approach to pipelines regulated under the NEB Act.

### **Phased-In Application to Existing Pipelines**

The NRCan press release referenced above indicates that the government intends to apply these requirements for proof of financial responsibility to existing pipeline facilities over a 12-month transition period.

CEPA suggests that the schedule for a 12-month transition period is too aggressive and recommends that it be replaced by a phased-in approach in which existing pipelines would be required to file evidence that they are in compliance within 12 months, after which time the Board would consider further action as appropriate, such as

- prompt acknowledgement that the existing financial capability is adequate;
- initiation of a regulatory process to test the adequacy; or
- order preliminary changes as necessary.

### **Agreement on a Worst Case Scenario**

In the NEB's Draft Guidelines for COGOA-regulated activities, proof of financial responsibility and consequent financial obligations are linked to the development and agreement by the proponent and the NEB (and presumably other stakeholders) on the 'worst case scenario' (WCS). This scenario is the basis for estimation of the costs of containment, clean up, and appropriate compensation to affected third parties in the event of an incident and subsequent determination of the amount and form of financial security to be provided by the proponent. CEPA supports this WCS-based approach to determination of financial responsibility. We also support the clear distinction between funds required immediately for containment and longer-term funding from a range of sources for cleanup and compensation.

In the Draft Guidelines, the NEB has provided a list of some of the elements that should be considered in the development of a WCS. CEPA recommends that the guidelines be made clear that the WCS be defined as a reasonable worst case scenario, rather than an extreme worst case scenario. Many parties will have views on the WCS, and the issue will be a key point of discussion in the NEB's environmental assessment and regulatory process. The NEB will be required to arbitrate and decide on a reasonable WCS. Given that CEPA is recommending that financial capability be determined at the parent-company level, the WCS will need to be based on each company's unique pipeline system.

### **Quantum of Financial Capability**

CEPA believes that companies should be required to demonstrate financial capability (third party coverage or self-insurance capacity) based on the reasonable worst case scenario for their specific facilities and projects, rather than in accordance with an arbitrary limit of C\$1 billion, as indicated in the NRCan press release. If one pipeline company's reasonable WCS and risk are assessed at C\$250 million, they should demonstrate financial capability at that level. If another company's reasonable WCS is assessed at C\$750 million, they should demonstrate financial capability based on that reasonable WCS. CEPA believes that an arbitrary level of financial capability for all companies is not efficient and therefore does not support or enhance the goal of protecting the public and the environment.

CEPA recommends the following approach:

- determine at the outset that the objective is a parent-company-wide demonstration of financial capability to respond to accidents or leaks, not an asset- or project-specific approach;
- use a parent-company-wide risk profile of the company and accordingly, determine the accessible amount and type of financial capability required; and
- adjust the risk profile and financial capability requirements as new facilities are added or old facilities are decommissioned.

## **Components of Financial Capability and Their Use**

The Draft Guidelines require that companies demonstrate their ability to pay the full cost of addressing a WCS. This can be achieved through a combination of financial instruments:

- unfettered funds, likely in the form of irrevocable letters of credit to cover costs of containment
- spill and pollution insurance coverage for cleanup, remediation and compensation
- self-insurance with confirmation by the Accountable Officer that sufficient funds are and will be available if the company chooses to self-insure.

If the costs of addressing a worst case scenario are not fully covered by the above, then other instruments must be considered to make up any short-fall:

- additional third-party insurance
- audited financial statements demonstrating financial strength with readily accessible capital to cover the worst case scenario
- additional letter of credit
- parental or third party guarantee
- industry group fund

We believe this range of instruments offers flexibility to the NEB and to companies in meeting the intent of the regulation. CEPA offers the following comments on these types of instruments and their proposed application and use by the NEB.

## **NEB Role in Response**

The Draft Guidelines afford the NEB the discretion to take control of emergency response in the event that the NEB considers an operator to not be responding adequately to an incident. Although CEPA understands that such provisions give comfort to the public, we do not believe that they are necessary or desirable for the pipeline industry and should only be considered in the most extraordinary circumstances and upon strong evidence that the company is unwilling or unable to respond as the NEB considers appropriate.

For the pipeline industry, the pipeline operator is far better placed to manage a spill than the NEB, because it is familiar with the pipeline and its spill contingency plan and has direct control of and authority over the technical and financial resources needed to respond. Locally-based company staff have direct connections to senior management and a relationship with local first responders available to assist. Above all, the company has the greatest motivation to stop the incident and bring the pipeline back into compliance and into service as soon as possible.

If the NEB maintains the ability to take over the response, there should be clear guidelines by which a pipeline operator is deemed to be non-responsive. The consequences of having any third party take over responsibility for containment/clean-up, as noted above, are very serious and may have long-term financial consequences for both the operator and the NEB in the situation.

## **Irrevocable Letters of Credit**

CEPA notes that costs of containment are typically an order of magnitude less than costs for cleanup and remediation. An irrevocable letter of credit (LOC) to be drawn upon solely for containment may be the appropriate instrument for ensuring rapid access to funds in an initial response phase in some circumstances where overall balance sheet strength is questionable. However, it is not prudent, however, to incur LOC costs where liquid assets exist to cover immediate response and containment.

The Draft Guidelines also indicate that the NEB would have the discretion to use the spill containment funds available through the LOC for other purposes, including compensation. CEPA believes this discretion is unnecessary and inconsistent with the purposes of the LOC. There are established means of determining compensation and damages from accidents and pipeline leaks including litigation and insurance. Use of these funds for purposes for which they are not intended prior to discussion or consideration creates significant risk that the costs will not be recoverable from insurers. The NEB may order compensation from any source it wishes, without resorting to use of the containment funds.

### **Spill Liability Insurance**

The Draft Guidelines require that the NEB is named as a beneficiary of spill liability insurance policies. CEPA believes this is unnecessary as a general requirement of all companies. If this requirement is designed solely to facilitate the NEB taking control of spill response, then we repeat our comments above, that the NEB is not the best-placed responder and can order whatever action it determines is necessary without this provision. Further, it potentially puts the NEB in the position of having to negotiate directly with the insurance companies which may not be the most effective or efficient method to establish the ultimate cost split between the company and its insurer(s).

The Draft Guidelines anticipate that insurance will be available on a continuous basis. This may not be consistent with how insurance coverage is provided.

### **Audited Financial Statements**

The Draft Guidelines indicate that any shortfall in financial responsibility through LOCs and insurance (third party or self) to meet the costs of the WCS may be made up through a number of other instruments, including provision of audited financial statements that demonstrate sufficient financial strength or readily accessible capital. CEPA can support this as an option if it is within the company's discretion. We note that new pipeline operators may not be rated or may not be in a position to provide such statements.

### **Pooled Industry Group Fund**

The NEB offers the option of an 'industry group fund' as an 'other financial instrument'. Such a scheme across operating pipeline companies does not currently exist. CEPA member companies may consider this approach.

### **Closure**

In closing, CEPA views these Draft Guidelines for COGOA facilities as an initial step in addressing an important issue for the industry, the NEB, and the Canadian public. Application of the approaches set out in this Draft Guideline to onshore pipeline facilities will require adjustments to acknowledge the strong regulatory regime under which our facilities already operate, the extensive operational experience of the industry, and its commitment to safety and pipeline integrity. Throughout our comments, we support approaches that provide flexibility for the NEB and for CEPA-member companies to achieve the desired outcomes, rather than specific requirements that are immutably set in regulation.

In summary, our key recommendations regarding future application of similar guidelines to facilities regulated under the NEB Act are:

- financial capability should be based on a company-wide, not asset- or project-specific, consideration of risk
- financial capability should be commensurate with risk and a well-defined reasonable worst case scenario, not based on an arbitrary specified limit
- pipeline operators are best-placed to respond to any incident involving their facilities; assumption of management control by the NEB should only be considered in extraordinary circumstances

CEPA and its member companies look forward to continuing the discussion of how best to ensure continued strong responsibility and performance, and to build and confirm the confidence of the Canadian public that their safety and protection of the environment are of paramount importance to our industry.

Yours truly,



Brenda Kenny  
President and CEO

c.c.: Jeff Labonté, Director General, NRCan