AltaGas Ltd.

Second Quarter 2020 Financial Results Conference Call

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PRESENTATION

Operator

Welcome to the AltaGas Second Quarter 2020 Financial Results Conference Call. My name is Chris, and I will be your Operator for today's call.

All lines have been placed on mute to prevent any background noise. If you have any difficulties hearing the conference, please press star, and then zero for Operator assistance at any time. After the speaker remarks, there will be a question-and-answer session. As a reminder, this conference call is being broadcast live on the Internet and recorded.

I would now like to turn the conference call over to Adam McKnight, Director of Investor Relations. Please go ahead, Mr. McKnight.

Adam McKnight — Director of Investor Relations, AltaGas Ltd.

Thanks, Chris. Good morning, everyone. Thank you for joining us today for the AltaGas second quarter 2020 financial results conference call. Speaking on the call this morning will be Randy Crawford, President and Chief Executive Officer, James Harbilas, Executive Vice President and Chief Financial Officer. We are also joined here this morning by Randy Toone, Executive Vice President and President of our Midstream business, Blue Jenkins, Executive Vice President and President of our Utilities business and Washington Gas, and new to the team, John Morrison, Senior Vice President, Investor Relations and Corporate Development.

As always, today's prepared remarks will be followed by an analyst question-and-answer period. I'll remind everyone that the Investor Relations team will be available after the call for any follow-up or detailed modeling questions. We'll proceed on the basis that everyone has taken the opportunity to view the press release that we issued earlier today and also remind everyone that we will refer to forward-looking information on today's call.

This information is subject to the risks and uncertainties as outlined in the forward-looking information disclosure on Slide 2 of our presentation which can be found on our website and more fully within our public disclosure filings on the EDGAR or the SEDAR system.

As for the structure of the call, we'll start with Randy Crawford to review some strategic and other focus points, followed by James Harbilas on the financial results and outlook, then we'll turn it over for a healthy Q&A session.

With that, I'll now turn the call over to Randy Crawford.

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Thank you, Adam, and good morning everyone. AltaGas delivered strong second quarter results and continued to perform well, both financially and operationally while managing the ongoing impacts of the COVID-19 pandemic. Despite the challenges created by the pandemic, our second quarter normalized EBITDA adjusted for prior year sale, asset sales increased by more than 13 percent versus the prior year comparable quarter and we are well positioned to meet our overall objectives for the year.

We continue to be pleased with the resilience and durability that our Midstream and Utility businesses have exhibited. We believe this is a testament to our diversified platform and our purposeful actions that we have taken over the past 18 months to focus the Company, de-risk the platform and reduce financial leverage.

I am proud of the fact that our dedicated workforce has been able to maintain safe and reliable operation, continue to deliver critical energy to our customers, and honour our social and moral contract with the communities we serve. This achievement was only possible through their tireless efforts, adaptability and our valued vendor partners. Our people are the heart of this Company and their spirit and resilience ensures my confidence that we will continue to execute our strategy and maintain our commitment to safety and operational excellence.

At AltaGas we have an unwavering commitment to our core values. It's our approach to governance and oversight, combined with how we invest in and support our people, our customers, our communities, and the environment that will allow us to build, both a sustainable and financial, successful future.

We are committed to diversity and inclusion. Diverse and inclusive teams are better positioned to deliver more positive business results for the communities that we serve. Our commitment to having a diverse workforce and inclusive culture is not new and our diversity metrics reflect the communities we serve. We remain committed to continue our efforts to build more diverse and inclusive teams going forward.

Our Utility business has continued its strong execution during the quarter. Our focus on operational excellence at WGL continues to progress well with the year-to-date operating income up nearly 10 percent versus the prior year comparable period. Our transmission and distribution systems continue to operate in line with our high reliability standard. This strong execution is a result of the capital investments we have made over the past few years through our accelerated pipeline replacement program and our renewed focus on operational excellence to enhance our customer value proposition, provide outstanding customer service, and clean energy solutions.

We remain committed to continue our history of proven energy innovation and to focus on environmental, social and governance issues or ESG. Both AltaGas and Washington Gas have excelled in bringing new clean energy sources to customers. Of note, WGL has filed with the Washington DC Commission our plan to deliver our commitment to help Washington DC and our world to meet future climate goals. The plan builds on the foundation of key ESG elements we have been focused on for more than 25 years.

Through collaboration with the district to implement the steps towards decarbonization, it provides us the opportunity to continue to leverage our resilient, fast and established energy delivering storage system to reduce emissions while providing affordable and reliable energy. Our plan promotes customer energy efficiency and savings, builds and maintains a modern infrastructure for today and the future, and introduces carbon free fuels, such as renewable natural gas and hydrogen. This includes investing in and piloting some of these emerging technologies and will maintain and enhance the region's position as responsible climate leaders.

Our Midstream segment continues to leverage our unique structural advantage to export cleaner energy to Asia and expand our footprint in Northeast BC. RIPET celebrated its first-year anniversary of being operational in the quarter and had another strong performance with the terminal contributing $30 million in normalized EBITDA.

In Q2, we reported nearly 42,000 barrels a day of Canadian propane to Asia spread across seven ships. We were also very close to loading an eighth ship at the end of June, but that was pushed to July

1st and July 2nd, and will now be captured in the third quarter. With strong execution from the Midstream team and the work we are doing with our strategic partners to bring operations and logistics together, we remain confident that we will be able to hit our 50,000 barrels a day export target before year-end.

This business is well positioned to continue to deliver ongoing financial performance with approximately 70 percent of our Midstream normalized EBITDA being underpinned by take-or-pay and fee-for-service agreement. In addition, 86 percent of RIPET's 2020 expected export volumes are underpinned by tolling agreements or hedge price contract.

We were also pleased to see the transaction announced last week where Kelt Exploration, one of our high-quality customers in Northeastern BC, sold its Inga assets to ConocoPhillips for more than $500 million. We look forward to working with ConocoPhillips as the Company expands its presence in the region. The transaction validates our thesis behind building a leading Midstream presence in Northeastern BC and further positions us to lean on recent CAPEX deployments, including the North Pine and Townsend expansions that came online in the quarter, as well as RIPET to deliver stable results.

We are excited about the opportunity to expand our LPG export footprint and Midstream presence through our acquisition of an increased ownership of Petrogas, confident that this transaction will create value for our shareholders and customers. It will expand our Midstream value proposition through the increase of additional assets at Ferndale and Fort Saskatchewan, we will continue to advance our strategic goal towards operating a fully integrated logistics network that underpins our position as a leading Midstream company.

We continue to focus on operational excellence business model, improving our financial returns and driving value within our existing core assets. We are building a resilient business that is focused on creating durable and expanding earnings. There is simply no better way to generate value for our shareholders and improving the return on capital has already been deployed and ensuring a return above our cost of capital on all new organic investment. We are immensely proud of what we have accomplished in the past 18 months. There is more good work left to be done and we look forward to continuing that work.

We believe there is a uniqueness in our diversified model. We have the opportunity for industry leading rate-based growth at our Utilities. We are positioned to be able to internally fund the growth of our Utilities rate base and reduce debt through the significant excess free cash flow coming from our strong and growing Midstream business and redeploy a portion of those funds into our profitable investment in our rate-based growth at our Utility operation.

Having the ability to operate a self-funding model with the opportunity to profitably execute on one of the highest rate-based growths in the industry is a rarity and we're excited for the opportunity. We remain committed to continue adding shareholder value. Our actions will follow the well-defined strategy that we've laid out. The journey to achieving operational excellence is continuous and we are relentlessly evaluating what other levers we may pull with a driven and creative team that is focused on continuous improvement.

Overall, we are pleased with the progress we've made so far in 2020. Heading into the second half of the year, we believe we are well positioned to achieve the previously disclosed full year expectations and are well positioned for profitable earnings growth into the future.

In summary, we are pleased with the second quarter operating and financial results and the ongoing resiliency of the platform. We firmly believe in our Utilities infrastructure investment program. It continues our commitment to improve safety and provide reliable value to our customers and positions us to create a more carbon neutral environment.

We have the unique opportunity to grow our Midstream business through our strategic footprint in Northeast BC and our ability to increase the export of Canadian produced propane to Asia. Our recent investments in Townsend, North Pine and RIPET, position us to capture a significant free cash flow, that will provide us the opportunity to grow our utilities rate base, reduce debt and increase dividend.

And with that, I will turn the discussion over to James.

James Harbilas — Executive Vice President and Chief Financial Officer, AltaGas Ltd.

Thank you, Randy and good morning everyone.

Looking at the financial highlights of the second quarter, our diversified platform continues to provide predictable and reliable performance. Within the Midstream segment, we realized continued strong operations at RIPET including record export volumes in the quarter, which was aided by contributions from the Townsend 2B and North Pine expansions.

Within our Utility segment, results reflected the normal seasonal slowdown in energy demand that is associated with the spring and summer months. Positively, we realized growth across each of our regulated utilities driven by 2019 rate cases and continued spending in our accelerated replacement programs. The most significant headwind in the quarter was lower margins within our retail business which was underpinned by COVID-19 impacts and pressures on some of our commercial and industrial customers.

The business unit is a small component of our platform representing approximately 3 percent of 2020 estimated EBITDA. Normalized EBITDA came in at $206 million for the quarter, slightly below Q2 2019 levels of $211 million. Excluding lost EBITDA of approximately $29 million associated with the non-core asset sales, our remaining businesses grew by approximately 13 percent year-over-year.

Normalized net income for the second quarter was $17 million or $0.06 per share, up considerably from $1 million in Q2 2019. Overall lower interest and depreciation and amortization expenses were partially offset by higher income taxes. Interest expense was down approximately $12 million year-over-year on lower debt balances as a result of the deleveraging work we completed over the past year, combined with lower interest rates on refinances.

Depreciation and amortization expense was lower by approximately $14 million year-over-year primarily due to asset sales and a one-time adjustment related to the termination of a natural gas contract for purchase commitments in the U.S. Midstream business. Finally, income taxes were higher by $10 million largely due to higher earnings in the quarter.

Normalized funds from operations were up approximately 18 percent year-over-year to $141 million or $0.51 per share due to lower current interest expense and lower current income tax expense. During the quarter, we successfully refinanced all our remaining 2020 maturities through two debt financings. This included SEMCO, completing a private placement of US$450 million of first mortgage bonds on April 21st and AltaGas closing a $500 million issue of senior unsecured notes on June 10th.

These two issuances combined with lower interest rates are expected to result in interest expense savings of approximately $9 million in 2020 and roughly $14 million on an annualized basis.

We also continue to make progress on our strategy to focus the business. In June, we entered into a stock purchase agreement with Clarion Energy to sell the Ripon facility. The transaction is expected to close in the third quarter. Subsequent to quarter end, on July 20th, we closed the sale of the Pomona battery storage facility for gross proceeds of US$47 million, less closing working capital adjustments. Although the transaction was smaller in scale compared to past divestitures, it demonstrates our continued efforts on focusing the business and will be slightly credit positive.

Normalized EBITDA within the Utilities segment was $80 million for the quarter, slightly below Q2 2019. As I previously mentioned, growth at our regulated utilities was driven by our 2019 settled rate cases, ARP spending and strong operational execution, which was partially overshadowed by COVID-19 related impacts, including lower margins in our retail business.

As a reminder, approximately 70 percent of our regulated utilities earnings are protected through decoupling and fixed billing charges. In all the jurisdictions where we operate have approved the creation of regulatory assets to allow for the recovery of incremental costs related to COVID-19. We are tracking these costs and our lost revenue due to the pandemic and we will continue to work with our regulators on the definitions and treatment of recoverable impacts within those regulatory assets.

We anticipate that a portion of our COVID-19 related impacts within our regulated utilities will be recoverable down the road, however there will be a timing lag associated with these recaptures. At the regulated utilities, WGL's normalized EBITDA was approximately $44 million for the second quarter, up

$3 million year-over-year on higher revenue from the Maryland and Virginia rate cases and higher accelerated pipe replacement program spending.

This growth was partially offset by the cancellation of late fees and service charges revenue due to regulatory orders that suspended this activity in our jurisdictions as a result of COVID-19. We also experienced less usage for C&I customers in certain jurisdictions that don't benefit from decoupling.

In Michigan, SEMCO contributed $21 million in normalized EBITDA in the second quarter, up $3 million year-over-year. Higher rates associated with the 2019 rate case and colder weather were partially offset by lower customer usage. ENSTAR and CINGSA contributed $17 million of normalized EBITDA for the quarter which was in line with last year and our expectations.

Lastly, in the Utilities segment, normalized EBITDA from the retail business was lower by $7 million year-over-year, primarily due to lower margins associated with COVID-19. This is where we saw some of the largest impact of the pandemic, but we do not expect this to result in a long-term or lasting impact on the platform. All-in-all, we are pleased with the performance of the Utilities business and the stability that it continues to demonstrate.

Looking ahead though the remainder of the year, we believe the largest of the COVID-19 related impacts within our regulated utilities platform are behind us, but we caveat that by acknowledging that we are living in uncertain times, as a result of the pandemic that changed from week-to-week. Within the retail business, things have started to improve and the third and fourth quarters are expected to exhibit performance that is pushing back towards more traditional operating patterns.

Within the Midstream segment, second quarter normalized EBITDA was $111 million, up approximately 9 percent over Q2 2019. Factoring in lost EBITDA of approximately $14 million associated with the 2019 sale of Stonewall and Central Penn, our remaining Midstream business grew by approximately 26 percent year-over-year.

RIPET generated approximately $30 million of normalized EBITDA in the second quarter on exports of nearly 42,000 barrels per day, spread across seven ships. This equates to a blended EBITDA margin of approximately $8 per barrel. Approximately 30,000 barrels of RIPET's second quarter export volumes were hedged at an average spread of approximately US$9 per barrel. Fractionation in liquids handling volumes increased in the second quarter, due to the North Pine expansion, and the Townsend deep cut facility that were brought into service earlier this year.

Growth was partially offset by lower volumes at Harmattan due to reduced upstream activities and shut-ins that were associated with low commodity prices. Positively, we have seen much of those volumes come back in recent weeks as shut-ins have been brought back online. Gas processing volumes were modestly lower in the second quarter versus the same quarter last year. New volumes at the Nig Creek and Townsend deep cut facilities, and higher interruptible volumes at Gordondale were more than offset by lower volumes at Blair Creek and the Townsend shallow cut facilities, as well as lower volumes at the extraction facilities, due to reduced upstream activity. We have seen volumes improve at our facilities to start Q3.

During the second quarter, we recorded equity earnings of $7 million from Petrogas compared to $11 million in the same quarter of 2019. The decrease was due to the slowdown in industry activity related to COVID-19, lower export volumes and lower commodity prices and realized margins. Positively, demand for North American propane in Asia remains strong, and this should drive improvements at Petrogas in the second half of the year.

Overall, our Midstream business continues to deliver strong results, despite the economic challenges that the entire industry is facing. We continue to see healthy throughput volumes at our facilities, which we believe is a function of the quality and location of our assets, as well as AltaGas being partnered with high-quality clients, and operating an integrated value chain that links our customers to premium export markets in Asia.

We remain on track to hit our 50,000 barrels per day export target by year end with over 85 percent of RIPET's expected 2020 export volumes, either operating under tolling agreements or hedged. As such, we continue to expect strong and predictable results from RIPET through the second half of the year.

Volumes have been constructive through the first half of 2020, and we are optimistic that the recent momentum in crude and NGL pricing will help mitigate what could have been more pronounced upstream spending declines over the next 12 to 18 months.

In the second half of the year, we anticipate that processing volumes will improve towards the levels that we were expecting earlier in the year, which we have seen play out in recent weeks, with much of this production linked to our recent facility expansions, and the associated ramp up in customer throughput at these facilities. We have hedges in place for approximately 100 percent of our frac exposed NGL volumes at a blended rate of $29 per barrel

Our $900 million 2020 capital program remains unchanged with approximately 75 percent to 80 percent directed towards the Utility business. Roughly 80 percent of that utilities CAPEX is being targeted to accelerated replacement programs while maintenance spending is largely being calibrated to match depreciation. Most of our 2020 Midstream CAPEX spending has already been deployed on the Townsend and North Pine expansions, which are both now in service and contributing to stable operations and earnings.

We ended the second quarter with $6.8 billion in net debt, down from $7.2 billion at the end of 2019. Our self-funded 2020 capital plan remains unchanged, with the only item that could materially alter that spend profile being the Petrogas transaction, where we continue to work through the valuation process. As we have said in the past, although our funding plan is not dependent on any further asset sales, we will continue to look at non-core divestitures opportunistically as the market moves back to a more normal state, in an effort to continue to strengthen the balance sheet.

The largest remaining non-core assets in our portfolio includes our 10 percent interest in the Mountain Valley pipeline and our approximate 507-megawatt Blythe natural gas fired power generation asset in Southern California. Now, while the total cost estimates on the Mountain Valley pipeline have seen cost escalation in recent years, we remind investors that our capital commitment for our 10 percent stake has been capped at US$352 million, with no more cash to be deployed on our part, which makes our ownership stake a unique asset.

The project is currently 92 percent complete, only the Appalachian Trail crossings remaining, while two recent favourable Supreme Court rulings have significantly de-risked the project, leading to revise in service date of early 2021. As we have said in the past, we continue to maintain significant financial flexibility with AltaGas' excess liquidity expected to exceed $4 billion dollars at 2020 year end.

In summary, we are happy with how our Midstream and Utilities businesses have performed through the first half of the year, with only marginal impacts associated with the global pandemic. And, while the macro said is naturally opaque, and we continue to monitor COVID closely, we are pleased with the resilience and durability of the platform experienced today.

We also believe that similar high-level trends should be exhibited in the back half of the year, and as such, we are reiterating 2020 guidance and expect to land in the range of normalized EBITDA of $1.275 billion to $1.325 billion and normalized EPS of $1.20 to $1.30 per share.

Adam McKnight — Director of Investor Relations, AltaGas Ltd.

With that, we'd like to turn it over to the Operator for the Q&A session.

Q & A

Operator

Thank you. Ladies and gentlemen, we will now conduct the analyst question-and-answer session. If you would like to ask a question, press star, then the number one on your telephone keypad. If you would like to withdraw your question, press the pound key. There will be a brief pause while we compile the Q&A roster.

Our first question comes from Rob Hope with Scotiabank. Your line is open.

Robert Hope – Analyst, Scotiabank

Afternoon everyone or morning if you're on the West. Thanks for taking the questions. The first one's on RIPET. So, we saw a ship kind if slip into July, but your July volumes have been quite strong. As you look into August and September and I guess the balance of the year, are you targeting kind of that two to three a month to get to the 50,000 barrels a day for the rest of the year, and if so, kind of, what are your key constraints right now there?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Thank you, Rob, and thank you for your question. Good morning and afternoon to you as well. I think good morning. Look, we've experienced increasing Canadian demand and access to our unique capability and the team is doing an excellent job in debottlenecking so, you know, I'm very optimistic about where we're headed. But I'm going to let Randy go through and answer a little bit more detail about some of the actions we're taking to drive increased throughput and meet the demand of our customers. Randy?

Randy Toone — Executive Vice President and President, Midstream, AltaGas Ltd.

Thanks Randy. So, the eighth ship did go into Q3 and if that ship was loaded at the end of Q2, we would have been closer to that 50,000 barrel a day level. So, the goal is to do eight ships a quarter and with this ship going into Q3, you know, the goal would be to do nine ships in Q3. But we do have the supply, and now it's just optimizing logistics to make it work.

Robert Hope – Analyst, Scotiabank

All right, that's helpful. And then turning over to the utilities, how are you balancing your cost containment initiatives in a COVID world? And I guess, secondly there is, do you think you could get resolutions on cost recovery on some of these COVID costs by the end of the year?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Well Rob, I think that, I think as James had said, but particularly these costs were coming into our kind of off-peak periods and we think, most of this is behind us. So again, we've got a filing in August to update Maryland on the cost structures that we're in and some of the questions. So, I think, there hasn't been a formal way of proceeding to recover these costs, but we’ve had pretty clean orders on the deferral, and we’re working through the timing of the recovery mechanisms. But overall, not overly material, clearly as to where we are now.

On your second question in terms of how we, what I would say about the operationally effectiveness journey, if you will, that we have created, we've got a really creative team that’s focused on the continuous improvement and I think they've done an excellent job, but it does require the ability to identify new technologies and take cost out over time and we don’t—I don't estimate, that requires in terms of culture and focus to implement these new technologies and take cost out over time.

So, there's work to do, but Blue has pulled together a team that is coming up with so many creative and great ideas, so our discipline is there. Our creativity, our innovation commitment, and we are going to improve those costs, improve service and create value to our customers. So, I think that working with our customers the commissions I think that we're going to be able to meet our targets of general return into 2021.

Robert Hope – Analyst, Scotiabank

All right. I appreciate the colour. Thank you.

Operator

Our next question is from Jeremy Tonet with JP Morgan. Your line is open.

Joe Martoglio

Hi, this is Joe on for Jeremy. Wanted to start out with the ConocoPhillips Kelt acquisition and what that means for you guys. So, have you had any discussions with Conoco yet? And are you just thinking that increases volumes to your gas plants or allows for potential expansions longer term?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

I think, obviously, the transaction hasn't been closed and so we have not had a great deal of detailed discussions, but clearly ConocoPhillips has adjoining acreage in the region. We have had discussions with them and we're excited about them coming in. I think, as I said in my prepared remarks, Joe, and thank you for the question, that it really validates the economics within our Northeast BC position.

And yes, we would think that we've got firm commitments that we had previously had from Kelt and Conoco will step into those shoes. So, we're excited about that. It's difficult to predict how quickly volumes will come on with the environment, increased volumes that is, but over time we're very excited about it.

Joe Martoglio

Thanks, that's helpful. And then maybe, could you also just update us on if you've had any recent discussions on selling the MVP stake and the ACP cancellation? If you think that could potentially garner any interest there either, for someone who acquires a stake or getting additional commitment?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Yes, good question. I mean, look I've consistently said that we believe strongly in the Mountain Valley Pipeline project, that there is an absolute essential need for that project. James mentioned in his prepared remarks, that we're pleased with the Supreme Court's ruling regarding the Appalachian Trail authorization and we expect the issuance of the revised biological opinion shortly.

So again, and assuming the timing resolution of those outstanding permits, I think it's targeted to be full in service during 2021, so from our perspective, the asset is clearly being de-risked. We defined it as non-core, and we will work through the year to see if, at the end of the day if we could get full value for that. I mean, I've said previously that we positioned our Company to, if we are going to monetize our non-core assets, we are not going to be taking below market value for those assets.

So, we're well positioned to do that. But clearly, as you point out, the recent order and the importance of MVP to the marketplace has certainly increased, and just underscores the value, quite frankly, of pipelines that are in the ground. As we look at it that's, I think that clearly demonstrates even if you think about it the value of our export facilities, it's very hard to replicate those assets and we feel the same way with the completion of MVP.

Joe Martoglio

Thank you. That's good to hear.

Operator

Our next question comes from Robert Catellier with CIBC Capital Markets. Your line is open.

Robert Catellier – Analyst, CIBC Capital Markets

Primarily follow up questions here, but I think I heard you say, effectively, you don't expect any significant impact on your earnings at the utilities from recurring costs related to COVID. But then there's the question of the recovery period and so the impact on cash flow. Can you just give a comment on what impact you think it might have on cash flow or credit metrics? It sounds like it wasn't material from your previous comments.

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Now since we get out of the first quarter, right, which is our seasonally high quarter from a revenue perspective and we're in our off-peak season. But I'll let James talk about that, but relatively minor, but I think he laid out the specific numbers. Do you want to go over those quickly?

James Harbilas — Executive Vice President and Chief Financial Officer, AltaGas Ltd.

Yes, Robert’s it’s James here. I mean with respect to COVID impact, I guess it's important for us to break it out into two categories. Right? I mean, we did touch on the fact that there was certain regulatory orders that suspended the charging of late fees and service charges and that was about $7 million to $8 million of revenue impact and we're tracking those and we'll bring those forward for consideration by the regulators in the future. And then we had obviously some bad debts and other direct costs in operations that totaled about $5 million that we've put into a regulatory asset account that we're going to bring forward for future collection in consideration from the regulators.

In terms of your broader question on the impact to AR or a slowdown in collections. For us, we've seen a working capital unwind in Q1 and Q2. We haven't seen a considerable deterioration in aging at this point, although that's something that we'll continue to monitor. So, we haven't seen other than the usual build of some working capital to build storage at our utilities, we haven't seen a considerable deterioration in the aging of AR at this point.

Robert Catellier – Analyst, CIBC Capital Markets

Okay, you gave some pretty good colour on your hedging position. Now, I'm wondering if you could talk a little bit more about what happens beyond 2020? I don't know if you can address how much of the capacity will be tolling next year, how much you've hedged or how much you might have merchant risk?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Sure. Let me go ahead and address it as best I can here. So, right now, we have about 30 percent of our 2021 volumes hedged through our tolling agreements. We've had a recent improvement in the forward curve around 2021, so it's trading north of $8.80 a barrel. That's the FEI spread, and so we've begun to layer in hedges, for our expected 2021 merchant volumes and we would expect to be 60 percent to 80 percent hedged as we enter into 2021.

Now, with respect to your broader question about tolling and the de-risking of the asset over the long term, it's a major driver for us. We've experienced, as I said, increased demand to access this unique capability, and I feel good about it because we're consistently being approached by launch aggregators who want access to this unique capability. So, we're not prepared to go beyond where we are today, but in terms of that guidance, but I think you can tell by my tone that we're optimistic that we'll continue to move toward a tolling arrangement over the next year.

Robert Catellier – Analyst, CIBC Capital Markets

Yes, and maybe just a little bit more colour on the—beyond the tolling, just the structure of the market that spreads have come in a bit. So, any update you can give us on the fundamentals and your expectations as to how they might have been impacted year-to-date and how they might improve going into 2021 for the FEI spread?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Sure. We've, you know, we continue to see some improvement in the spreads and in the volumes in the basin are constructive, begin to be constructive here in the second half, and so we're expecting processing volume to improve. We're seeing, strong demand at RIPET we're seeing volumes come back really at the end of the day and I've talked about this a great deal but the benefits of our structural shipping advantage and so, shipping cost as margins contract go down. Right? So overall margins can necessarily improve.

And so, we've got some shipping hedges as well, but overall, I think you've got the best market in Canada for propane. You're going to continue to see an overwhelming of the local market as a lot of the demand-based projects are pushed out. And so, we're, in the long run, we continue, to be bullish in expanding and de-risking these volumes and we continue to see robust and long-term fundamentals of supply and demand imbalance for North America. So, we're going continue to lock in the spreads, but we see that continuing in the long-term.

Robert Catellier – Analyst, CIBC Capital Markets

Okay, that's very helpful. Thank you.

Operator

Next question is from Patrick Kenny with the National Bank Financial. Your line is open.

Patrick Kenny – Analyst, National Bank Financial

Yes, good morning guys. So clearly, the energy patches, entering a phase of consolidation here, you guys appear to be in a unique situation to offer customers or new customers like Conoco some new market access opportunities. So just curious, how that might play into discussions surrounding potential tuck-in opportunities for additional processing capacity, and, I guess boosting your proprietary access to propane closer to RIPET's full capacity, appreciating that balance sheet strength is priority, but again, to the extent that there is a unique window of opportunity here to consolidate, just how you're thinking about potential upstream infrastructure opportunities.

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Yes, you know, that's a good question. We've continued to put a fundamental focus on improving our leverage metrics, but we see opportunities to invest in both of our businesses, and we think this is an opportunistic time to capture more volumes. We're in an excellent position in our Midstream business. We're unique in the fact that we can offer our customers access to both domestic and international markets, in the growing demand in the petchems in Asia.

So, from that standpoint, in my experience, connecting producers to markets and improving their net back is a key driver in increasing volumes to your facilities, obviously. And so, we can offer our customers—at this point we have significant low-cost expansion capacity at all of our facilities. And so, we’ve certainly worked to help the producers in a variety of different ways to have them work to expand their volume.

So, again, we're focusing right now on harvesting those cash flows in through the year, but we can very well be opportunistic, and we will be, as we have further discussions and fill up the existing capacity and really add a lot of value to our customers at the end of the day. So, we'll be looking for those opportunities as we go forward.

Patrick Kenny – Analyst, National Bank Financial

And I guess Randy, at a high level, from a business mix perspective, as you look to grow your Midstream cash flows, especially once you close the Petrogas option, just in the context of how the market is currently valuing Midstream, versus Utility assets, is there any internal limits on what percentage of total EBITDA comes from Midstream? Or said differently, is there an appetite to shift your waiting more towards utilities, just given the current macro backdrop?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Yes, I think that, clearly with our capital spending this year, into the next year with an 8 percent to 10 percent rate base growth, you're going to continue to see our Utility EBITDA and rate-based growth over the next five plus years. So, Utility is going to grow as a percentage of our mix, but at the same time, we're expecting similar type of profile growth out of our Midstream company. And so, we take a position of a capital disciplined approach and earning a return in excess of our cost of capital and both businesses have excellent opportunities, and it's why we've focused our efforts on improving our balance sheet, so that we can profitably pursue these opportunities.

So, I think you'll see us continue to become more and more of a utility mix over the next year or two. But we also continue to see opportunities for growth at the Midstream. So, those percentages, I think will tilt a bit more to the Utility post—again, after Petrogas will change the percentage a bit more. From that forward point, and I think you'll continue to see Utility be a larger percentage.

When you talk about business mix, look we've—I want to make a comment that we've done a lot of work to focus on the businesses where we see the greatest opportunity now, and we've got a unique investment, as I've said position, combining our Midstream Utility businesses. So, I continue to believe that's the right strategy. And, as the quality and diversification assets provide us that opportunity to deliver that sustainable growth, so well, the mix will fluctuate. We have opportunities prospectively to keep the Utility to be a significantly large portion of that as we grow the Midstream too.

Patrick Kenny – Analyst, National Bank Financial

Okay, that's great. I'll leave it there. Thanks, Randy.

Operator

Our next question is from Robert Kwan with RBC Capital Markets. Your line is open.

Robert Kwan – Analyst, RBC Capital Markets

Hey, good morning. If I can just maybe continue on that topic, and can I get your thoughts on, the Dominion transaction and if you're able to provide some thoughts to compare and contrast their decision with your situation?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Yes, well, look, I mean, if Dominion made a strategic decision to focus in toward its electric side of its business and has significant capital requirements in that business. So, there's—clearly, I don't think we have a $5 billion pipeline that we're writing off, so we're not exactly the same there. But, I understand your point, Robert, and I think that, when we look at—as a management team, we're always looking at ways to surface that, the full value of our assets, and that's potentially, one day could be separating those two platforms similar to what Dominion did.

But, we also need to stack that up against the fact that we are still in the early days of executing our strategy that we laid out last year and we want to continue to focus at the task at hand and so we see a significant opportunity in both businesses. And so, I think that we're a bit—that contrast our view, I think maybe from what Dominion saw on its pipelines in terms of the opportunities for expansion.

Robert Kwan – Analyst, RBC Capital Markets

Does that—when you think about your Midstream business, then does that cause you to maybe think differently? With respect to how you pursue that business in the sense of, if you're thinking about the potential for a full break, does that change your appetite to take on partnerships or a partial sell down as they make the standalone be less attractive given the medium to long-term?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Sure look, I think, now is our time to execute and we've done the work and we believe that's the best way to maintain that. And we're always looking at opportunities to—I said this before on the calls, if there is an opportunity to partner or do JVs that one plus one equals three, we're absolutely going to do that, and we will not be constrained. What we are focused on is growing profitable, both our profitable business in a capital disciplined manner and consistently growing our business platform to continue grow earnings and the resiliency of our model.

I think we're doing a great job, and no, I don't think it affects our decision making, but we take all those factors into account as we make—management sits down and looks at every lever that we have available to us Robert.

Robert Kwan – Analyst, RBC Capital Markets

And may I just finish with a question on the upcoming elections, and specifically when the Tax Cuts and Jobs Act was put into place, I think the guidance was that it would be about a 5 percent reduction in EBITDA and FFO and the negative impact on Utilities from the lower tax rates. Just wondering, do you—have you taken a look at what actually got realized as part of that? And do you have some thoughts as to, if tax rates were to go up in the future, what that would mean kind of for your business as it stands now and the ability to actually recover some of that in a timely fashion?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Yes, thank you for that question. I would—my perspective is that when tax law and rates were reduced from a utility perspective, we had excess deferred taxes on the balance sheet, meaning that future liabilities that would not be at the same tax rate. So, the utilities began to flow those back and those are over periods of time and in different jurisdictions.

I would expect that from a utility perspective, if tax rates were increased, then we would adjust those deferred taxes, or I guess we're in a position, and maybe that's somewhat enviable, then maybe other businesses where we would actually have excess deferred taxes that could absorb a federal tax increase.

Robert Kwan – Analyst, RBC Capital Markets

Okay, and just in terms of that 5 percent guidance that originally was put out, is that fairly similar to what actually got realized in the business, if on FFO?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Sure, I am going to have to defer that one to James, Robert, because I don't have those numbers, if James has them in front of him or not.

James Harbilas — Executive Vice President and Chief Financial Officer, AltaGas Ltd.

Yes, no Robert, I think that's very much in the range of the impact obviously. It was a bit different in terms of how certain regulators treated the refund of that and the timing of it to some customers. The most aggressive refund was in Virginia, and we reflected that impact in 2019, but that's very much in the range of the impact that occurred on FFO to that.

Robert Kwan – Analyst, RBC Capital Markets

That's great, thank you very much.

Operator

Our next question is from Julien Dumoulin-Smith with Bank of America. Your line is open.

Julien Dumoulin-Smith – Analyst, Bank of America Merrill Lynch

Good afternoon, good morning. Thanks everyone for the time. So, just a follow-up on some of these questions here, you talk about focusing on the Utility, want to focus on Utility CAPEX. Obviously, you've got a number of programs underway in terms of accelerated replacement programs. Can you talk about the DC program? What your ability is to shift capital around with which it isn't fully approved at your ask or otherwise? You know what I'm saying? Like as in the consistency and planning around to ensure sort of a smooth trajectory on capital?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Yes, great question Julien and we absolutely manage that as we move capital around and look at specific projects. It's sort of a project-based approach, but I'm going to let Blue go ahead and answer that question for you. Blue?

Blue Jenkins — Executive Vice President and President at Utilities and Washington Gas, AltaGas Ltd.

Sure, yes thanks Randy. Julien, it's a great question. As you know those are regulatory processes and proceedings. So, we are in the process of working through what is called DC Project Pipes 2. And so, to your point, what we look for is an ongoing project mix that maximizes the positive impact of the system for safety, reliability, but also allows us to smooth the cash flow or the CAPEX if you will, spend, which then follows through on the cash flow.

We do that across all of our jurisdictions. So, we're very thoughtful about that. We're in constant conversations with the oversight bodies on how that works and what's next there. We do look to maximize all of those programs as we move forward. So, does that answer your question?

Julien Dumoulin-Smith – Analyst, Bank of America Merrill Lynch

Yes, all right. You've got contingencies in mind, maybe that's the critical.

Blue Jenkins — Executive Vice President and President at Utilities and Washington Gas, AltaGas Ltd.

Correct.

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

We can move dollars to other jurisdictions and cruise around on lines, so that we can still smooth out and meet our plans to the best extent possible on our accelerated pipeline replacement program. It's a big focus area. So, yes and we had some consistency in Virginia and Maryland that gave us flexibility, Julien.

Julien Dumoulin-Smith – Analyst, Bank of America Merrill Lynch

Excellent, all right. If I can turn back to just quickly to the Midstream side with RIPET, can you talk a little bit more about the depth of the market? I mean, obviously things have turned around here, shall we say? How do you think about the ability to hedge forward, especially on a tolling basis? I heard your comments earlier on '21 to the last questioner, but can you elaborate a little bit more on the depth of multi-year contracting? And then just also the ability to sustain over time that 60 percent to 80 percent. How high can you get as long as the tender?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Yes, you know what I mean, clearly when it comes to liquidity and hedging, we can get there over the next two months, as we do, but you're talking longer term. And when we go to de-risk these assets, longer term, we're really looking at our tolling strategy, and we, as we do that right, and I've said that we're experiencing demand for accessing this capability, so I feel pretty good. And those are longer term, right? Those go into the 10-year plus agreements and the team has done an excellent job to date.

And why am I bullish that we're going to do this over the long-term and de-risk these assets including Ferndale? That's because we're—as we have continued discussions with large aggregators and others in the basin, that gives us the confidence that we're going to toll those. Now, we could do multi-year hedges as well and we could look at that, but I think our real driver is that we are a Company and a Midstream company that connects producers to markets, and we are not in the commodity business, and so, we'll continue to de-risk that and let our customers be able to realize those margins in Asia. If that answers your question.

Julien Dumoulin-Smith – Analyst, Bank of America Merrill Lynch

All right, yes just quick clarification, because you said it this way, over the long term, what time period do you think you get to a point in which you're hedged at that 60 percent to 80 percent on the tolling basis without putting words in your mouth?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

No, I got you. No, I think—so we're about 30 percent right now. I'd be disappointed if we're not there by the end of next year. I mean, on the lower end of that, right as we go through 2021 if we don't get to that part then we'll double that, that's going to be our objective. But again, we'll see how the market works, but that's where we're going to try to target as we go through 2021.

Julien Dumoulin-Smith – Analyst, Bank of America Merrill Lynch

Excellent, thanks for the added clarity.

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Sure.

Operator

Our next question is from Linda Ezergailis with TD Securities. Your line is open.

Linda Ezergailis – Analyst, TD Securities

Thank you, appreciate the comprehensive update today and presentation. Looking at Slide 35, appreciate the sources and uses of cash and that you're at a self-funded model. But, I'm wondering what might cause AltaGas to either be opportunistic and maybe accelerate some deleveraging or prefunding of future opportunities, or conversely, might cause you to shift your plans for sources for example, if asset sales don't materialize? And, can you discuss kind of what other leavers you might consider pulling, including potentially an ATM or a discrete equity issuance and what factors would be in place for you to consider that seriously?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Sure. I can let James get a bit more specific into your question Linda, and thank you for the questions. From our perspective, we have a pretty strong track record of executing on our non-core asset sales, so we're very confident that we'll be able to do that. But clearly, this is not the best environment to be moving that forward, so we've continued to deleverage, and we feel confident that we'll be there.

We will not miss if we have opportunities for financially rewarding capital projects that we can have access to capital to do that going forward. But I think clearly our plan is pretty conservative. But James, why don’t you, I'll let you go ahead.

James Harbilas — Executive Vice President and Chief Financial Officer, AltaGas Ltd.

Yes. So, it really comes down to the current macro environment we're in and with the timing of moving forward with some of these asset monetizations as some of these continue to de-risk. So, if we like some of the values that we're seeing for these assets because they've been de-risked, then that's something that we could move ahead with in the latter part of this year and potentially raise some funding for next year's CAPEX program.

But obviously, the other thing that we're tracking closely is just this current year CAPEX program. At the end of Q2, we're tracking a bit behind our spend in terms of what our expectations were. So that could take some money and move that into 2021 as well potentially, especially given the fact that our Midstream CAPEX program is a capital light approach that we're using right now.

Linda Ezergailis – Analyst, TD Securities

Okay, and what might cause you to shift your funding plans and revisit it in any situation, if you see more opportunities potentially or other factors?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Yes, I would tell you more strategically Linda, there would have to be some other opportunities that we would see out there that would require us to access capital beyond what we have in our plan, inclusive of Petrogas obviously. It would have to be something along those lines, but right now we have a pretty focused plan, as I said in my comments, we're executing very well, the team has in terms of our EBITDA and our guidance.

Look, we're focused, laser focused on achieving net debt to EBITDA that's less than 5x and getting our ratings notched, one or two above the BBB- and that's a priority. So, that's where our focus is, but certainly if there are opportunities that come up with a new and better that creates shareholder value, we could revisit that.

Linda Ezergailis – Analyst, TD Securities

Okay, and maybe as a follow up to the coming presidential election, I guess beyond potential changes in tax rates, I'm wondering if there are any other policy changes potentially, as it relates to perhaps renewable energy or other infrastructure build, that might open up opportunities for your franchise in the U.S.?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Yes, I think that really, it's hard to predict elections clearly, especially in the times that we're in today. But we try to position our Company to be successful with whomever might be in office, because oftentimes it’s really about economics and what makes sense for customers at the end of the day. So, renewables are clearly a big push and I think they'll continue to be because the economics supports them.

And we'll look for funding on infrastructure to look at new technologies around, as I've said in my prepared remarks, hydrogen and other fuels that may be able to blend into our system that can reduce and decarbonize, and that's why I'm very excited, but we're early in the process and what we're doing working with the Washington DC Commission as to further enhance, really our ability to innovate and deliver clean energy solutions.

So, I think as the election plays out, we'd like to position our Company to be successful and confident that we will either way. But those might be some ideas about the clean energy and incenting infrastructure, and we think we'd be well positioned in the U.S. And really we have a long history as I mentioned around developing innovative clean energy solutions.

Linda Ezergailis – Analyst, TD Securities

Thank you.

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Sure.

Operator

Before we move onto our last question, I would like to remind participants that if you have any further questions, simply press star, and then one on your telephone keypad.

Your next question comes from Andrew Kuske with Credit Suisse. Your line is open.

Andrew Kuske – Analyst, Credit Suisse

Thanks, just on the frac spreads that you realized, and I'm aware of your hedging program as you disclosed it, so, it looks like ballpark on the unhedged portion of the frac, you actually outperformed the average spot price through the quarter. Can you maybe give a little bit of detail as to what went on there in the quarter on hedge portion?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

James, do you want to address that or Randy?

James Harbilas — Executive Vice President and Chief Financial Officer, AltaGas Ltd.

Sorry Andrew, can you repeat the question?

Andrew Kuske – Analyst, Credit Suisse

Yes, if I look at your frac spreads what you realized, the $16.61 and then I deconstruct your hedging program a little bit, which is about half the barrels that you had in the quarter, it seems like you've outperformed versus the average spot price on your unhedged portion? If you could maybe just give a bit of colour as to what happened there? Is that just the value of having your physical footprint positioning? Any other colour would be great.

James Harbilas — Executive Vice President and Chief Financial Officer, AltaGas Ltd.

Yes, well I think it's really the fact that we were hedged at a much higher rate than 50 percent. We've been hedged at north of 90 percent for most of the year, so we were able to realize the higher frac spread relative to spot because of our active hedging program at the end of last year and the beginning of this year. That's really what it came down to.

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

You know, but to your broader question, and that's spot on, but Randy and his team have always leveraged the physical assets to optimize value for both our customers as well as ourselves, so it doesn't surprise me that they get a little bit better on some of that spot.

Andrew Kuske – Analyst, Credit Suisse

Okay, that's great. And then one maybe follow-up and little bit different then just on the balance sheet. And Randy, you mentioned about all the work you've done on the balance sheet. I guess, how do you think about your metrics, where you want to land them, and this is really at the WGL level, and also the top of the house? And then the positive benefit of let's just say the regime changes and the U.S. tax regime, and we see tax rates go up again? How does that play into your thought process?

Randy Crawford — President and Chief Executive Officer, AltaGas Ltd.

Yes, I think that, with the Utility, they tend to want to be financed more from a say, 55 percent equity thickness, and the rest debt. From our leverage from a corporate perspective, and I just mentioned it just a little bit earlier in a question that might have been from Linda, but I was talking about our target of a net debt to EBITDA of less than 5x and a notch or two above BBB-.

So, that continues to be a priority from a corporate perspective and we think with our business mix that gives us—positions us quite well, both from our ability to fund growth, but also a strong balance sheet with dry powder. And so, I don't think that the tax rates or changes would impact how we want to finance the business. James, did you want to comment on that any more?

James Harbilas — Executive Vice President and Chief Financial Officer, AltaGas Ltd.

No, I think you covered the salient points there Randy. I mean, we do have additional levers to pull that we've highlighted a few times on this call with respect to additional asset monetizations and we continue to invest in the Utility CAPEX program with heavily weighted to ARP, so that gives us immediate recovery and reduces regulatory lag. So, that's another way for us to continue to move those leverage metrics down.

Especially with the Midstream business being capital light and having the ability to grow into some of our existing investments that we've made in prior years through increased volumes, which will in turn, drive increased EBITDA.

Andrew Kuske – Analyst, Credit Suisse

Okay, that's great. Thank you.

Operator

This concludes the Q&A portion of today's call. I will now turn the call back over to Mr. McKnight.

Adam McKnight — Director of Investor Relations, AltaGas Ltd.

Thanks again, Chris and thank you everyone once again for joining our call today and for your interest in AltaGas. Just as a reminder, the Investor Relations team will be available after the call if you have any follow up questions. And that concludes our call this morning. I hope everyone enjoys the rest of their day. And you may now disconnect your phone lines.