UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 2

Issue 1.1 - What are the implications associated with a revenue cap, a price cap and other alternative multi-year incentive ratemaking frameworks?

Question:

Union cites the Board's NGF Report, "A properly designed plan will ensure downward pressure on rates by encouraging new levels of efficiency in Ontario's gas utilities – to the benefit of customers and shareholders". Please identify, specifically, what new levels of efficiency Union plans to implement and how Union will ensure a downward pressure on rates during its IR plan period under its proposed plan.

Response:

Union has no specific initiatives planned at this time that would provide the productivity improvements. Union will pursue as much productivity improvement as possible. Union's efforts to date have been focused on getting the incentive regulation framework established rather than on implementation. Under Union's incentive regulation proposal, customers benefit through the annual adjustment mechanism and through rebasing. Customers benefit through the annual adjustment mechanism as a result of rates increasing by approximately inflation and less than they would otherwise under cost of service.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 2

Issue 1.1 - What are the implications associated with a revenue cap, a price cap and other alternative multi-year incentive ratemaking frameworks?

Question:

Please explain, in detail, why Union does not support an earnings sharing mechanism as a part of its price cap plan. Please provide evidence as to how an earnings sharing mechanism has, in the past, inhibited Union from implementing productivity initiatives that would benefit Union's shareholders and ratepayers.

Response:

Please see interrogatory response provided at Exhibit C1.15.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 5

Issue 1.1 - What are the implications associated with a revenue cap, a price cap and other alternative multi-year incentive ratemaking frameworks?

Question:

Union's evidence states that, "The benefit of productivity improvements, both cost efficiency gains and growth, should ultimately be shared between customers and the utility." Please explain, how, under Union's proposal productivity improvements would be shared with its customers during the plan.

Response:

Please refer to interrogatory response provided at Exhibit C1.4.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 12

Issue 1.1 - What are the implications associated with a revenue cap, a price cap and other alternative multi-year incentive ratemaking frameworks?

Question:

Please explain why it would be fair to ratepayers to eliminate the three transmission related accounts. Please provide a schedule which sets out for each year since the accounts were established the total amounts in each account. Also, please provide the amounts cleared to ratepayers and shareholders in each of those years.

Response:

As indicated in Union's interrogatory response provided at Exhibit C1.19, Union is proposing to eliminate the Transportation & Exchange Services Deferred Account (179-69), Other S&T Services Deferral Account (179-73) and Other Direct Purchase Services Deferral Account (174-74) beginning January 1, 2008, by adjusting base rates applicable to in-franchise customers to include 100% of the 2007 forecast margin approved by the Board in the EB-2005-0520 proceeding.

Currently, 90% or $0.768 million of the 2007 approved forecast of Other S&T Services margin and Other Direct Purchase Services margin is included in in-franchise delivery rates. For the Transportation & Exchange Services margin, 90% of the 2007 approved forecast amounts to $2.325 million, of which $0.222 million is included in in-franchise rates. The remainder ($2.103 million) is credited to ex-franchise customers through a monthly credit on customer's bills.

As part of eliminating the Transportation & Exchange Services Deferral Account (179-69), Union will adjust the base rates applicable to in-franchise customers to include 100% ($2.583 million) of the 2007 forecast approved by the Board.

In light of Union's proposal to eliminate the Transportation & Exchange Services Deferral Account, Union no longer believes that crediting a portion of Transportation & Exchange Services margin to ex-franchise customers is appropriate because:

1. Ex-franchise transmission customers have the ability to market their own capacity to mitigate the costs associated with contracting for firm capacity on Union's system; and

2. Continuing the credit as it is today will result in some ex-franchise customers receiving the credit while others will not.

Please see interrogatory response provided at Exhibit C1.19 for additional information.

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: What are the implications associated with a revenue cap, a price cap and other alternative multi-year incentive ratemaking frameworks?

Issue 1.1 - B/T1/p. 19

Question:

Under what conditions would Union support a revenue cap mechanism for its IR plan.

Response:

In Union's view, a price cap plan is superior to a revenue cap plan with respect to a number of objectives such as alignment, comprehensiveness, rate predictability & stability, and simplicity. In Union's view, a revenue cap could not be designed that would address all of the deficiencies of a revenue cap plan relative to a price cap plan.

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1

Issue 1.1 - What are the implications associated with a revenue cap, a price cap and other alternative multi-year incentive ratemaking frameworks?

Question:

Please provide copies of all documents presented to Union's senior management, Board of Directors and its shareholders in seeking approval of Union's proposed price cap plan.

Response:

The attached presentation was provided to senior management in Spectra Energy.

Approval from Union's senior management was provided as a result of a review of Union's evidence, specifically the summary of Union's price cap plan that appears on the table on p. 8 of Exhibit B, Tab 1 of Union's evidence. Further, the financial forecast provided in the interrogatory response provided at Exhibit C23.52 was also presented to and approved by Union's senior management.

Question: August 20, 2007
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Docket: EB-2007-0606 / EB-2007-0615

uniongas
A Spectra Energy Company

Incentive Regulation Strategy and Process

June 4, 2007

Houston, Texas

Incentive Regulation

- Completion of multi-year regulatory strategy
- Supporting a price cap form of incentive regulation
- Regulatory process underway
- Effective January 1, 2008

Why a Price Cap Framework?

- Aligns customer and shareholder interests (price and service quality)
- Most prevalent form of incentive regulation
- Multi-year rate certainty
- OEB Policy report
- Simplest to administer
- Superior earnings with superior performance
- US pipeline experience

Price Cap Components

- **Annual formula applied prospectively**
- **Allows for:**
  - Inflation factor
  - Historical productivity (including input cost differences, declining use per customer, stretch factor)
  - Continued pass-through of certain costs
  - Material non-routine adjustments outside of management's control

Other Price Cap Framework Components

- 3-5 year term
- No earnings sharing
- Reporting requirements
- Rebasing requirements
- Consistent with Natural Gas Forum Policy Report (March, 2005)

Union's Request

- **Draft Price Cap Evidence:**
  - ❑ Net annual escalator to approximate inflation
  - ❑ 5 year term
  - ❑ No earnings sharing
  - ❑ One-time adjustment for symmetrical weather risk
  - ❑ Continued pass-through of certain costs (e.g. commodity, upstream transportation, DSM)
  - ❑ Allowance for material non-routine adjustments (e.g. LPP litigation, permit fees, tax changes, accounting changes, generic ROE)
  - ❑ Pricing flexibility
  - ❑ Reporting requirements
  - ❑ Rebasing requirements

Net Annual Escalator

- **From PEG Study (draft only)**

GDP IPI	1.77%
IPD	-0.33
Historical productivity	0.26
Declining use per customer	-0.73
Stretch factor	0.30
Total (X-factor)	-0.50
Net escalator	2.27%
Service cap – small volume	1.90/2.50
Service cap – large volume	2.79

Incentive Regulation Process - To Date, and Expected

- OEB/stakeholder consultations and discussion papers Oct 2006 – April 2007
- Draft external productivity study (PEG) – Mar 30
- Union rate application - May 10
- Final external productivity study (PEG) – June 1 (or later)
- Union evidence – June 22 (or later)

Incentive Regulation Process – To Date, and Expected

- Enbridge evidence - July
- Interrogatories and responses - August
- Intervenor evidence – September
- Settlement conference – October
- Hearing – November
- Argument – December
- Decision – March
- Rate order – April 2008 (retroactive)

Key Risks

- **Process:**
  - ❑ Enbridge
  - ❑ Customer and market reaction to retroactivity
- **Financial**
  - ❑ History / Productivity factor (X)
  - ❑ Acceleration of key business impacts (e.g. input costs, declining use)
  - ❑ Cost management
  - ❑ Earnings sharing
  - ❑ Re-basing impacts

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 24

Issue 3.1 - How should the X factor be determined?

Question:

Union's evidence states that the rate indexing research that supported PEG's proposed price cap design and overall IR recommendations for Union and Enbridge "appear to be strong conceptually and generally consistent with the approach in other jurisdictions." What empirical analysis did Union undertake in assessing PEG's data? Please provide copies of any studies or reports Union produced in response to the PEG study.

Response:

Union did not undertake any empirical analysis to confirm the numerical results. There were no studies or reports produced in response to the PEG Study. Union's conclusions were based on a review of the approach described in the PEG Study and information conveyed by PEG at the stakeholder meetings. While Union did not do any empirical analysis, Union does believe the results are directionally correct.

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 36

Issue 3.1 - How should the X factor be determined?

Question:

Union has proposed its own method of calculating the X factor attributable to the general service class which differs from the approach proposed by PEG. Please provide examples of this method being applied in the context of other IR plans, if any. What evidence can Union provide to support its proposal that a 2.24 PCI is appropriate?

Response:

It is Union's understanding that it is unusual for there to be different PCIs for different service groups (i.e. that a single PCI not be applied to all rate classes) and that the two service group approach proposed by PEG resulted from comments by stakeholders at the consultation meetings initiated by Board Staff last fall. Some stakeholders were suggesting that the affects of declining use per customer should be reflected in the PCI for those rate classes where it was most pronounced.

The 2.24 % PCI proposed by Union is based on the TFP data produced by PEG, excluding a stretch factor, and with a simpler, more intuitive way to determine the AU factor by service group.

Under Union's proposal the PCI for the general service rate classes would only be 2.24% if the rate of inflation (as measured by the GDP-IPI FDD) during the incentive regulation period was equal to 1.86%. Union's actual proposal is that PCI = GDP-IPI FDD – X, where X= -0.38% for the general service rate classes, and X = +0.74% for all other rate classes.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 37

Issue 3.1 - How should the X factor be determined?

Question:

Is the differential between 2.24 and 1.12 PCs for general service and all other rate classes entirely related to historical declines in average use? If not, please explain what the differential is attributable to.

Response:

Yes. Please see Table 3 in Union's evidence, Exhibit B, Tab 1, Page 37.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 32

Issue 3.2 - What are the appropriate components of an X factor?

Question:

Union has rejected the incorporation of a stretch factor in the determination of its proposed X-factor. Union's evidence is that volatile gas prices as one reason for decreasing throughput and revenue and therefore the need for a stretch factor. If the OPA undertakes significant fuel switching initiatives over the next few years has Union assessed the potential impact on its throughput? If these initiatives materialize how will they be treated during the IR plan? Would Union support a Z-factor to deal with the potential impact of fuel-switching? If not, why not?

Response:

Fuel switching and other OPA programs have both potential benefits and risks to Union.

There will be no adjustment during the IR plan to reflect impacts of fuel switching initiatives. Union would not support a Z factor to deal with the potential impact of fuel-switching. There should be no Z factors to deal with either increases or decreases in revenue driven by a changing marketplace. As noted in Union's plan objectives Exhibit b, Tab 1, Page 6, the ratemaking framework should allow the utility to manage its business in total, including growth opportunities, and not focus on individual aspects that can create distorted incentives.

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 24

Issue 4.2 - How should the impact of changes in average use be calculated?

Question:

Please provide evidence which supports the determination of the -.72 average use factor adopted by Union. What analysis has Union done to determine its applicability to Union?

Response:

Please see interrogatory response provided at Exhibit C32.11 a).

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 12

Issue 5.1 - What are the Y factors that should be included in the IR plan?

Question:

Union is proposing that the base rates be adjusted to reflect the impact of moving to the 20-year declining trend weather forecasting methodology. Please explain how the $7 million amount was calculated.

Response:

Please see interrogatory response provided at Exhibit C3/C16/C33.3.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 39

Issue 6.1 - What are the criteria for establishing Z factors that should be included in the IR plan?

Question:

Union is not proposing any new deferral accounts other than those established in the base year. Please provide a complete list of all existing deferral accounts and the approved method of accounting for each account.

Response:

Please see interrogatory response provided at Exhibit C1.10.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 40

Issue 6.1 - What are the criteria for establishing Z factors that should be included in the IR plan?

Question:

Union has referred to Late Payment Penalty costs as a possible example of inclusion as a Z-factor. Please identify, to the extent possible, the expected LPP costs to be included in such an account.

Response:
Union expects the Late Payment Penalty costs could include:

- In the event that Union was able to affect a favourable settlement or in the event of a final adverse order awarding damages on other costs, Union would put these amounts in the deferral account. Union is not in a position to comment on the likely amount of any such settlement or award at this time. However, it should be noted that (1) The plaintiff has claimed damages of $170 million plus interest in their initial statement of claim; and (2) a similar but factually different class action was settled for $22 million; and (3) during the period in question, Union billed not more than $77 million in late payment penalty charges (2006 annual report note 21).

- Any legal and other costs of defending the claim. The size of this component will be dependent on whether the matter is settled or proceeds to trial, and whether the matter is appealed or not.

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 41

Issue 6.1 - What are the criteria for establishing Z factors that should be included in the IR plan?

Question:

Union has listed Permit Fees as a potential Z-factor category. Please estimate the potential annual costs associated with permit fees.

Response:

Union is unable to determine with certainty what costs will be incurred associated with permit fees as it will depend on the number of municipalities that proceed to implement a permit fee and the amount of any such fee. As Union is required to access its pipelines tens of thousands of times annually for maintenance, repair or improvement work, even a modest fee may have a significant impact. Union also expects permit fee costs to increase annually as the charging of fees becomes more prevalent among municipalities.

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1

Issue 6.1 - What are the criteria for establishing Z factors that should be included in the IR plan?

Question:

What is the expected ongoing cost of implementing GDAR for Union over and above what is in Union's base rates? How will those <original truncated>

Response:

In the RP-2003-0063 proceeding, the Board approved Union's proposal to recover in rates the costs it had originally estimated would be required to comply with GDAR ($4.78 million in capital and $1.3 million in operating and maintenance expenses). The Board also approved the introduction of a GDAR Costs deferral account to track any variances from these amounts. As it became clear the scope of GDAR was much broader than Union's initial interpretation, in the EB-2005-0520 proceeding Union forecasted it would require an incremental $18.2 million of capital to implement GDAR plus an additional $500,000 in annual operating expenses. Of this additional spending, $8.7 million in capital and $460,000 in O&M was specific to the functionality required to implement a bill-ready distributor consolidated billing service as mandated by GDAR. At the time of the EB-2005-0520 proceeding, the bill-ready service was not anticipated to be in-service until January 1, 2008. Thus, Union sought pre-approval to change rates effective January 1, 2008 to incorporate the incremental bill-ready capital and O&M costs. As part of the EB-2005-0520 Settlement Agreement (issue 3.13) there was complete settlement on the appropriateness of Union's forecast GDAR compliance costs. Parties also accepted Union's proposal for pre-approval to change rates effective January 1, 2008 to incorporate the bill-ready costs (issue 6.8).

In light of bill-ready implementation developments, most recently the Board issuing a Notice of Proposal to Amend the Gas Distribution Access Rule (EB-2007-0685), it is evident the January 1, 2008 in-service date will likely no longer apply. As stated at Exhibit B Tab 1 p. 11 of Union's EB-2007-0606 pre-filed evidence, in the event there is a change to the timing of the implementation of the bill-ready phase, Union will address the impact on base rates once a decision is made by the Board. Once a formal request for the bill-ready service is made, Union will develop a revised bill-ready cost estimate to reflect more current pricing assumptions. Consistent with GDAR compliance costs incurred to date, Union expects to be able to record these costs in the GDAR Costs deferral account and recover these incremental costs in rates.

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 16

Issue 8.1 - What is the appropriate plan term for each utility?

Question:

Union is proposing a 5-year term plan. The evidence states that, the term of a price cap plan must be long enough to justify incurring the implementation costs required to pursue the productivity improvements. Please provide examples of productivity initiatives that would be undertaken in a five-year plan but could not be undertaken in a three or four year time period.

Response:

Please see interrogatory response provided at Exhibit C32.4.

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 42

Issue 9.1 - Should an off-ramp be included in the IR plan?

Question:

Union's evidence is that within the context of a properly constructed IR plan there is no need for off-ramps. Under what circumstances would Union support an off-ramp? Please explain.

Response:

Union could support an off-ramp if the incentive regulation plan was not designed properly and as a result it is the cause of a decline in financial stability for the company. All stakeholders benefit from a financially stable utility.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 17

Issue 12.3.1 - What should be the criteria for changes in rate design?

Question:

Union's evidence states that it would like the opportunity to adjust the fixed and variable charges annually. Please provide Union's proposals in terms of how it intends to adjust the fixed and variable components under its proposed 5-year plan.

Response:

Please see interrogatory response provided at Exhibit C1.21.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 17

Issue 12.3.1 - What should be the criteria for changes in rate design?

Question:

Union's evidence is that it requires the flexibility to respond to a changing marketplace by developing new services. Please identify all new services contemplated and how those services will be priced.

Response:

Please see interrogatory response provided at Exhibit C5.1.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615

UNION GAS LIMITED

Answer to Interrogatory from
Consumers Council of Canada ("CCC")

Reference: B/T1/p. 41

Issue 12.4.4 - What should be the information requirements for new non-energy services?

Question:

Union's evidence is that it expects that if changes are required to the non-energy charges during the plan it will provide the Board with evidence that supports the change. What type of approval process is contemplated? Would it be outside Union's annual review process? Please provide details as to how these changes would occur. From Union's perspective would prior Board approval be required? If not, why not?

Response:

Union would include a request for changes to non-energy charges as part of its Rate Setting Filings. Union would file requests for changes earlier if Union anticipated that more time to review the proposed changes would be required than available to review Rate Setting Filings. Non-energy charges form part of the Board's rate order. As such, Board approval is required to change them.

Question: August 20, 2007
Answer: September 4, 2007
Docket: EB-2007-0606 / EB-2007-0615