



By electronic filing and by e-mail

January 4, 2010

Kirsten Walli
Board Secretary
Ontario Energy Board
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Dear Ms Walli,

Union Gas Limited ("Union")
Dawn Gateway Limited Partnership ("Dawn Gateway LP")
Board File No.: EB-2008-0411
Our File No.: 339583-000036

A. Introduction and Overview

These are the submissions of Canadian Manufacturers & Exporters ("CME") pertaining to the estimate provided by Union Gas Limited ("Union") on December 23, 2009, of the Cumulative Under-Recovery since January 1, 2003, related to the St. Clair Line. Union's estimate is \$3.951M as of March 1, 2010.

We also support Mr. Quinn's request for an extension of the deadline for responding to Union's subsidy burden calculation to Friday, January 8, 2010. We seek the deadline extension to enable us to liaise with Mr. Quinn for the purpose of preparing and filing by Friday a Schedule comparable to Appendix B in Union's December 23, 2009 evidence that will show the corrections that we say are needed to reflect the spirit and intent of the Board's November 27, 2009 Decision and Order.

For reasons which follow, we submit that Union's estimate is incorrect and materially low.

1. Summary of Errors in Union's Calculation

The reasons why Union's calculation is incorrect and materially low, each of which is discussed in further detail below, include the following:

- (a) The estimate should be done as of December 31, 2010, and not March 1, 2010, as Union proposes. By grossing up, for twelve (12) months, Union's Under-Recovery estimate of \$118,000 for the two (2) months ending March 1, 2010, we

estimate that the use of a December 31, 2010 calculation date increases Union's calculation by about \$590,000.¹

- (b) Union's exclusion from the subsidy burden absorbed by its ratepayers since January 1, 2003, of the St. Clair River crossing toll of \$342,000 per annum is incorrect and inappropriate for the reasons described below. These costs are clearly part of the subsidy burden related to the St. Clair Line as Union acknowledged in its evidence in this proceeding and, in particular, in Exhibits J1.1 and J1.2, upon which the Board relied in rendering its November 27, 2009 Decision and Order. Including the St. Clair River crossing toll increases Union's calculation of \$3.951M to March 1, 2010, by \$2.451M and by a further \$285,000 from March 1, 2010, to December 31, 2010, for a total increase of \$2.736M.²
- (c) Union's calculation fails to include yearly interest at the Board approved rate applicable to deferral account balances on the cumulative balances for each of the years between January 1, 2003, and December 31, 2010. Using an illustrative simple interest rate of 3% per annum, we estimate that without compounding the inclusion of interest in the subsidy burden calculation from January 1, 2003, to December 31, 2010, adds an amount of about \$1M to the calculation. We need Mr. Quinn's input to verify that we have properly estimated the interest amount.³

When adjustments are made for the errors in Union's calculation, the portion of the gain on the sale to be recorded in the deferral account is not \$3.951M, as Union proposes, but an amount of about \$8.277M, including interest, or about \$7.277M, excluding interest.⁴

2. Other Ratemaking Consequences to be Considered in Union's Next Rate Case

At the outset, it needs to be emphasized that the amount that the Board is now determining for recording in the deferral account only pertains to the ratepayers' share of the gain on the sale of the St. Clair Line to Dawn Gateway Limited Partnership ("DGLP").

In its November 27, 2009, Decision and Order, the Board defines the gain as the difference between the Net Book Value ("NBV") of the St. Clair Line and its market value sale price that the Board established at the replacement costs of the pipeline. The ratemaking consequences for Union's ratepayers of the transfer of the St. Clair River

¹ To add 10 months to Union's 2010 calculation, one multiplies Union's 2 month Under-Recovery estimate of \$118,000 by 5 for a total of \$590,000.

² These amounts are extrapolated from Union's Appendix B.

³ When the information in Union's Appendix B is adjusted to include Union's St. Clair crossing costs and to reflect 12 months instead of 2 months for 2010, the subsidy burden in 2003 becomes \$1.138M and the cumulative subsidy burden in 2010 is about \$7.278M. We estimate the interest amount by applying 3% to the average of these 2 amounts being \$4.208M to produce an annual amount of about \$126,000 which we then multiply by 8 to cover the years 2003 to 2010 inclusive. This gives us a total amount slightly in excess of \$1M.

⁴ These numbers reflect the addition of \$3.951M (Union's calculation); \$.590M for the December 31 date adjustment, \$2.736M for St. Clair River crossing toll and \$1M for interest, for a total of \$8.277M including interest or \$7.277M excluding interest.

crossing and the St. Clair Line to DGLP in addition to their share of a portion of the gain, include the removal of the St. Clair Line and related assets from Union's utility Rate Base and the Cost of Service.

We submit that these other ratemaking consequences are to be determined in a Union Rate Case. We interpret the last sentence in paragraph 123 of the November 27, 2009 Decision and Order to be a finding to this effect. There, the Board stated as follows:

"Rates can be adjusted at a subsequent rate proceeding."

Union did not include this sentence in the passage it extracted from paragraph 123 of the Board's Decision and Order of November 27, 2009, which is quoted at page 3 of Union's Evidence filed on December 23, 2009.

Since Union's 2010 rates have already been set under its five year Incentive Rate Plan ("IRP"), the first Union Rate Case in which these other ratemaking consequences can be considered will be Union's Application for 2011 Rates.

In its initial pre-filed evidence in this proceeding, Union suggested that these other ratemaking consequences were limited to the removal of the NBV of the St. Clair Line on re-basing when Union's five year IRP terminates on December 31, 2012. The Board referred to this aspect of Union's proposal in paragraph 78 of its November 27, 2009, Decision and Order.

We wish to emphasize that we disagree with Union's position that these other ratemaking consequences are not to be considered until re-basing. It is our position that such an approach is incompatible with the terms of Union's IRP and is unreasonable and unfair. It is inappropriate for Union's owner to concurrently collect costs associated with the St. Clair Line and St. Clair River crossing from both Union ratepayers and DGLP ratepayers.

While we recognize that this is not a matter to be determined now, we wish to make it clear that we reserve our client's rights to raise the matter in Union's 2011 and 2012 rate applications. We will raise the matter in the event that Union does not reduce its IRP rates in each of those years by the net cost reductions that will ensue in each of those years as a result of the transfer of the St. Clair River crossing and St. Clair Line to DGLP.

These net cost reductions are in an amount of \$993,000 in each of those years if one uses the full year 2010 subsidy burden as the measurement surrogate, or about \$1.196M if one uses the 2007 base year subsidy burden as the measure of those cost reductions.⁵

The Board recently determined in Union's restructuring application that net cost reductions of about \$1.3M per year during the term of Union's IRP are material and are to be flowed through to ratepayers.⁶ The materiality of the 2011 and 2012 cost reductions

⁵ These numbers reflect the amounts in Union's Appendix B adjusted to include St. Clair crossing tolls.

⁶ EB-2008-0304 Decision and Order dated November 19, 2008.

cannot reasonably be challenged when it is recognized that in combination with the ratepayer share of the gain, they total between about \$9M and \$10M using our estimate of the ratepayer share of the gain at \$8.277M, including interest, or \$7.277M, excluding interest.⁷

3. Implications for 2009 Earnings Sharing

In its December 23, 2009 evidence, Union suggests that the cumulative under-recovery amount will have implications for 2009 Earnings Sharing. The evidence suggests that Union plans to deduct the entire amount of the gain to be allocated to ratepayers as an expense when calculating 2009 Earnings Sharing. If this is what Union plans, then we do not agree that this is appropriate. However, rather than debating matters pertaining to 2009 Earnings Sharing in this proceeding, we suggest that the implications for 2009 Earnings Sharing, if any, of the final determination in this proceeding of the ratepayers' share of the gain should be determined in the second quarter of 2010 when Union has presented its 2009 Earnings Sharing calculation to the Board and interested parties for their consideration.

4. Regulatory Framework and Leave to Construct Issues

The Board's November 27, 2009 Decision and Order allows a regulatory framework proposal for DGLP to be made in this the concluding phase of this proceeding. However, Union has not presented the regulatory framework proposal in its evidence.

Union's December 23, 2009 letter to the Board indicates that DGLP has initiated separate proceedings with respect to the regulatory framework issue. In those proceedings, DGLP has requested leave to construct the Bickford to Dawn extension of the St. Clair Line.

DGLP has not yet provided a copy of this Application to us and, as a result, we are, as yet, unaware of the regulatory framework it proposes.

In these circumstances, we assume that in due course, the Board will require DGLP to provide parties to this proceeding with notice of its application and that initial comments on the regulatory framework DGLP proposes will now be made in its application rather than in this proceeding.

We also assume that the Board will follow its normal processes in responding to DGLP's application for leave to construct the new Bickford to Dawn pipeline and that in due course, further directions with respect to pre-hearing discovery and a hearing of matters pertaining to the relief DGLP seeks will issue.

In these circumstances, we are not planning to make any initial comments in this proceeding on the regulatory framework DGLP proposes. We expect CME will intervene in DGLP's application to support construction of the new Bickford to Dawn

⁷ When you add 2 x \$993,000 or 2 x \$1.96M to these numbers, you get amounts in the \$9M to \$10M+ range.

pipeline and to support a regulatory framework which reasonably accommodates the contracts DGLP has executed with shippers.

B. Detailed Rationale for Corrections to Union's Subsidy Burden Calculation

1. Factual Context for Subsidy Burden Calculation

(a) Date for Subsidy Burden Calculation

In its initial evidence in this proceeding, Union stated that obtaining all of the requisite regulatory approvals may take several years. The Board referred to this evidence in paragraph 17 of its November 27, 2009 Decision and Order. On the basis of this evidence, Union requested and the Board approved the transfer of the St. Clair Line to DGLP as long as it takes place before December 31, 2013.

In its December 23, 2009 evidence, Union is now suggesting that the requisite regulatory approvals need to be granted on an immediate basis. This evidence is incompatible with the initial filing.

The reality is that the sale transaction cannot be completed before DGLP obtains the regulatory approvals it has requested. In the context of Union's initial evidence, as well as the processes that need to be followed by the Ontario Energy Board to respond to DGLP's December 23, 2009 application, we suggest that it is unrealistic for DGLP and Union to expect all requisite regulatory approvals will be granted before the end of February 2010.

While CME will likely be supporting DGLP's leave to construct request and a regulatory framework that allows DGLP to honour the agreements it has already signed, it is unrealistic to expect that all requisite regulatory approvals will be granted before sometime in the third quarter of 2010. There may well be environmental, landowner and other issues that the Board will need to hear and determine in DGLP's application.

On this ground alone, the date of March 1, 2010, that Union has used in its calculation is unreasonable and unrealistic.

Moreover, another important fact relevant to a determination of the date to use in the subsidy burden calculation is that Union's 2010 rates have already been set. In these circumstances, an adjustment to 2010 rates to reflect a mid-year transfer of the St. Clair Line and the St. Clair River crossing to DGLP cannot now be made with ease.

We submit that, in combination, these two facts operate to require the use of a December 31, 2010 date in the subsidy burden calculation.

(b) Union's St. Clair Crossing Costs are part of the Subsidy Burden

The St. Clair River crossing connects the integrated system of Michigan Consolidated Gas Company ("MichCon") to Union's integrated system at the north westerly end of the St. Clair Line. St. Clair crossing tolls are embedded in Union's rates and are costs that Union incurs to generate the Rate C1 revenues that are included in Appendix B to the December 23, 2009 evidence.

In these circumstances, Union's St. Clair crossing tolls are clearly part of the subsidy burden on its ratepayers related to the St. Clair Line. We submit that Union's recognized this reality when it submitted its initial evidence in this case, including Undertaking Response J1.1. The acknowledgement that St. Clair crossing tolls and/or costs are part of the subsidy burden is reflected in the heading of Union's response in Exhibit J1.1 which reads:

"2003-2008 Net Revenues and Estimated Operating Costs"

Exhibit J1.1 also included a specific line item for "St. Clair River crossing toll" in the amount of \$342,000 per year.

These costs are not absorbed by the owner of the St. Clair crossing and there is no reasonable basis for now excluding these costs from the subsidy burden calculations.

Exhibits J1.1 and J1.2 are St. Clair Pipeline subsidy burden calculations submitted by Union during the course of the hearing. They cover the period 2003 to 2008 inclusive and do not deal with the years 2009 and 2010. These calculations are not dependent upon the jurisdictional character of either the St. Clair crossing or the St. Clair pipeline. The Board's determination that the St. Clair pipeline remains within provincial jurisdiction does not operate to permit Union to now materially change the subsidy burden calculations in Exhibits J1.1 and J1.2.

The fact that, in a constitutional sense, the St. Clair Line is not integral to the St. Clair crossing is irrelevant to the question of whether the St. Clair crossing tolls are costs incurred by Union to produce the Rate C1 revenues reflected in Appendix B of its December 23, 2009 evidence. Union's reliance on the Board's jurisdictional determinations to now attempt to exclude St. Clair crossing costs from subsidy burden calculation is inappropriate and lacks merit.

We recognize that in paragraph 122 of its November 27, 2009 Decision and Order, the Board estimated the cumulative subsidy burden at about \$5M. While the manner in which the Board derived its subsidy burden estimate of \$5M is not detailed in the Decision and Order, relevant evidence pertaining to the matter is contained in Exhibits J1.1 and J1.2. Because these exhibits cover the period 2003 to 2008, we believe that the Board's \$5M estimate is for the period January 1, 2003, to December 31, 2008. This belief is reinforced by the Board's reliance on Exhibit J1.1 in paragraph 83 of the November 27, 2009 Decision and Order to

quantify the cumulative operating cost deficit at about \$1.8M. This deficit is for the period 2003 to 2008 inclusive.

Our belief that the Board's \$5M cumulative subsidy burden estimate does not include 2009 and 2010 subsidy burdens is also corroborated by Union's Appendix B in its December 23, 2009 evidence which shows the cumulative subsidy burden at December 31, 2008, at about \$5.680M⁸ when St. Clair crossing costs are included in the subsidy calculation. This amount is higher than the Board's \$5M estimate because Union's calculations in Appendix B include Rate Base items for working capital and line pack that bring the 2008 Rate Base to about \$5.8M which is higher than the \$5.2M NBV discussed at the hearing and to which the Board refers in paragraph 78 of its November 27, 2009 Decision and Order.

We rely on this analysis to make two points. The first is that in rendering its November 27, 2009 Decision and Order, the Board has relied on Union's evidence which acknowledges that its St. Clair crossing costs are part of the subsidy burden. Union cannot now effectively make a material change to that evidence by eliminating its St. Clair crossing costs as part of the subsidy burden for the purpose of implementing the Board's Decision and Order of November 27, 2009. Union is estopped from now resiling from that evidence.

The second is that our calculation of the subsidy burden to December 31, 2010, at \$8.227M including interest and at \$7.277M excluding interest is compatible with the Board's Decision and Order estimate of \$5M at the end of 2008 based on Union's evidence in Exhibits J1.1 and J1.2. In contrast, Union's calculation of the subsidy to March 1, 2010, at \$3.951M is, we submit, at odds with the Board's \$5M estimate based on Exhibits J1.1 and J1.2. Union is seeking approval for a calculation that is not in accordance with the evidence at the hearing and the November 27, 2009 Decision and Order based thereon. We urge the Board to reject Union's post-Decision attempt to benefit its owner by now materially reducing the subsidy burden calculations submitted during the hearing in Exhibits J1.1 and J1.2.

We reiterate that Union incurs St. Clair crossing costs to provide Rate C1 service from St. Clair to Dawn. With a transfer of the St. Clair Line and the St. Clair crossing to DGLP, the Rate C1 service from St. Clair to Dawn will no longer be available. This, in and of itself, demonstrates that St. Clair crossing costs are a part of the subsidy burden. Put another way, Union cannot reasonably expect to have St. Clair crossing costs remain embedded in its rates after completion of the sale transaction when the Rate C1 transportation service from St. Clair to Dawn is no longer available. Yet, this is the effect of what Union is now proposing.

⁸ This is the cumulative amount in Union's calculation at December 31, 2008, with St. Clair tolls included.

2. Corrections to Reflect the Use of a December 31, 2010 Calculation Date

We have already noted in Section 1, subparagraph (a) of the Introduction and Overview Section of this letter that the use of a December 31, 2010 calculation date increases Union's calculation of \$3.951M by \$590,000.

3. Corrections to Reflect Inclusion of St. Clair Crossing Costs to December 31, 2010

As earlier noted in Section 1, subparagraph(b) of the Introduction and Overview Section of this letter including St. Clair crossing costs to March 1, 2010, increases Union's calculation by \$2.451M and by a further \$285,000 for the period March 1 to December 31, 2010, for a total of \$2.736M.

4. Rationale for Interest on Yearly Cumulative Balances and Corrections to Include Interest

We recognize that in its November 27, 2009 Decision and Order, the Board did not require Union to include interest on the annual cumulative subsidy burden amounts from January 1, 2003. Nevertheless, we suggest that an interest allowance in each year is appropriate because Union's owner has enjoyed the use of the subsidy burden money ratepayers have provided since January 1, 2003.

If the situation were reversed and Union's owner had absorbed part of this subsidy burden for ten (10) years, then Union would undoubtedly have included an interest component in any subsidy burden calculation that its owner was authorized to recover from the gain on the sale of the assets.

For illustrative purposes, we have assumed that the interest rate the Board allows on deferral account balances in each of the years 2003 to 2010 inclusive is 3%. Under the assumptions we have used, we calculate the interest rate addition to be about \$1M. We rely on the Board to apply the correct rate in each year if it agrees with us that an interest rate addition to the subsidy burden calculation is appropriate. In this regard, CME urges the Board to apply the prescribed interest rates established pursuant to the methodology approved in EB-2006-0117 for deferral and variance accounts.

5. Corrected Amount to be Recorded in the Deferral Account

Based on the foregoing, we submit that the subsidy burden from January 1, 2003, to December 31, 2010, to be recorded in the deferral account is the sum of about \$8.277M, including interest, or about \$7.277M, excluding interest.

C. Conclusion

For all of these reasons, we urge the Board to determine that the ratepayers' share of the gain to be recorded in the deferral account is about \$8.277M as of December 31, 2010.

As noted above, our plan is to obtain Mr. Quinn's help in preparing and filing by Friday, January 8, 2010, a Schedule comparable to Union's Appendix B in its December 23, 2009

evidence to reflect the corrections to Union's calculation that we say are needed to properly reflect the spirit and intent of the Decision and Order.

We urge the Board to direct Union to present its proposals for clearing the deferral account and for addressing the other ratemaking consequences of a transfer of the St. Clair Line and the St. Clair crossing to DGLP in its application for 2011 rates. Any attempt by Union to avoid adjusting its 2011 and 2012 rates for cost reductions associated with these transfers to DGLP can be addressed at that time.

Any implications for 2009 Earnings Sharing should be addressed later when Union seeks Board approval for its 2009 Earnings Sharing Mechanism ("ESM") calculations.

D. Costs

We request that CME be awarded its reasonably incurred costs of participating in this phase of this proceeding.

Please contact us if there are any questions about the manner in which we derived the correction amounts described in this letter.

Yours very truly,

A handwritten signature in black ink, appearing to read 'Peter C.P. Thompson', with a long horizontal flourish extending to the right.

Peter C.P. Thompson, Q.C.

PCT\slc

c. Sharon Wong (Blakes)
All Intervenors EB-2008-0411
Paul Clipsham (CME)

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