



By Email

November 28, 2007

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Dear Ms Walli

Union Gas Limited	
Application to purchase shares of Tipperary Gas Corp.	
Board File No.:	EB-2007-0837
Our File No.:	302701-000421

Introduction

We are writing this letter on behalf of our client, the Industrial Gas Users Association (“IGUA”) to comment on the Application by Union Gas Limited (“Union”) for permission to purchase 75% of the Tipperary Gas Corp. (“Tipperary GP”).

The details of the proposed transaction are described in the Board’s Notice of Application and Notice of Written Hearing herein dated November 13, 2007, which we received on November 14, 2007.

The Board has asked for comments on whether the proposed transaction “... facilitates the maintenance of a financially viable industry for ... the storage of gas”. IGUA’s comments on this question are set out below.

IGUA Comments

A “financially viable industry”, in a competitive market, is achieved when new competitors can enter the market without difficulty and when the competitive market participants earn returns which are reasonably commensurate with the risks undertaken.

The fact Union is seeking permission to buy a majority interest in what was formerly a new and independent entrant into the “competitive” Ontario storage services market demonstrates that prospective Ontario storage services operators, who are entirely independent of Union and its affiliates, have difficulty surviving on a stand-alone basis. The proposed transaction is indicative of Union’s market dominance of the Ontario market as Ontario’s largest storage services provider.

The proposed transaction, in conjunction with Union’s recently announced purchase of a 1Bcf Storage Pool, near Sarnia, from Midway Petroleum Company, demonstrates that

Union, the market dominant incumbent, is, as a result of the Board's November 7, 2007 NGEIR Decision, eliminating what little competition it faces from storage services operators in Ontario. A copy of Union's November 27, 2007, Press Release announcing its acquisition of these storage assets is available on Union's website at <http://www.uniongas.com/news/releases/2007/Nov272007.asp>. Union's actions in acquiring prospective competitors are anti-competitive and constitute behaviour by a market participant which wields market power.

Allowing a dominant market participant to increase its market concentration facilitates and enhances that participant's opportunities for earning excessive or supernormal returns. Permitting a dominant market participant to increase its market concentration does not facilitate a "financially viable industry". It facilitates enhanced dominance and, thereby, enhances Union's opportunities to earn supernormal returns from its unregulated storage business.

The extent to which Union's in-franchise ratepayers will be called upon to pay for the services Tipperary GP will sell at "market prices" is not disclosed in Union's Application materials. Accordingly, it is impossible to determine the extent to which Union's purchase of a majority interest in Tipperary GP will have an impact on Union's regulated customers. Any transaction which increases the market concentration of an incumbent operating in a market which is insufficiently competitive to prevent that incumbent from earning excessive and supernormal returns is likely to have an adverse effect on consumers. The statement to the opposite effect contained in paragraph 21 of Section 3 of the Project Summary in the Application is unsupportable.

The proposed transaction reinforces views expressed by IGUA in its Petition to the Lieutenant Governor in Council ("LGIC") seeking relief with respect to the Board's November 7, 2006, NGEIR Decision. For the reasons described in its Petition to the LGIC, the market for the storage services which Union provides is insufficiently competitive to prevent Union's owner from earning excessive and supernormal returns from selling storage services at so-called market prices. For this reason, IGUA and others have urged the LGIC to find that the entire storage business being conducted by Union should remain subject to regulatory scrutiny.

Further information is available which strongly indicates that Union's earnings from the unregulated segment of the storage business, which the NGEIR Decision creates, are and will be excessive and supernormal. The additional information to which we refer is as follows:

- (a) At the moment, only about \$103M of Union's 2007 Rate Base is allocated to its unregulated storage business segment (see NGEIR Decision at page 72);
- (b) In proceedings before the Board on July 9, 2007, in EB-2007-0598, Union confirmed that the average price achieved in 2006 for short-term storage services was \$2.86/GJ. This price results in a premium over Union's cost-based storage rate of 30¢/GJ of some \$2.56/GJ. At a premium of \$2.50/GJ, the 50 PJs of ex-franchise storage services Union provides will produce unregulated "premium" storage-related earnings for Union of some \$125M per year when the transition period established in the NGEIR Decision ends;

- (c) In its recently released Interim Report for the Third Quarter ending September 30, 2007, Union reports earnings for the nine (9) months ending September 30, 2007 of \$113M, which is a \$47M increase over earnings of \$66M for the nine (9) months ending September 30, 2006. The Interim Report at page 5 states that this \$47M increase in earnings is attributable, in part, to favourable storage market conditions and strong storage revenues; and
- (d) Union now relies on the NGEIR Decision to attempt to “claw back” about 4PJs of storage space and deliverability currently contractually allocated to large volume customers served by Union under the auspices of its T1 and T3 Rate Schedules. This relief, if granted, could add another \$10M per annum to Unions’ unregulated storage services earnings.

All of this further information indicates that in the “end state” contemplated by the NGEIR Decision, Union could be earning as much as \$135M per annum on the \$100M of Rate Base currently allocated to the unregulated segment of its storage business. By any standard, this level of earnings is not only supernormal; it is unconscionable. It is not an earnings result that would ensue in a competitive market place.

Accordingly, IGUA submits that if regulatory scrutiny of the entire storage services business conducted by Union is not restored, then Union’s purchase of 75% of Tipperary GP will increase Union’s dominance in a market which is insufficiently competitive to prevent Union’s owner from earning excessive and supernormal returns.

The proposed transaction will only facilitate the maintenance of a financially viable industry for the storage of gas in a scenario where the entire storage business being conducted by Union remains subject to regulatory scrutiny.

Costs

The Notice of Application for this proceeding requires a participant therein to indicate whether it expects to seek costs from Union. As the Board is aware, IGUA’s ability to actively participate in proceedings before the Board depends upon the issuance of cost awards in its favour. The Board has consistently found IGUA to be eligible for cost awards. In these circumstances, IGUA seeks and respectfully requests an award of its reasonably incurred costs of participating in this proceeding.

Please contact me if the Board requires any further information with respect to the comments made on behalf of IGUA.

Yours truly



Peter C.P. Thompson, Q.C.

PCT\slc

- c. Glenn Leslie (Blakes)
Michèle Thébeau (Union Gas Limited)
Murray Newton (Industrial Gas Users Association)