BOMA/LPMA/WGSPG #1

INTERROGATORY

Do the conclusions reached in this report also apply to pervasive corporate tax increases?

PEG RESPONSE

Yes.

Witness: Mark Lowry

BOMA/LPMA/WGSPG #2

INTERROGATORY

Please confirm that increased capital cost allowances being considered at the federal level:

i) relate to distribution assets (Class 1) and computer equipment (Class 45);

ii) are retroactive to assets added in 2007 (please provide the effective date);

iii) may or have been adopted for Ontario corporate tax calculations also effective in 2007.

PEG RESPONSE

i) It is my understanding that increases in federal capital cost allowances are being considered for assets acquired after March 18 2007 in the following categories:

   a. buildings used for manufacturing and processing in Canada;
   b. other non-residential buildings;
   c. computer equipment;
   d. natural gas distribution lines; and
   e. liquefied natural gas facilities.

ii) It is my understanding that the effective date is March 18, 2007.

iii) Adjustments to these allowances have not to my knowledge been adopted in Ontario.

BOMA/LPMA/WGSPG #3

INTERROGATORY

What companion reductions in corporate tax burdens are under consideration in Ontario?

PEG RESPONSE

It is my understanding that Ontario's government plans to cut capital tax rates over a multiyear period and to eliminate the tax for all corporations in 2010.

Witness: Mark Lowry

BOMA/LPMA/WGSPG #4

INTERROGATORY

Does PEG believe that any changes that are in effect for the base year, but not reflected in base year rates, should be reflected as adjustments to base year rates? If not, please explain.

PEG RESPONSE

We believe that either approach is defensible in principle. Base year rates were presumably based on a forward test year. If the rate adjustment mechanism is considered sequentially, after the establishment of base rates, information could come to light during the consideration of such a mechanism that would cause these rates to be unreasonable. However, it is not clear that the changes in tax policy at issue here are important enough to warrant such an adjustment. More generally, we are concerned that the establishment of multiyear rate plans would be much more difficult if base year rates were routinely reviewed in the year following their establishment in the light of new information.

BOMA/LPMA/WGSPG #5

INTERROGATORY

With respect to the phrase "pervasive reductions in corporate taxes" please provide the following:

i) the proportion of corporations in Canada that pay federal corporate income tax;

ii) the proportion of corporations in Canada that pay provincial income tax;

iii) the proportion of corporations in Canada that pay a provincial capital tax;

iv) the thresholds for which corporations do not pay any provincial capital tax by province;

v) any provinces that do not collect a provincial capital tax.

PEG RESPONSE

i) It is my understanding that all for profit corporations in Canada are subject to corporate income taxes.

ii) I don't know.

iii) I don't know.

iv) I understand that in Ontario, smaller firms effectively pay no capital tax. I do not know the policy in other provinces.

v) I don't know.

BOMA/LPMA/WGSPG #6

INTERROGATORY

What would have been the impact on the 1.73% X factor recommended by PEG for Union under a price cap mechanism had the reduction and elimination of the provincial capital tax, the reduction in the federal corporate tax rates and the increase in the CCA rates, all as shown in Exhibit N1, Tab 1, Schedule 1, Appendix D of the Enbridge Gas Distribution Settlement Agreement dated February 4, 2008 (see attached) been in effect for the last five years of the period provided by PEG? Please explain. If a price estimate cannot be provided in the timeframe, please provide a “best guess” range of the impact.

PEG RESPONSE

The effect of the tax reduction would have been registered chiefly via the input price differential. In calculating the recommended 1.73% X Factor for Union, PEG elected not to consider tax effects in calculating the IPD on the grounds that any changes in tax rates over the 2000-2006 period would not inform the calculation of a long term input price differential. The hypothetical tax developments would therefore have had no effect on our recommended X factor.

BOMA/LPMA/WGSPG #7

INTERROGATORY

The evidence indicates that "In the long run, competition between firms is apt to pass cost savings of both kinds through to customers in the form of slower growth in the prices of the products that they sell".

i) Please define "long run".

ii) Would the same result be expected of an appreciation in the country's currency?

PEG RESPONSE

i) The long run is a period long enough for firms to increase capacity sufficiently to slow the rate of price growth to the point where the excess economic profits created by the tax cuts are eliminated. Economic intuition suggests that this process should be completed within five years.

ii) To the extent that products traded internationally by Canadians

   i. are final goods and services

   ii. affect the marginal cost of production (like jet fuel prices affect the marginal cost of air travel)

   I would expect the effect of appreciation in a company's currency to affect inflation *more* quickly than a drop in corporate income and capital taxes.

BOMA/LPMA/WGSPG #8

INTERROGATORY

The evidence states that "any Z factor intended to rectify this problem must consider the extent to which the effect of tax reductions is captured by the slowdown that does occur in the GDPIPI". Should any such Z factor also consider the lead or the lag associated with the effect of a tax change? If not, please explain why not

PEG RESPONSE

Z factors can in principle consider leads and lags but this greatly complicates their calculation and raises the cost of incentive regulation. Suppose, by way of illustration, that Union is obliged to reduce rates for a large share of its tax savings during this plan on the grounds that lower taxes only slow inflation with a lag. In that event, Union can file for a Z factor in the next rate plan on the grounds that inflation is being slowed with a lag by tax cuts that occurred during the prior rate plan.

BOMA/LPMA/WGSPG #9

INTERROGATORY

The evidence states that "the tax reductions under discussion are pervasive and should slow the growth of the GDPIPI materially". Please define materially in this context.

PEG RESPONSE

By materially I mean by more than 10 or 20 basis points.

Witness: Mark Lowry

BOMA/LPMA/WGSPG #10

INTERROGATORY

Does the provincial capital tax have a larger or smaller impact on a capital intensive utility relative to the average corporation? Please explain.

PEG RESPONSE

Capital taxes are proportional to the value of capital. I therefore expect that the provincial capital tax has a disproportionately large impact on a capital intensive business such as gas distribution.

Witness: Mark Lowry

BOMA/LPMA/WGSPG #11

INTERROGATORY

Is a change in the CCA rate for Class 1 (distribution assets) pervasive? Please explain.

PEG RESPONSE

This change is not pervasive, inasmuch as it affects gas distributors such as Union much more than it affects the typical firm in the economy.

Witness: Mark Lowry