



uniongas

A Spectra Energy Company

October 31, 2008

Ontario Energy Board
2300 Yonge Street,
27th Floor
Toronto, ON
M4P 1E4

Attention: Ms. Kirsten Walli, Board Secretary

Re: EB-2008-0292 – Motion to Review

Dear Ms. Walli:

Please find attached Union's Prefiled Evidence related to the above noted docket number.

Yours truly,

[original signed by]

Chris Ripley
Manager, Regulatory Applications

cc: All Intervenors
Michael Penny, Torys

Union Gas Limited

Prefiled Evidence

Union filed a notice of motion to the Ontario Energy Board (“Board”) on August 28, 2008 seeking clarification of the Board’s Decision and Order (“Decision”) dated July 31, 2008 issued in Union’s incentive regulation (“IR”) proceeding EB-2007-0606.

On October 27, 2008 the Board issued a Notice of Motion and Procedural Order No. 1. The Board directed Union to file evidence by October 31, 2008.

This submission is Union’s evidence.

Tax Change Pass Through

At page 9 of the Decision, the Board concluded that 50% of the cost consequences of certain federal and provincial tax changes which became effective during the incentive regulation term (as applied to the tax level reflected in the 2007 Board approved rates) should be treated as a Z factor and passed through to customers.

The Board also made the observation that “the approach used in Exhibit E3.1.1 is indicative” of how the savings are to be calculated for the purposes of the sharing.

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Exhibit E3.1.1 was provided by Union in response to an interrogatory to provide a schedule “similar to that in the Enbridge Gas Distribution Settlement Agreement ... Page 52” (“EGD Settlement”). Union had no involvement in the negotiation or preparation of the schedule shown on page 52 of the EGD Settlement.

Union responded to this interrogatory in accordance with its terms and provided a table similar to the table negotiated in the EGD Settlement. No Union witness adopted Exhibit E3.1.1 as a correct or appropriate basis for calculating a 50/50 sharing of the possible tax savings during the incentive regulation term, nor was this suggestion ever put to Union during the hearing.

The Enbridge document (and, therefore, Exhibit E3.1.1 in lines 2, 6, 10 and 14) assumed that 2007 Board approved capital additions would also be added to the capital cost of computer equipment and distribution assets for each of the years 2008 to 2012, i.e., in Union’s case, that rate base would increase by \$8.74 million each year for computer equipment and increase by \$133 million each year for distribution assets. The impact of the change in the capital cost allowance (“CCA”) on these capital additions is included in the calculation of the impact of the CCA rate change in Exhibit E3.1.1.

However, Union’s 2008 to 2012 IR plan operates off 2007 rates. Customers’ rates approved by the Board for 2007 do not include the costs related to new capital additions in the years 2008 to 2012. Union’s rates, and specifically the cost of capital and taxes, do not change during the IR plan as a result of capital additions undertaken during the IR term.

Exhibit E3.1.1 is, therefore, not indicative of the impact the identified tax rate changes would have on 2007 Board approved rates. Specifically, the impact on tax expense and revenue requirement of the changes in the CCA shown at lines 19 and 20 respectively is overstated by including asset additions beyond 2007. The impact on tax expenses in 2008 to 2012 of higher CCA on 2008 to 2012 additions should, therefore, not be passed through to customers. Rather, the impact of the tax changes which become effective during the incentive regulation term should be applied only to the amounts underlying 2007 Board approved rates.

To reflect this reality, Exhibit E3.1.1 has been revised to remove the impact of the 2008 to 2012 additions and is attached as Schedule 1 to this evidence.

Union, therefore, seeks clarification of the Decision from the Board that, in saying Exhibit E3.1.1, as filed in EB-2007-0606 is “indicative” of how savings are to be calculated for the purposes of sharing, the Board was not directing Union to share 50% of tax “savings” associated with new capital additions during the incentive regulation term (for which no rate increase for cost of capital and taxes will be available). The revised Exhibit E3.1.1 reflects how Union should capture tax pass through items throughout the IR term.

Risk Management

Union is seeking clarification with respect to two issues arising out of the Board's decision on risk management:

- 1) the 24 month fixed price purchase plan; and
- 2) the "costs" of risk management.

24 Month Fixed-Price Purchase Plan

In EB-2007-0520 Union sought Board approval to purchase 20% of its total sales service supply portfolio on a rolling 24 month fixed cost basis.

The Board recognized that Union's proposed 24 month fixed-price purchase plan was a form of hedging, as noted in the Board's decision at para. 2.3.7 where it stated:

"It is important to highlight the fact that the 24-month fixed price contracts form part of Union's Risk Management program...Insofar as the Board has approved the Risk Management program and the form of hedging instrument represented by the 24-month fixed price contracts, no further Board approval is needed...."

On page 16 of the July 31, 2008 Decision, the Board stated:

"What is at issue, however, is the narrow activity of financial hedging.

The other activities, including Union's use of rolling 24 month fixed-

price contracts, are in the area of gas supply procurement and are not being considered as part of this issue.”

As the Board found in EB-2007-0520, Union’s rolling 24 month fixed price purchase plan is financial in nature and does not directly involve the physical supply of gas. The rolling 24 month fixed price purchase plan is not simply -part of Union’s physical gas procurement plan. The rolling 24 month fixed price purchase plan is effected through a financial hedging instrument known as a “swap.” As such, the financial swaps underpinning the 24 month fixed price plan are in all material respects the same as other financial hedging instruments and contribute to mark to market gains and losses. —It was these gains and losses associated with Union’s hedging program which the Board found, in its recent decision, were of no material net benefit to customers.

Following- the release of the Board’s decision, Union concluded that the prudent course was to implement the Board’s decision promptly. Accordingly, Union unwound all outstanding hedges, including the financial swaps underpinning the 24 month fixed price purchase program, and reflected the impacts in its October 1, 2008 QRAM proceeding (EB-2008-0281).

Union felt it appropriate to clarify to the Board that the 24 month fixed price plan was a part of Union’s financial hedging program. Accordingly, given the Board’s findings that Union’s risk management plan provided no material net benefit to customer, the 24 month fixed price plan along with all other financial hedging was eliminated.

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Risk Management Costs

The Board, on page 17 of the July 31, 2008 Decision, disallowed the recovery of certain costs associated with commodity risk management and directed Union “to record the costs, which are currently embedded in rates” in a deferral account for future disposition at the end of the existing incentive regulation period. The Board also stated that the “appropriate adjustments to distribution rates will be considered at the time of rebasing.”

Exhibit J10.03 filed in the EB-2005-0520 proceeding explained that the cost of administering Union’s risk management program is recovered through the gas supply administration charge. There are no costs associated with Union’s risk management program included in Union’s distribution rates. The costs related to Union’s risk management program of \$103,831 were recovered through a Board-approved gas supply administration charge. As noted above, Union discontinued its risk management program in EB-2008-0281 effective October 1, 2008. The total cost of this program of \$103,831 was eliminated from the calculation of the gas supply administration charge, which reduced the administration charge by $\$0.0035/\text{m}^3$.

It is Union’s belief that the Board’s July 31, 2008 Decision with respect to the disallowance of costs was referring to the \$103,831 administrative cost of Union’s risk management program and that the Board was not using the word “cost” to refer to mark-to-market losses that Union might incur in the prudent discontinuation of its risk management program. In Union’s view, it would be inconsistent for risk management

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gains or losses to accrue to Union given all prior Board decisions related to gas supply risk management. This interpretation of the Board's directive is consistent with past practice. Prior to discontinuing the risk management program as of October 1, 2008, both gains and losses associated with financial hedging (including the 24 month fixed price purchase plan) were taken into account in the Union North and South Purchased Gas Variance Accounts which are recovered / refunded prospectively through the QRAM process.

As noted, Union unwound all transactions related to risk management before the October 1, 2008 QRAM application. The result was a modest mark to market year-to-date gain of \$2 million that flowed through to the PGVA with the elimination of the risk management program

Union, therefore, seeks clarification to the effect that the Board's intention was to disallow only the \$103,831 cost of Union's risk management program and that the elimination of those costs should be accomplished, not by a deferral account to record the elimination of an amount "embedded in rates" but through a reduction in the annual gas supply administration charge of \$103,831, as has now been done through the approval of the October 2008 QRAM application.

Estimated Tax Rate Change Impacts (2008-2012)

(\$ millions)

Line No.	2008 (a)	2009 (b)	2010 (c)	2011 (d)	2012 (e)	Total 2008-2012
Tax Related Amounts Forecast from CCA Rate Changes						
1	6.77	10.50	12.55	13.68	14.30	
2	8.74	8.74	8.74	8.74	8.74	
3	5.02	6.69	7.61	8.12	8.40	
4	10.50	12.55	13.68	14.30	14.64	
5	6.34	9.19	10.47	11.05	11.31	
6	8.74	8.74	8.74	8.74	8.74	
7	5.89	7.46	8.16	8.48	8.62	
8	9.19	10.47	11.05	11.31	11.43	
9	130.56	255.90	376.23	491.74	602.64	
10	133.23	133.23	133.23	133.23	133.23	
11	7.89	12.90	17.71	22.33	26.77	
12	255.90	376.23	491.74	602.64	709.09	
13	129.23	250.71	364.89	472.23	573.13	
14	133.23	133.23	133.23	133.23	133.23	
15	11.75	19.04	25.89	32.33	38.38	
16	250.71	364.89	472.23	573.13	667.97	
17	4.74	6.90	8.73	10.36	11.84	
18	33.50%	33.00%	32.00%	30.50%	29.00%	
19	1.59	2.28	2.79	3.16	3.43	
20	2.39	3.40	4.11	4.54	4.84	19.27
21	2.39	1.01	0.71	0.44	0.29	
17a	1.77	1.77	1.77	1.77	1.77	
18a	33.50%	33.00%	32.00%	30.50%	29.00%	
19a	0.59	0.58	0.57	0.54	0.51	
20a	0.89	0.87	0.83	0.78	0.72	4.10
21a		-0.02	-0.04	-0.06	-0.05	
Tax Related Amounts Forecast from Income Tax Rate Changes						
22	80.782	80.782	80.782	80.782	80.782	
23	23.12	23.12	23.12	23.12	23.12	
24	-	-	-	-	-	
25	103.9	103.9	103.9	103.9	103.9	
26	36.12%	36.12%	36.12%	36.12%	36.12%	
27	33.50%	33.00%	32.00%	30.50%	29.00%	
28	2.62%	3.12%	4.12%	5.62%	7.12%	
29	2.72	3.24	4.28	5.84	7.40	
30	4.09	4.84	6.30	8.40	10.42	34.05
31	4.09	0.74	1.46	2.11	2.02	
Tax Related Amounts Forecast from Capital Tax Rate Changes						
32	3,020.9	3,020.9	3,020.9	3,020.9	3,020.9	
33	-	-	-	-	-	
34	3,020.9	3,020.9	3,020.9	3,020.9	3,020.9	
35	0.285%	0.285%	0.285%	0.285%	0.285%	
36	0.225%	0.225%	0.075%	0.000%	0.000%	
37	0.060%	0.060%	0.210%	0.285%	0.285%	
38	1.81	1.81	6.34	8.61	8.61	27.19
39	1.81	-	4.53	2.27	-	
40	8.29	10.05	16.75	21.56	23.86	80.51
40a	6.80	7.52	13.47	17.79	19.75	65.33
41	4.15	5.03	8.37	10.78	11.93	40.26
41a	3.40	3.76	6.74	8.89	9.88	32.67
42	4.15	0.88	3.35	2.41	1.15	
42a	3.40	0.36	2.97	2.16	0.98	