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November 6, 2008

VIA EMAIL and COURIER

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
26th Floor
2300 Yonge Street
Toronto, ON
M4P 1E4

Dear Ms. Walli:

Re: Union Gas Limited-EB-2008-0292
Submissions re: Risk Management Program-Union Gas Limited

Please find enclosed the written submissions of VECC with respect to the above noted proceeding. Please be advised that we are unable to attend the oral hearing scheduled for Monday November 10, 2008, and so will be relying solely on our written submissions.

Yours truly,

Michael Buonaguro
Counsel for VECC
Encl.

IN THE MATTER OF the *Ontario Energy Board Act 1998*, S.O.1998, c.15, (Schedule B);

AND IN THE MATTER OF an Application by Union Gas Limited for an Order or Orders approving or fixing a multi-year incentive rate mechanism to determine rates for the regulated distribution, transmission and storage of natural gas, effective January 1, 2008.

SUBMISSIONS OF VECC
RE: UNION GAS LIMITED MOTION FOR REVIEW AND VARY

ISSUE 1: Clarification re: Continuation of Risk Management Program

1. Union's motion seeks clarification with respect to the continuation of its 24 month fixed-price purchase plan in light of the Board's ruling in EB-2007-0606 with respect to the use of financial hedging.

2. In VECC's view the distinction in the Board's decision between financial hedging and the 24 month fixed price purchase plan was a recognition that in the normal course of its gas procurement activities Union retains the ability to enter into a variety of gas procurement contracts including but not limited to short, medium, and long term contracts, including fixed price contracts. VECC notes, for example, the Board's consultation process in EB-2008-0280 which seeks to establish a process for the approval of long term contracts for the procurement of gas by utilities such as Union.

3. That Union's existing 24 month fixed-price purchase plan was built on financial tools within the confines of its Risk Management portfolio is now, it would appear, moot, as Union has discontinued that program.

ISSUE 2: Elimination of Risk Management Costs

4. VECC agrees with Union's analysis of how the $103,831 in Administrative costs should be eliminated, namely through the removal of those costs from the gas supply administration charge.

ISSUE 3: Tax Change Pass Through

5. VECC supports the Board's decision with respect to the use of Exhibit E3.1.1 as illustrative of how Union is to calculate the tax savings to be shared with ratepayers.

6. Union asserts that it should not be required to share tax savings associated with new capital additions made during the IRM period. Union's argument is that "Customers' rates approved by the Board for 2007 do not include the costs related to new capital additions in the years 2008 to 2012" and that "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."[1]

7. VECC respectfully submits that Union's argument is flawed. Union's characterization of its rate structure from 2008 to 2012 is that of a rate freeze, which is fundamentally incorrect. Union's rates are not frozen, they are subject to an automatic adjustment based on an incentive mechanism.

8. An incentive mechanism replaces cost of service regulation by providing a formulaic adjustment to rates in lieu of a detailed analysis of the components of a utility's cost of service that would individually increase or decrease a utility's revenue requirement in a particular test year. Instead of providing evidence of an increase or decrease in any particular revenue requirement item, the utility instead applies the incentive mechanism to the previous year's rates to determine what rate increase or decrease it will receive.

9. In this way all of the individual increases and decreases in revenue requirement that a utility will experience in the test year are subsumed within the incentive mechanism. Rather then apply for specific increases and decreases related to each discrete revenue requirement item, the utility instead is expected to operate within the increase or decrease provided by the incentive mechanism despite all of its actual cost increases and decreases.

10. Just because the rate change caused by the operation of the incentive mechanism is not translated into specific increases and/or decreases in the discrete revenue requirement items in Union's cost of service does not mean, as Union asserts, that Union's rates are frozen.

11. With respect to capital additions, for example, there is a presumption that the incentive mechanism, once applied, will provide sufficient rates to fund an appropriate level of capital additions within the rate year.

12. One of the few exceptions to the mechanical application of the incentive mechanism is the application of a Z factor, applicable when a utility will experience a material increase/decrease in its actual cost of service that, in

[1] Union's pre-filed evidence dated 20081031, page 2 of 7.

accordance with the criteria for Z Factor treatment, the Board determines will not be captured by the incentive mechanism.

13. By its very nature a Z factor, having been found to operate outside the confines of the incentive mechanism, reconnects the utility's rates to specific items of its cost of service.

14. In the present case, the Board has determined that despite the increase or decrease in rates produced by the IRM applicable to Union, Union will experience a material additional decrease in its actual cost of service during the IRM period related to its tax burden. The Board has determined that 50% of that decrease should be passed on to ratepayers as a Z factor.

15. In order to calculate those savings it is necessary, as the Board determined by reference to Exhibit 3.1.1 to identify the cost of service items in each affected rate year that yield the relevant tax savings and then calculate the actual tax savings in order to pass 50% of the savings on to ratepayers, including savings related to capital additions.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 6th DAY OF NOVEMBER, 2008

Michael Buonaguro
Counsel for VECC