unionGas
A Spectra Energy Company

November 6, 2008

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4

Dear Ms. Walli:

Re: EB-2008-0304

Please find attached an addendum to Exhibit C.2, an interrogatory from the Canadian Manufacturers and Exporters, in response to a letter from Mr. Thompson dated October 29, 2008.

Yours truly,

[original signed by]

Chris Ripley
Manager, Regulatory Applications

Attach.

c.c.: EB-2008-0304 Intervenors
Michael Penny, Torys
Bruce Pydee, WEI
Mark Garner, OEB

UNION GAS LIMITED

Answer to Interrogatory from
Canadian Manufacturers and Exporters ("CME")

Question:

Exhibit C.2 indicates that Union's ultimate parent, Spectra, will realize an additional 35¢ from every dividend dollar which emanates from Union Gas Company ("UGC") if the new internal restructuring is approved. We understand that the additional 35¢ which Spectra will receive from every dividend dollar is a result of US tax savings which the proposed restructuring is expected to produce.

One of the attachments to Exhibit D.7 is a memo to the Board of Directors of Union Gas Limited ("Union") from Curt Bernardi, Director, Legal Affairs, dated September 5, 2008. The US tax savings benefits to Spectra of the proposed restructuring are quantified on page 2 of that memo at "an estimated C$50 million".

Would Union please clarify the foregoing information by providing an exhibit which shows the estimated benefits Spectra will receive as a result of the proposed restructuring year-by-year from 2009 to 2012 inclusive so we can understand how the C$50 million estimate was derived and determine whether that estimated benefit is a total global benefit or an estimate of annual benefits which Spectra is expected to realize if the proposed restructuring is approved.

Response:

It is important to put the proposed internal reorganization, and CME's request for clarification of Exhibits C.2 and D.7, in its proper context. The issue in Exhibit C.2 and D.7 relates to an indirect U.S. shareholder tax under U.S. tax accounting rules on income received in the U.S. This has nothing to do with what Union's customers pay for gas service in Ontario. It is therefore the Applicants' position that the kind or magnitude of U.S. tax consequences under any ownership structure, present or proposed, are irrelevant to this application and beyond the Board's jurisdiction. Without prejudice to that position, and in an effort to be helpful, the Applicants offer the following clarification.

It is important to understand that one principle underpinning Canadian/U.S. tax treaty rules is that income earned should only be taxed once. However, complex rules surround cross border taxation issues and some structures are more effective than others in realizing this principle of no double taxation. As can be seen from Exhibit C.2, under the present structure, there is exposure to double taxation of Union income received in the U.S. by a U.S. tax paying shareholder - Union pays tax on its profits in Canada; Spectra is exposed to tax on Westcoast Energy Inc. ("WEI") dividends in the U.S. (which includes Union dividends). Union dividends paid to WEI, by contrast, when it was the ultimate corporate owner of Union before 2002, did not attract any double taxation, nor do they now.

Further, Union has certain U.S. tax attributes that are measured by its indirect U.S. shareholder for U.S. tax accounting purposes. These attributes arise from a combination of the annual activity of Union under U.S. tax accounting rules and U.S. tax purchase accounting elections and value allocations from when Union was indirectly acquired as part of the acquisition of WEI by the U.S. parent group (now Spectra). Again, these are U.S. tax accounting rules that have nothing to do with Union's costs or Canadian tax obligations. However, due to the annual tax accounting convention applied by the U.S. tax authorities and Union's management of its regulatory debt/equity structure through regular equity distributions, full access to all favorable U.S. tax attributes associated with Union is difficult to obtain, such that double taxation of the group can occur. The proposed structure will permit accelerated access to U.S. favorable tax attributes to minimize U.S. shareholder taxes in the U.S. over some period of time.

Within this context, specifically, Exhibit C.2 is not a representation that Spectra "will realize 35¢ from every dividend dollar which emanates from" Union, as characterized by the CME. The measurement of U.S. taxes is not a simple matter given that WEI represents a non-U.S. subsidiary group with multiple operating subsidiaries (i.e., not just Union). Exhibit C.2 is simply illustrative of how the proposed structure provides Spectra with more control over the timing of when Union's dividends are moved to WEI. A consequence of the limited partnership structure may be to enable the distribution of Union dividends to be timed with the distributions of other operating subsidiaries so as to achieve minimal cross border double taxation. However, it should be understood that this is only a tax deferral which may or may not, depending on many assumptions that must be made in estimating the impact on any particular year or series of years, result in the partial or complete elimination of double taxation.

Similarly, the reference in Exhibit D.7 to C$50 million is a potential global amount of benefit that might be achieved through the timing of non-regulatory loss carry forwards for U.S. tax accounting purposes. These U.S. loss carry forwards result from the premium over book value (goodwill) paid by Duke (now Spectra) on the WEI acquisition in 2002. The good will is Spectra's goodwill and has no impact on Union or its customers.