Alberta Energy and Utilities Board Miscellaneous Rates Non-Routine Order U2005-102

MADE at the City of Calgary, in the Province of Alberta, on 7th day of March 2005.	ALBERTA ENERGY AND UTILITIES BOARD

AltaGas Utilities Inc. Debentures Application	Application No. 1376589

1 INTRODUCTION

On December 17, 2004, AltaGas Utilities Inc. (AltaGas or AUI) filed an application (#1376589) with the Alberta Energy and Utilities Board (EUB or the Board) requesting approval to issue to AltaGas Utilities Holdings Inc. (AUHI) the following three debentures:

1. 6.06% debenture in the principle amount of $10,000,000;
2. 5.88% debenture in the principle amount of $10,000,000; and
3. 5.82% debenture in the principle amount of $10,000,000.

In the Application, AltaGas submitted that the debentures were necessary to help maintain the appropriate level of capital structure and support capital investment and further, that the debenture issue would complete the financing requirement as approved in Decision 2004-063.

On May 1, 2004, AltaGas Services Inc. (ASI) reorganized its business into AltaGas Income Trust (AIT). AIT, AltaGas Holding Trust, AltaGas Holdings Inc. and AltaGas Operating Partnership (AOP) hold directly or indirectly all of the assets, liabilities and businesses owned by ASI. AUI is an indirect operating subsidiary of AIT. AOP owns all the common shares of AUHI and AUHI owns all of the common shares of the AUI.

Prior to its reorganization, ASI entered into three swap transactions:

1. Swap transaction dated with effective date May 16, 2003 with a notional amount of $10,000, 0000 at a fixed rate of 4.1875% maturing on May 16, 2008, plus stamping fees of 1.875% and issuance costs of .168%.
2. Swap transaction dated with effective date May 22, 2003 with a notional amount of $10,000, 0000 at a fixed rate of 4.00% maturing on May 22, 2008, plus stamping fees of 1.875% and issuance costs of .168%.
3. Swap transaction dated with effective date May 29, 2003 with a notional amount of $10,000, 0000 at a fixed rate of 3.945% maturing on May 29, 2008, plus stamping fees of 1.875% and issuance costs of .168%.

AUI submitted that the issuance costs of .168% assumed in connection with swaps was compatible to the issuance costs associated with the existing 7.28% Debenture to AUI (in the principle amount of $30,000,000 issued to AUI by AUHI with an effective date of December 15, 2000).

AUI submitted that debentures are to be issued by AUHI to AOP in the amount of $30,000,000. The interest rates payable by AUI, in the Application, are equal to the interest rates payable by AUHI to AOP. Based on the utilization of the swap transactions entered into by ASI, AUI has established deemed debentures at the same fixed rates as the ASI swap transactions plus issuance costs and stamping fees. AUI's deemed debentures mature on the same dates as the ASI swap transactions.

On January 19, 2005, the Board issued a Notice of Application inviting interested parties to register their objections, if any, by January 25, 2005. The Board further advised interested parties that in the event no bona fide objections were received by this date that the Board would proceed to process the application without further notice.

On January 25, 2005, the Board received an intervention from the Municipal and Gas Co-op Interveners (MGCI), and a joint submission from the Alberta Irrigation Projects Association (AIPA) and the Consumers' Coalition of Alberta (CCA) regarding AUI's Application. No other signatories to the memorandum of agreement (MOA) provided submissions on AUI's debenture application.

The Board notes that the MGCI did not oppose the Application, rather MGCI suggested it appeared to be consistent with Board Decision 2004-063 and the MOA approved therein.

2 BACKGROUND

In Decision 2004-063, the Board approved the MOA and Negotiated Settlement (Settlement) reached between AltaGas and customers for the 2003/2004 General Rate Application Phase I. As part of the Settlement, AltaGas agreed that $30 million of debt would be deemed to be in place commencing January 1, 2003 and would continue to be accessible for AltaGas financing for a period of five years, maturing on December 31, 2007. In support of the MOA the cost of the new debt was set at 6.0%. AltaGas undertook to issue actual new debt, maturing in 2007. Upon completion of the issuance of the new debt, the actual interest rate for the new debt would be used in determination of the final revenue requirement. Regardless of the interest rate at which the debt was actually placed, for ratemaking purposes the cost of the new debt would not exceed 6.0% over 2003 to 2007.

3 VIEWS OF THE PARTIES

CCA/AIPA

CCA/AIPA submitted comments in respect of four matters: (1) stamping fees and issue costs; (2) timing of the new debt; (3) creation of the AIT; and (4) the impact of the new debt on Revenue Requirement.

Stamping Fees/Issue Costs
CCA/AIPA noted that the stamping fee for a letter of credit for a non-investment grade entity similar to AUI would be approximately 187.50 basis points, based on a letter dated December 16, 2004 from RBC Capital Markets.

CCA/AIPA argued that stamping fees are typically associated with short-term paper such as issuance of banker's acceptance (one to three months), not with an issuance of long term debt. CCA/AIPA further noted that the swap transactions were all dated May 2003 while the estimate of the stamping fee was December 16, 2004. Consequently, CCA/AIPA submitted that if the Board deemed the concept of stamping fees to be acceptable, the appropriate rate should be that which prevailed as at May 2003.

CCA/AIPA also suggested that there may be double counting in including both the stamping fees as well as issue costs. CCA/AIPA noted that the combined stamping fees and issue costs amounted to 2.043% (1.875% plus 0.168%). This combined rate was more than half of the stated interest rate of 3.945% for the May 29, 2003 issue, and about half of the stated rates of the other two deemed debentures.

Timing of New Debt
CCA/AIPA noted that AUI's deemed debentures were raised in May 2003, with fixed rates between 3.945% and 4.1875%. CCA/AIPA assumed that these fixed rates were reflective of the debt cost applicable at that time period. CCA/AIPA noted that rates have decreased since May 2003 and therefore, CCA/AIPA argued that since the Application is dated December 2004, it would be more appropriate to have debt costs referenced to prevailing rates for an entity with a debt rating of AIT.

Creation of AIT
CCA/AIPA noted that on May 1, 2004, ASI reorganized its business into AIT. CCA/AIPA suggested that if, as a result of the creation of the income trust, there were beneficial aspects in terms of obtaining financing, such benefits should be passed on to the customers of AUI.

Impact of New Debt on Revenue Requirement
CCA/AIPA noted that Section 2(h) of the MOA dated March 23, 2004 indicated that for ratemaking purposes the cost of the new debt would not exceed 6.0% over the period 2003-2007. In addition, if new debt was not issued in 2004, the MOA provided that a Debt Cost Reserve Account would be created for revenues received over and above the cost of short-term debt in place since January 1, 2003 and the funds in the Reserve Account would be returned to customers. CCA/AIPA argued that AUI has not raised new debt as contemplated by the terms of the MOA and therefore, the Board should direct AUI to provide the build-up of funds in the Debt Cost Reserve Account since January 1, 2003 and the balance in this account should go to the account of customers.

In the event the Board agreed with AUI that this application met the definition of new debt as contemplated in the MOA approved by the Board, CCA/AIPA submitted that a further process[1] was needed to examine the need for and quantum of the stamping fees, reasonableness of issue costs, appropriateness of deeming long term debt rates prevailing in May 2003 as being applicable in 2004, and the impact of the creation of AIT on financing costs for new debt raised by AUI in 2004.

AUI

1 CCA/AIPA suggest information requests are required and a written Argument/Reply following receipt of responses.

AUI argued that CCA/AIPA's submission related to Phase 1 revenue requirement issues and appeared to not take issue with Board approval of the actual issuance of the debentures. AUI submitted that the Board should approve the application as filed, with CCA/AIPA's submission to be addressed in AUI's next GRA. With respect to the specific issues raised by CCA/AIPA, AUI provided the following reply.

Stamping Fees and Issue Costs
AUI submitted that stamping fees are properly part of the all-in cost of long-term debt, under a swap arrangement as they represent fixed rates assessed by banks based on credit quality of the borrower, and do not fluctuate between periods. AUI also indicated that the inclusion of stamping fees and issuance costs does not represent any form of double counting, as stamping fees relate to the credit risk of the borrower which, over the long term, may be subject to market conditions, whereas issuance costs are hard costs incurred for the financing transaction. Finally, AUI advised that with respect to the concern expressed by CCA/AIPA regarding the percentage of the total rate that was comprised of stamping fees and issue costs, it was not uncommon to see transactions of this nature given the low interest rate environment in 2003 and 2004.

Timing of New Debt
AUI disagreed with CCA/AIPA's suggestion that stamping fees should reflect the rate that prevailed in 2003 rather than 2004. AUI advised that there was no need to make any adjustment for date as stamping fees are fixed rates assessed by banks based on the credit quality of the borrower. Since there has been no material change in the credit quality of AUI over this period, any suggestion to change the stamping fee would be unfounded.

Creation of AIT
AUI submitted that the debt was issued by ASI and that the credit rating of both ASI and AIT was BBB (low), with little difference in capital market access. As such, there is no impact.

Impact of New Debt on Revenue Requirement
AUI noted that the CCA/AIPA argued that since AUI was accessing debt in 2004 that was initially obtained by its parent in 2003, that AUI had not acquired new debt under the terms of the MOA. AUI also noted CCA/AIPA's submission that the difference between the revenues received and cost of short-term debt in place since January 1, 2003, should be returned to customers.

AUI argued that there was no basis for this suggestion. AUI argued that the new debt was issued prior to the end of 2004, as per the terms under the MOA.

4 BOARD FINDINGS

The Board is empowered under Section 26(2)(a)(ii) of the *Gas Utilities Act* to approve the issue of indebtedness.

Pursuant to Decision 2004-063, the Board approved the MOA and Settlement reached by AUI and its customers for the 2003/2004 General Rate Application Phase I.[2] The Board notes that the

[2] AUI reached the Settlement and MOA on the Phase I portion of its 2003/2004 GRA with the following customer groups: Alberta Urban Municipalities Association (AUMA), Consumers Coalition of Alberta, Municipal & Gas Co-op Intervenors, and the Energy Users Association of Alberta (collectively, the Customers).

CCA and AIPA are the only signatories to the 2003/2004 Phase I Settlement that oppose AUI's debenture application. The views of CCA/AIPA were previously summarized in this Order.

The Board notes that as part of the Settlement, the cost of new debt for ratemaking purposes was not to exceed 6%. The Board also notes that AUI agreed that in the event the new debt was not issued in 2004, a Debt Cost Reserve Account would be created for revenues received over and above the cost of short-term debt in place since January 1, 2003 and the funds in the Reserve Account would be returned to customers.

The Board considers that AUI's debenture issues to AUHI, utilizing an existing swap transaction, do not appear to be unreasonable. However, in light of the concerns raised by CCA/AIPA, the Board is not prepared to approve the Application in its entirety. Rather, the Board considers that it is only appropriate to approve the issue of the AUI debentures to AUHI, and to defer consideration of the other issues raised by CCA/AIPA. Such approval would not prevent AUI from completing the proposed financial transactions, but would defer the review of how the consequences of the Application should be reflected in AUI's revenue requirement. The Board considers that these matters should be more fully explored at the upcoming AUI GRA.

Based on the aforementioned, the Board approves AUI's three debenture issues to AUHI.

5 ORDER

THEREFORE IT IS ORDERED THAT:

1) The Board hereby approves AltaGas Utilities Inc.'s request to issue to AltaGas Utilities Holdings Inc. the following three debentures as described in the Application:

- 6.06% debenture in the principle amount of $10,000,000;
- 5.88% debenture in the principle amount of $10,000,000; and
- 5.82% debenture in the principle amount of $10,000,000.

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