

National Energy Board

TransCanada PipeLines

2001 and 2002 Fair Return Application

Hearing No. RH-4-2001

Written Evidence Of John McCormick

on Behalf of

the Canadian Association of Petroleum Producers

January 21, 2002

J. D. McCormick Financial Services, Inc.
Suite 2400
645 7 Avenue South West
Calgary, Alberta T2P 4G8

1 **Q.1 Please state your name, business address and occupation?**

2 A My name is John D. McCormick, and my business address is Suite 2400, 645
3 7th Avenue South West, Calgary, Alberta. I am a financial consultant and
4 President of J. D. McCormick Financial Services, Inc. A description of my
5 professional qualifications is found in Attachment 1.

6 **Q.2 What is the purpose of your evidence at this proceeding?**

7 A The Canadian Association of Petroleum Producers (“CAPP”) has requested that I
8 provide an opinion with respect to market response to the ROE adjustment
9 mechanism and the allowed capital structure for the Mainline.

10 **Q.3 Have you ever given evidence in a regulatory proceeding?**

11 A. Yes. In 2001, I was retained by the Alberta Energy and Utilities Board (“AEUB”)
12 as an independent financial expert to give evidence at the 2000 Pool Price
13 Deferral Accounts Proceeding.¹ The 2000 Pool Price Deferral Accounts
14 Proceeding was convened to permit the AEUB to determine the amount payable
15 to the owners of six electrical distribution systems in respect of the prudent cost of
16 financing of the deferral accounts, which in aggregate were approximately \$632
17 million. Pursuant to the relevant regulation, the prudent cost of financing of the
18 deferral accounts could include the costs of “debt financing, equity financing or a
19 combination of debt and equity financing.”² My duties included, among other
20 things, analysis of the applications, and; filing a written submission on the prudent
21 financing options, cost of financing, impact of debt financing on capital structure
22 and the impact of the cost of financing for other corporate purposes.

23 **Q.4 Was the evidence prepared by you or under your direct supervision and**
24 **control?**

25 A Yes.

1 **Q.5 Please summarize your conclusions.**

2 A The combination of the current equity return resulting from the adjustment
3 mechanism and the allowed capital structure appear to be appropriate to the
4 financial markets, relative to the market's perception of the Mainline's business
5 risk.

6 **Q.6 What facts do you rely on to support this conclusion?**

7 A The best evidence of the appropriateness of the current equity return resulting
8 from the adjustment mechanism and the allowed capital structure is found in the
9 prices at which securities of TransCanada trade in the market.³ The common
10 shares of TransCanada, the public entity that investors must buy to participate in
11 owning the Mainline, are trading at a material premium to book value.⁴ The senior
12 debentures of TransCanada are rated as "A" and are trading at spreads over the
13 comparable government bonds of similar term within the range of other similarly
14 rated credits.^{5 6}

15 **Q.7 Do you agree that TransCanada need be awarded a return on the Mainline
16 based on an ATWACC of 8.24%?⁷**

17 A No, I do not.⁸ The ROE resulting from the adjustment mechanism on the 30%
18 equity layer appears to be well within the range of what the market requires.

19 In their evidence as to the effective ROE of a 7.5% ATWACC, TransCanada
20 advises that the equivalent on a deemed 40% equity basis would be 12.52%.⁹
21 Since the Mainline has an approved 30% equity layer, the requested ROE will be
22 materially higher.¹⁰ In their response to IR-CAPP-28, they calculated that this
23 would equate to an ROE of 15.35% on a 30% equity layer.¹¹ TransCanada,
24 though, has requested an ATWACC of 8.24%.

25 The effect of awarding the Mainline, in mid 2002, a return of 12.5% on a 40%
26 common equity layer for the years 2001¹² and 2002¹³ appears to result in a large

1 bonus to existing equity holders and would compensate TransCanada for an
2 equity layer that was not in place.

3 For the sake of contrast between the TransCanada implicit request for a 15.35%
4 ROE on the 30% equity layer, I compared that request to the allowed returns of
5 two newer pipelines, Alliance and Maritimes & Northeast. In Canada, Alliance is
6 allowed 11.3% on its 30% equity layer and in the U.S. it is allowed 10.7% ROE.¹⁴
7 Maritimes & Northeast is allowed a 13% return on its 25% equity layer for its
8 first 5 years ending in 2004.¹⁵ These rates of return were determined in the
9 recognition that Alliance and Maritimes & Northeast were new pipelines facing
10 different risks.¹⁶ I would also observe that TransCanada is one of several pipelines
11 for which the ROE may be determined by the adjustment mechanism.¹⁷

12 **Q.8 Do you agree that “changes in the competitive environment, combined with**
13 **developments in financial markets, warrant an increase in the fair return of**
14 **the Mainline”?**¹⁸

15 A No, I do not. It is, of course, very difficult to say for a certainty what the market is
16 expecting out of these proceedings.¹⁹ TransCanada, the public entity which owns
17 the Mainline, is followed by a host of equity analysts,²⁰ several bond rating firms
18 and thousands of investors²¹ and potential investors, all of whom to some degree
19 make up the “market” and affect securities prices with their behavior. The
20 “market” has been aware of the development of other pipelines for years.²² The
21 “market” is made aware of the economic and political developments with a host
22 of communication options. The “market” is aware of the return to which the
23 Mainline is entitled for 2001 and 2002 under the adjustment mechanism.²³ The
24 “market” is aware of a host of alternative investment opportunities in both
25 pipelines and other industries in Canada and internationally and with all this
26 knowledge still awards TransCanada a large premium over its book value.²⁴

1 **Q.9 Is it correct to use the prices of TransCanada securities as a guide for**
2 **determining whether the allowed return of the Mainline is adequate in light**
3 **of the business risks that Mainline faces?**

4 A Since TransCanada, the public entity which owns the Mainline, owns other
5 businesses the view that we may obtain of the required returns from the prices of
6 securities is a little blurred by the inclusion of those other businesses within the
7 financing entity. Those other businesses have included both regulated and
8 unregulated²⁵ businesses. To the extent that the regulated businesses have returns
9 that move in parallel with the returns allowed on the Mainline, there is little
10 blurring.²⁶ To the extent that the proportion of unregulated business increases
11 relative to the regulated businesses and the unregulated businesses have returns
12 that vary²⁷ from the returns allowed on the Mainline, there is more blurring.
13 Fortunately, the relative size of the unregulated businesses within the financing
14 entity has been reduced in recent years. Securities prices are the best evidence of
15 the market reaction to TransCanada's expected relative returns. While it would be
16 ideal if the Mainline were in a separate financing vehicle so as to remove any
17 blurring, it remains the largest asset and is therefore a major driver of
18 TransCanada's results.

19 **Q.10 Where do bond ratings fit within your analysis?**

20 A Bond ratings are one of many sources of information available to the market on an
21 issuer's securities. Bond ratings provide the market with an independent
22 assessment or measure of the relative probability that the debt of the various
23 issuers will be repaid in accordance with the terms of the instruments. The rating
24 could be viewed as a proxy for an assessment of business risk and financing risk.
25 Each instrument has a position within the capital structure of the firm.
26 TransCanada's outstanding First Mortgage Pipe Line Bonds²⁸ are clearly at the
27 top on the heap in terms of security of repayment. The various classes of
28 unsecured debt would obviously rank below, each in accordance with its priority.

1 **Q.11 Are the American precedents of companies allowed higher rates of return**
2 **and higher equity layer relevant?**

3 A To the extent that TransCanada competes with companies for debt and equity
4 capital, allowed returns on the regulated portion of each company's businesses are
5 of interest, but are only part of the picture. The prospective returns of the
6 unregulated business, the relative proportion of regulated and unregulated
7 businesses, and the capital structure of each firm will also be of interest to
8 prospective investors.

9 Witnesses for TransCanada have drawn the Board's attention to a number of
10 American based pipeline and energy companies.²⁹ They have pointed out that
11 these companies are allowed a higher rate of return on a larger equity layer in
12 respect of pipeline operations than the equity return and equity layer which has
13 been allowed to the Mainline. This information does not give the Board the full
14 picture. They have omitted, among other things, the debt ratings of the
15 comparable companies. I observed that the debt instruments of several of the
16 companies discussed to support the proposition of higher returns on higher equity
17 layers had debt ratings differing from those of TransCanada. Without a detailed
18 examination of the covenants of each of the instruments rated and the capital
19 structure of each company, it is hard to attempt to explain the variation of rating,
20 but as the table below shows, several of the companies identified as comparable
21 have debt ratings lower than those of TransCanada. As such, in the view of the
22 rating agencies, the probability of repayment on those debt instruments varies
23 from those of TransCanada's. For that reason, I infer that there are elements of
24 business and financial risk that differ from those faced by holders of like
25 instruments issued by TransCanada.

<u>Company</u>	<u>Moody's Rating</u>	<u>S&P Rating</u>
Duke Energy ³⁰	A1	A+
Columbia ³¹	A3	BBB
El Paso /Coastal ³²	Baa2	BBB
Enron ³³	Ca	D
Kinder Morgan	Baa2	BBB
TransCanada	A2	A-
Williams	Baa2	BBB

1 **Q.12 Are there companies which you consider to be more comparable to**
2 **TransCanada on the debt side?**

3 A Yes. In light of the size of the Mainline's debt requirements during the 2001-2002
4 period, it appears the Canadian market will be more than adequate for the
5 Mainline's needs. On the Canadian side, I compared some of the outstanding
6 TransCanada debt issues with a number of similarly rated obligations and found
7 that TransCanada's instruments were trading at comparable yields to maturity. As
8 such, it did not appear to me that investors were shunning TransCanada's debt
9 securities.

10 **Q.13 What is more important an "A" rating or a 2 times interest coverage ratio?**

11 A Of the two, I would view the "A" rating as more important. I would observe that
12 TransCanada has been able to maintain an "A" rating without maintaining a 2
13 times interest coverage ratio.³⁴ Neither of those items is as important as the
14 "market" reaction to the financial position of the company. A company's debt
15 securities do not always trade in line with the bond rating.

16 To propose a minimum target interest coverage ratio effectively makes the equity
17 return a function of the weighted average cost of the existing Mainline debt issues
18 and the current tax rate. The table below provides interest coverage numbers for a
19 simplified example of a 70% debt and 30% common equity capital structure using
20 a 41.7% tax rate for a range of interest and equity return rates.³⁵ To maintain a 2
21 times interest coverage ratio as the imbedded average debt costs increase from 7%
22 to 11%, the after-tax equity return must increase from approximately 250 basis

1 points greater than the average imbedded debt rate to 400 basis points greater than
2 the average imbedded debt rate. Were we to use a 38.28% tax rate, the after-tax
3 equity return must increase from approximately 310 basis points greater than the
4 average imbedded debt rate to 485 basis points greater than the average imbedded
5 debt rate as the imbedded average debt costs increase from 7% to 11%.

6

Rate Base	\$ 1,000		Pre Tax	Pre Tax
Tax Rate	41.70%	Rate	Rate	Return
Debt	70%	10.00%	10.00%	\$ 70.00
Equity	30%	9.51%	16.31%	\$ 48.94
				\$118.94

Debt Rate	Interest Coverage						
	Equity Return						
	9.00%	10.00%	11.00%	12.00%	13.00%	14.00%	15.00%
7%	1.95	2.05	2.16	2.26	2.37	2.47	2.58
8%	1.83	1.92	2.01	2.10	2.19	2.29	2.38
9%	1.74	1.82	1.90	1.98	2.06	2.14	2.23
10%	1.66	1.74	1.81	1.88	1.96	2.03	2.10
11%	1.60	1.67	1.74	1.80	1.87	1.94	2.00
12%	1.55	1.61	1.67	1.74	1.80	1.86	1.92
13%	1.51	1.57	1.62	1.68	1.74	1.79	1.85
14%	1.47	1.53	1.58	1.63	1.68	1.74	1.79

7 **Q.14 Have you any observations on TransCanada's Mainline financing calendar?**

8 A Yes. Compared with a number of historic periods in which TransCanada accessed
9 the capital markets, TransCanada's near term financing requirements for the
10 Mainline appear extremely light.³⁶ In the response to NEB 1.18(b), TransCanada
11 advises that it "does not expect to refinance any of the Mainline's debt that will
12 mature in 2001 and 2002."³⁷ Capital expenditures for the Mainline for 2001 and
13 2002 appear to be in the order of \$188 million³⁸ with approximately \$106 million
14 in 2001 and \$82 million estimated for 2002.³⁹ Depreciation for the Mainline
15 appears to be in the order of \$341 million for 2001 and \$362 million for 2002.⁴⁰

1 **Q.15 How does the corporate TransCanada near term financing calendar compare**
2 **with its capital markets activities in the past?**

3 A While TransCanada has not put into evidence their financing plans for their non-
4 regulated business, what they have said about the plans causes me to believe its
5 near term financing calendar is relatively light. It appears that TransCanada
6 expects to repay a total of \$1.6 billion in debt to the end of the test period.⁴¹
7 Mr. Lackenbauer observed that in the 1996 to 2000 period, TransCanada raised
8 \$7.7 billion.⁴² On a percentage basis, TransCanada's near term financing calendar
9 is a small portion of the financing it undertook in the late 1970's and early 1980's
10 when it was required to fund certain payments in respect of Future Gas Supply. In
11 1980, for example, TransCanada was required to finance \$465 million in
12 additional payments in respect of Future Gas Supply at a time when its 1979
13 balance sheet closed the year with \$2.5 billion in assets. At the end of 1980, the
14 \$832 million of payments in respect of Future Gas Supply represented 32% of the
15 other assets on the TransCanada balance sheet. At the end of 1981, TransCanada
16 had financed \$1.013 billion in payments in respect of Future Gas Supply.

17 **Q.16 Do you have a view with respect to the observation that there is there is**
18 **already a significant amount of TransCanada paper in the hands of**
19 **Canadian investors?**

20 A TransCanada is one of the largest publicly traded enterprises in Canada and as
21 such must have a significant amount of paper in the hands of investors to finance
22 its assets. As a result of the restructuring and the debt repayments, there is less
23 paper in the hands of investors now than there was several years ago. The
24 September 30, 2001 balance sheet shows long term debt of \$10.0 billion, down
25 from the December 31, 2000 amount of \$10.5 billion and down from the
26 December 31, 1999 amount of \$12.7 billion.⁴³

1 **Q.17 Do you have any comments with respect to TransCanada’s contention that**
2 **the company “is making investments today that have significantly higher**
3 **expected returns than the Mainline, with business risks that are equal or**
4 **less”⁴⁴?**

5 A I wish them well with each of their new investments. Only TransCanada can truly
6 know what is their expectation of the return and their judgment of relative
7 business risks. Unfortunately, there are many instances in which the expectation
8 of profit in new ventures is not realized.⁴⁵ Unless these investments are in a
9 regulated return area the investors will be exposing themselves to a level of
10 variation in return materially greater than an investment under regulation. In
11 1999, TransCanada booked \$524 million in after tax losses related to discontinued
12 operations.⁴⁶ I am confident that in each of the investments that gave rise to the
13 1999 losses, the decision makers approving the investment expected “significantly
14 higher expected returns than the Mainline, with business risks that are equal or
15 less.” I would also note that DBRS observed in its April 12, 2001 bond rating “the
16 Company exited some of its riskier areas of operation, which were yielding
17 disappointing results”.

18 **Q.18 Can you comment on the Duke offer for Westcoast referred to in evidence**
19 **filed on behalf of TransCanada?**

20 A I was interested in comparing the statement which suggested that U.S. pipeline
21 companies are entitled to earn and have returned to their shareholders “higher
22 earnings than their Canadian counterparts”⁴⁷, found in Mr. Gordon’s evidence,
23 with the statements about the purchase offer by Duke for Westcoast discussed in
24 Mr. Lackenbauer’s evidence.⁴⁸ Since Westcoast, in the absence of a negotiated
25 settlement⁴⁹ involving a higher or incentive rate of return, is saddled with the
26 apparently burdensome adjustment mechanism, I could not believe that the
27 synergies referred to outweigh the low rate of return on Westcoast’s NEB
28 regulated pipeline investment which Duke will acquire as part of the purchase.

1 **Q.19 Will the adjustment mechanism work well in any circumstance?**

2 A Any system created by human beings suffers from limitations, and as such, there
3 may develop in the future a confluence of events in which the current adjustment
4 mechanism would not provide an adequate return for a regulated company.
5 However, it seems clear to me that the adjustment mechanism has performed well
6 for a number of years. TransCanada has been able to access the capital markets on
7 a reasonable basis.⁵⁰ The high market to book ratio⁵¹ currently enjoyed by
8 TransCanada shareholders and the spreads⁵² at which their debt instruments are
9 trading provide tangible support for the view that the formula continues to work
10 well.

11 **Q.20 Please review your conclusions.**

12 A The combination of the current equity return resulting from the adjustment
13 mechanism and the allowed capital structure appear to be appropriate to the
14 financial markets, relative to the market's perception of the Mainline's business
15 risk.

16 **Q.21 Does this conclude your evidence?**

17 A Yes.

ATTACHMENT 1

PROFESSIONAL QUALIFICATIONS OF JOHN D. McCORMICK

Academic Training

LL.B. from the University of Alberta (1978)
M.B.A. in Accounting from the University of Alberta (1975)
B.A. in Political Science, from the University of Calgary (1972)

Professional Organizations

Law Society of Alberta

Professional Experience

September 1975 - May 1978 - Sessional Lecturer for the Department of Accounting, the Faculty of Business Administration and Commerce, the University of Alberta

June 1978 - March 1983 – Barrister & Solicitor and Articling Student, Parlee, Irving, Henning, Mustard & Rodney, Edmonton

September 1980 - May 1982 - Sessional Lecturer (M.B.A. Tax) for the Department of Legal and Industrial Relations, the Faculty of Business Administration and Commerce, the University of Alberta

March 1983 - October 1991 – Associate rising to Vice-President and Director, ScotiaMcLeod, Toronto and Calgary

In this capacity, Mr. McCormick represented the firm in transactions ranging from small private placements to major financings including the initial public offerings of Telus and Petro-Canada. The transactions included the issuance of preferred and common shares, special warrants, rights, warrants, partnership units, and trust and royalty units . . . domestic deals and crossborder financings. He executed approximately \$5 billion of financing, wrote five trust deeds for major borrowers in the energy industry covering secured and unsecured obligations in the domestic and European markets, and assisted a major airline to renegotiate the terms of its convertible debentures with key financial institutions. In the utility area, he provided coverage of a number of western Canadian utility issuers including Nova, Alberta Natural Gas and Foothills Pipe Lines. He developed expertise in a number of industries including Canadian energy and petroleum services, pipelines, basic and specialty chemicals, airlines, pulp and forest products, telephone and telecommunications, and magnesium.

November 1991 – January 1994 – President, J. D. McCormick Financial Services, Inc., Calgary

January 1994 – January 1997 – Vice-President & Director, Levesque Beaubien Geoffrion, Calgary

In this capacity, Mr. McCormick was responsible for account coverage of over 125 account relationships in Alberta, British Columbia and Saskatchewan. He gained additional expertise in the banking, gold and satellite communications industries.

January 1997 – October 1997 – President, J. D. McCormick Financial Services, Inc., Calgary

October 1997 - May 1998 – Sprott Securities, Calgary

May 1998 – present – President, J. D. McCormick Financial Services, Inc., Calgary

In this capacity, Mr. McCormick secured and executed valuation and financial advice assignments with junior and senior public companies and government. He recently assisted a senior issuer in a securitization transaction. He provided financial advice with respect to the recapitalization of Sunoma and Barrington, which had over \$400 million in debt, fairness opinions to directors of TSE, CDNX and ASE listed companies. He provided financial advice in respect of several oil and gas industry merger and acquisition assignments, including advice to Tappit in respect of its attempted \$13 million hostile takeover of Backer, and expert testimony or reports in three securities cases in Alberta and Saskatchewan. Among other things, he was retained to provide, strategic advice with respect to several corporate reorganizations, a valuation of a U.S. corporation with equity valued at over \$200 million and strategic advice to its owner, advice in respect of a \$15 million equity financing, the negotiation of a long term joint venture, disposition of an oil services firm, and, advice in respect of software company concerning a private placement by a major industry partner.

Previous Expert Reports

Mr. McCormick was retained by the Alberta Energy and Utilities Board to give evidence at the 2000 Pool Price Deferral Accounts Proceeding, which resulted in Decision 2001-92. He has provided expert reports in respect of a number of lawsuits related to securities matters.

Notes to J. McCormick Evidence:

¹ See the various decisions related to the proceedings including Alberta Energy and Utilities Board Decision 2001-92. In addition to written evidence, Mr. McCormick was examined on July 27, 28, and 30, 2001.

² See section 4 of the Deferral Accounts Deficiency Correction Regulation, Alberta Regulation 240/2000.

³ In response to CAPP 5(c), TransCanada noted, “Based on the recent performance of TransCanada’s common shares and the credit spreads on its debt, one can conclude that demand for these securities has increased.”

⁴ In response to CAPP 126(b), TransCanada has supplied certain data on market to book on a quarterly basis from 1Q94 to 3Q00. The particular method used to calculate the data supplied was not provided in CAPP 126(b). IGUA 11.2 provides the December 29, 2000 market to book, 1.56. Additional data for 2001 was included in CAPP 101(f) 1Q01 1.72; 2Q01 1.70; 3Q01 1.82. The average of the data points from 1994 to 3Q01 is 1.56. I observe that throughout the first portion of the test period, TransCanada has traded at market to book ratios that are generally above the average of such ratios for the period since 1994. See also IGUA 7.2 for the market to book ratio as at December 7, 2001, 1.72 times. See also IGUA 11.2 for the market to book ratio as at November 30, 2001, 1.78 times.

⁵ In response to CAPP 101(g), TransCanada has supplied certain data on spreads of unspecified 10 Year bonds of Enbridge, TransCanada and Westcoast for various dates, the latest of which shows TransCanada trading at spreads 6 basis points greater than Enbridge and 17 basis points greater than Westcoast. Recent trading in Westcoast securities may be affected by the offer for Westcoast by Duke. During the 2001 period for which data was provided the spread between the Enbridge and TransCanada ranged from 23 basis points to minus 2 basis points. During the 2001 period for which data was provided the spread between the Westcoast and TransCanada ranged from 22 basis points to minus 2 basis points.

⁶ In response to ADOE 1.57, TransCanada observes, “Spreads generally widen out before downgrades occur because the debt markets respond more quickly to changes in circumstances than do the rating agencies.” The data provided in response to CAPP 101(g) on spreads for TransCanada bonds for the most recent date set out therein is lower than those spreads that prevailed in June of 2000.

⁷ Written Evidence on Investment Perspectives, June 2001, Page 3 of 16, Answer 3, line 19.

⁸ In its response to ADOE 1.55, TransCanada advises that even with an ATWACC lower than 7.5%, “financing would likely continue to be sourced under similar conditions in the short-term.” While the concept of “short-term” is not defined in that response, in what may be a different context, the concept of “longer-term” is explained in ADOE 1.35 as referring to “beyond 2005”. In CENTRA 1, the words “short term” are described in a manner that “would include the test period”, but appear not to be limited to the test period.

⁹ Written Evidence on Investment Perspectives, June 2001, Page 7 of 16, Answer 8, line 2.

¹⁰ In response to NEB 1.39(a), TransCanada calculated a 14.84% return on equity on a 31.33% equity structure.

¹¹ In response to CAPP 122(a), TransCanada calculated a 15.31% return on equity on a 30% equity structure, using a 7.12% debt cost and a 41.699% tax rate and a 7.5% ATWACC. See also CAPP 19 (c).

¹² In response to IGUA 21.1, TransCanada advises “the return related increase for 2001 between the Board’s ROE formula of 9.61% on 30% and 12.5% on 40% is \$267.9 million or approximately 58% consisting of the change in equity return, associated income tax and pre-funded debt return.”

¹³ In response to IGUA 21.2, TransCanada advises “the return related increase for 2002 between the Board’s ROE formula of 9.53% on 30% and 12.5% on 40% is \$244.6 million or approximately 58% consisting of the change in equity return, associated income tax and pre-funded debt return.”

¹⁴ Alliance Pipeline Limited Partnership, Bond Rating DBRS, November 14, 2001, page 2. See also the information in reply to IGUA 10.9 which suggests the Alliance ROE for 2002 will be 11.25% and CAPP 47(a).

¹⁵ Maritimes & Northeast Pipeline Limited Partnership, Bond Rating DBRS, June 29, 2001, page 3. See also the information in reply to IGUA 10.9.

¹⁶ In response to ADOE 1.52 TransCanada acknowledges certain of the risks faced by new pipelines and some particular aspects of the Alliance arrangement.

¹⁷ The RH-2-94 Decision also covered Alberta Natural Gas Company Ltd, Foothills Pipe Lines Ltd., Trans Mountain Pipe Line Company Ltd., Trans Quebec & Maritimes Pipeline Inc. and Westcoast Energy Inc.

¹⁸ Additional Written Evidence of TransCanada PipeLines Limited, November 2001, Page 3 of 9, Answer 3, lines 3 to 5.

¹⁹ In response to IGUA 7.4, TransCanada advises, “there is no specific objective source that can provide the definitive answer to the question of investor return expectations”.

²⁰ On October 30, 2001 and January 16, 2002, the TransCanada web site showed 11 Canadian based and 2 US based analysts as providing research on TransCanada. In NEB 1.36, TransCanada refers to 12 analysts.

²¹ Page 75 of the TransCanada annual report for 2000 shows 30,758 registered shareholders. In response to IGUA 6.1 TransCanada updates that number to November 30, 2001. Registered shareholders represent a fraction of the total shareholders since many shareholders will own their shares through accounts registered with an investment dealer.

²² In the RH-2-94 decision that gave rise to the current adjustment mechanism, the Board observed at page 8, that “TransCanada noted that it can no longer be viewed as a monopoly with respect to deliveries to eastern Canadian markets since it faces increased competition from alternative pipelines and supplies, including U.S.-sourced supply. TransCanada pointed out that eastern Canadian local distribution companies (“LDCs”) are diversifying their gas supply portfolios to include, in some cases, up to 30% U.S.-supplied gas and are proposing new pipeline facilities to connect their franchise areas with U.S. supply and storage facilities.”

Among other proposals, applications and decisions throughout the period, on July 3, 1997, Alliance Pipeline Ltd. applied for the necessary certificates and authorizations to construct the Alliance Pipeline which was authorized in decision GH-3-97 issued in November 1998. In response to ADOE 1.38, TransCanada quotes a passage from that decision in which “the Board recognizes that the approval and construction of the Alliance Pipeline Project could result in pipeline capacity leading supply for a period of time.”

²³ On December 8, 2000, the National Energy Board announced the approved rate of return on common equity of 9.61% for the year 2001 and on December 6, 2001 announced the approved rate of return on common equity of 9.53% for the year 2002.

²⁴ In response to IGUA 11.2, TransCanada calculates its market to book ratio as at November 30, 2001, as 1.78 times.

²⁵ In response to ADOE 1.59, TransCanada advises that the “unregulated business of TransCanada represents less than 10% of the total assets of the Company.” In response to CAPP 210, TransCanada advises that the non-regulated businesses “do not have a material impact on TransCanada’s consolidated financial fundamentals”. In response to MIRANT 2(b), TransCanada identifies its “significant unregulated businesses”.

²⁶ Certain of TransCanada’s current pipeline investments were also part of the RH-2-94 decision, including Alberta Natural Gas Company Ltd, Foothills Pipe Lines Ltd., and Trans Quebec & Maritimes Pipeline Inc.

²⁷ In response to CAPP 101(a), TransCanada reports “the vast majority of the Company’s remaining non-Mainline assets deliver economic returns.” In response to CAPP 96(b), TransCanada calculates that as at the third quarter of 2001 the Alberta System, which has been the subject of a negotiated settlement, represents over half of the non-mainline assets.

²⁸ In 1993, TransCanada eliminated any ability to issue additional First Mortgage Bonds. See Part X Requirements, Section 33, Sheet 2 of 63 and CAPP 7(d)(i).

²⁹ Written Evidence of Richard K. Gordon, Page 26 of 29, Table 6 and 7, also page 29 of 29, line 4.

³⁰ Duke Energy Corp securities are generally rated A1 in Bloomberg data. Some of the obligations of its subsidiaries and affiliates have different ratings.

³¹ Columbia was acquired by NiSource November 1, 2000.

³² El Paso and Coastal merged in January 2001 in what the El Paso described in its 10K filing as a “\$24 billion merger”. Certain debt instruments by companies related to El Paso have different debt ratings than the parent.

³³ Enron is currently the subject of insolvency proceedings.

³⁴ In response to CAPP 29, rating reports in addition to those contained in Part X, section 36, were filed as part of the evidence in this proceeding. The face pages of the Moody’s reports show an A2 rating for the period 1994 to 1999 for TransCanada while in only one of those 6 years was a 2 times pre-tax interest coverage level achieved. The CBRS reports show A level ratings since 1990, but only one year of 2 times interest coverage for the period 1993 to 1998. The DBRS reports show net interest coverage for the period 1991 through 2000, with only one year in which TransCanada achieved a 2 times coverage level. During the period DBRS rated TransCanada’s senior unsecured debt A (high) in 1994 through 1997 and A during the balance of the period covered.

In the response to NEB 1.31(c), TransCanada provides interest coverage ratios for 1990 to 1995 which ranged from 1.65 to 1.76. In the response to ADOE 1.60, TransCanada provides consolidated interest coverage ratios for 1996 to 2000 which ranged from 1.50 to 2.33. In the response to NEB 1.31(d), TransCanada provides interest coverage

ratios for 2001 and 2002 based upon the continuation of the adjustment mechanism, which ranged from 1.64 for the year 2001 now past and 1.68 for 2002. TransCanada's DBRS bond rating was not reduced in 2001.

³⁵ Schedule 2.2 of the Fair Return Application estimates an 8.97% interest cost in respect of the outstanding debt. For simplicity in the example I have used an arbitrary rate of interest of 10% for all debt.

³⁶ In the response to CAPP 3(e), TransCanada provided data which shows that in 1998 the Mainline undertook Cdn. \$971 million and U.S. \$460 million as part of a corporate financing program of over \$2 billion. In 1997, the Mainline accessed capital markets for Cdn. \$709 million. In the response to CAPP 4(g), TransCanada reports "It is not envisioned that the Mainline will require external term debt financing in the near term". Although perhaps in a different context, in CENTRA 1, the words "near term" are described as "the period from 2001 to 2005."

³⁷ In the response to NEB 1.18(a), TransCanada advises that the "portion of debt maturing in 2001 and 2002 that is attributable to the Mainline is C\$347M and C\$279M." In response to CAPP 99(a), TransCanada estimated that \$630 million of Mainline debt would be repaid over the test period, in addition to US\$160 million in TOPrS that may be called.

³⁸ Additional Written Evidence on Investment Perspectives, Page 3 of 3, Answer 6, line 3.

³⁹ In response to CAPP 35(a), TransCanada provided a schedule of capital expenditures for the Mainline for the years 1990 to 2000. In four of the eleven years, Mainline capital expenditures exceeded \$1 billion per year. In the ten years beginning 1990, Mainline capital expenditures averaged \$839 million per year. For details on the 2001 and 2002 Mainline capital expenditures, see information in reply to IGUA 9.3. See MIRANT 12(d) for capital expenditures related to expansion commencing in 1994.

⁴⁰ See Schedule 1.0, line 8, of the material filed in reply to CAPP 17.

⁴¹ Additional Written Evidence on Investment Perspectives, Page 3 of 3, Answer 6, line 9. In contrast, in the response to CAPP 3(e), TransCanada provided data which shows that, in 1998 it undertook a debt financing program of Cdn. \$1.47 billion and U.S. \$1.06 billion. In 1997, TransCanada accessed capital markets for Cdn. \$709 million and U.S. \$293 million. In 1996, TransCanada accessed capital markets for Cdn. \$600 million and U.S. \$580 million.

⁴² Written Evidence of Gordon Lackenbauer, Page 14, Answer 18, line 4.

⁴³ The \$12.7 billion long-term debt amount is found in the original balance sheet for 1999, the comparative balance sheet for 2000 shows the 1999 long-term debt as \$12.2 billion. The amounts do not include Long-Term Liabilities of Discontinued Operations, Non-Recourse Debt of Joint Ventures or Junior Subordinated Debentures.

⁴⁴ Written Evidence on Investment Perspectives, June 2001, Page 7 of 16, Answer 10, line 20.

⁴⁵ In response to CAPP 6(d), TransCanada advises "most of its divested business were divested, in part, because realized returns did not meet TransCanada's expected return." In response to CAPP 96 (a) and (b), TransCanada sets out the percentage of EBIT and the percentage of Total Assets of the Mainline and Other business for each of the years 1994 to 2000. In each of those years the Mainline assets returned a greater proportion of the EBIT than their proportion of Total Assets. Similarly, in each of those years the Other assets returned a smaller proportion of the EBIT than their proportion of Total Assets.

⁴⁶ In response to CAPP 96(c), TransCanada listed the businesses that were considered discontinued in 1999 and in 2001, and in response to IGUA 10.2, TransCanada listed the various assets sold as part of its disposition program.

⁴⁷ Written Evidence of Richard K. Gordon, Page 29 of 29, Lines 4 through 10.

⁴⁸ Mr. Lackenbauer observes in his Additional Written Evidence, Page 5 of 7, Answer 9, line 19 that the proposed acquisition of Westcoast by Duke will be earnings accretive to Duke. Additional benefits are discussed beginning at Page 5 of 7, Answer 9, line 21.

⁴⁹ As disclosed on page 10 of the 2001 Westcoast Energy Inc. annual information form, the current negotiated settlement was approved by the National Energy Board in 1997 and is effective until December 31, 2001.

⁵⁰ See information provided in response to CAPP 3(d).

⁵¹ See information provided in response to CAPP 101(f) and CAPP 126(b).

⁵² See information provided in response to CAPP 101(g).