Sandell Group

Unlocking Shareholder Value at

Spectra Energy Corp (SE)

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Unlocking Shareholder Value at Spectra Energy Corp

Goal: Transform Spectra Energy Corp (SE) from 'Utility' to Energy Infrastructure Player

- SE is one of the largest North American energy infrastructure companies with $25bn+ of prospective investment projects, operated and perceived as a utility company
  - SE has underperformed peers by 70%+, trading at a meaningful discount due to its tax-inefficient, conglomerate structure, unnecessarily elevating its cost of capital versus an industry on the cusp of explosive organic growth
  - There are clear steps to unlocking and maximizing shareholder value through strategic/financial actions already undertaken by industry peers; in our analysis, the current FinCo + OpCo financing structure at SE does not prevent any of these steps

We estimate that an appropriate valuation for SE would be $41 to $48 per share (+32% to +55% upside) if it were to take the following steps

- Step 1: Drop-down SE's US Transmission (UST) assets into Spectra Energy Partners, LP (SEP), an MLP
  - Dropping UST into SEP would lower its overall cost of capital and be 20%+ accretive to both SE's dividend and SEP's distribution, vaulting SEP to the highest class of large MLPs (e.g., WPZ and KMP) that are widely followed and trade at premium multiples / yields to other MLPs
  - Through this step, SE would clearly target the separate MLP & 'GP HoldCo' shareholder bases, reducing the current conglomerate discount. Furthermore, SE's slate of organic growth projects would provide consistent growth for both SE/SEP's dividend/distribution
  - As shown by industry peers, the long term benefits of a lower cost of capital and the fast growing incentive distribution right (IDR) cash flow will directly accrue to the pro forma SE 'GP HoldCo' shareholders over time
- Step 2: IPO/Sell SE's Canadian operations, a fully-owned subsidiary operating as Westcoast Energy Inc. (WE)
  - By IPO'ing WE in Canada, SE can access the lower cost of capital afforded to Canadian infrastructure assets that trade at premiums given global interest in Canadian energy resources (oil sands, shale, LNG, NGLs), competitively low corporate tax rates (15%-20%) and yield-driven investors
  - We believe that an IPO of Westcoast would be oversubscribed as Canadian pension funds, mutual funds and traditional energy infrastructure investors would be attracted to its asset base, upside potential and significant market cap (~$10bn)
  - Comparable Canadian companies trade at 13x to 14x 2013 EBITDA vs. SE trading at less than 11x 2013 EBITDA
- Step 3: IPO/Sell SE's 50% stake in DCP Midstream LLC (DCP) to highlight DCP's MLP-qualifying income
  - In its current structure (where DCP is owned by tax-paying C-corps), its potential MLP-type valuation is obscured; an IPO of DCP would remove this veil
  - DCP's assets would be a natural target for other MLPs (including DPM or SEP), a transaction that would highlight the strategic value of DCP

These steps will 1) better align shareholder bases to assets, reducing SE's conglomerate discount thereby lowering cost of capital and 2) tie management incentives more directly to operational performance of assets and strategy

Unlocking Shareholder Value at Spectra Energy Corp

Spectra Energy (SE): Transformation from 'Utility' to Energy Infrastructure Player

UST / Liquids

Gulf coast to Northeast US Pipeline Infrastructure

Owns 61% of SEP (MLP)

Long term, take or pay, fee based reservation revenue (95%)

Distribution

Regulated, retail natural gas distribution in Ontario

2nd largest distributor in Canada; Dawn Storage is largest underground storage facility in North America

Western Canada

Canadian pipeline & midstream operations in BC/Alberta located in most productive shale gas fields; LNG upside

Empress NGL system exposed to NGL prices

Field Services

50% of DCP, largest US NGL producer and nat gas processor (with EPD & WMB); PSX is co-owner

40% POP, 10% KW contracts exposed to natural gas & NGL prices

M&NLP (Canadian Portion)

SEP (MLP)

<u>Drop-down all assets</u> into SEP, pushing significant future capex to lowest cost of capital entity

Increased market cap and growth trajectory will yield premium multiple

Westcoast Energy

<u>IPO/Sell</u> to garner premium multiple afforded to Canadian infrastructure assets due to global interest in Canadian energy, lower tax rates and yield-driven investors

DCP

<u>IPO/Sell</u> to garner premium multiple afforded to tax-efficient MLP which is lost in current structure with SE & PSX as tax-payers or

<u>Merge</u> with DPM/SEP or another large MLP

Unlocking Shareholder Value at Spectra Energy Corp

- SE's Sum of the Parts (SOTP) Valuation Range is $41 to $48/share (+32% to +55% upside)

- SE drop-down has successful case study
  - Williams Companies (WMB) dropped down its pipeline assets to Williams Partners (WPZ) in January 2010 with WMB owning 80% of WPZ; currently at 67% ownership
  - Given subsidiary financing structure at SE, no new debt will need to be raised and no cash to be transferred (avoiding capital gains treatment)

- WE IPO is efficient and easy to pursue
  - WE was acquired in 2002 by Duke Energy (DUK)
  - SE was spun out of DUK in 2006 with WE as a subsidiary
  - WE's debt (under Westcoast Energy Inc. and Union Gas Limited) is already at the subsidiary level

- DCP to be IPO'ed or sold
  - Crystallizes value for investors – specifically DCP's tax advantaged structure which is lost as DCP pays SE significant tax distributions
  - Motivates DCP management to operate more efficiently, grow more aggressively and better manage transition from commodity-exposed contracts to fee-based contracts

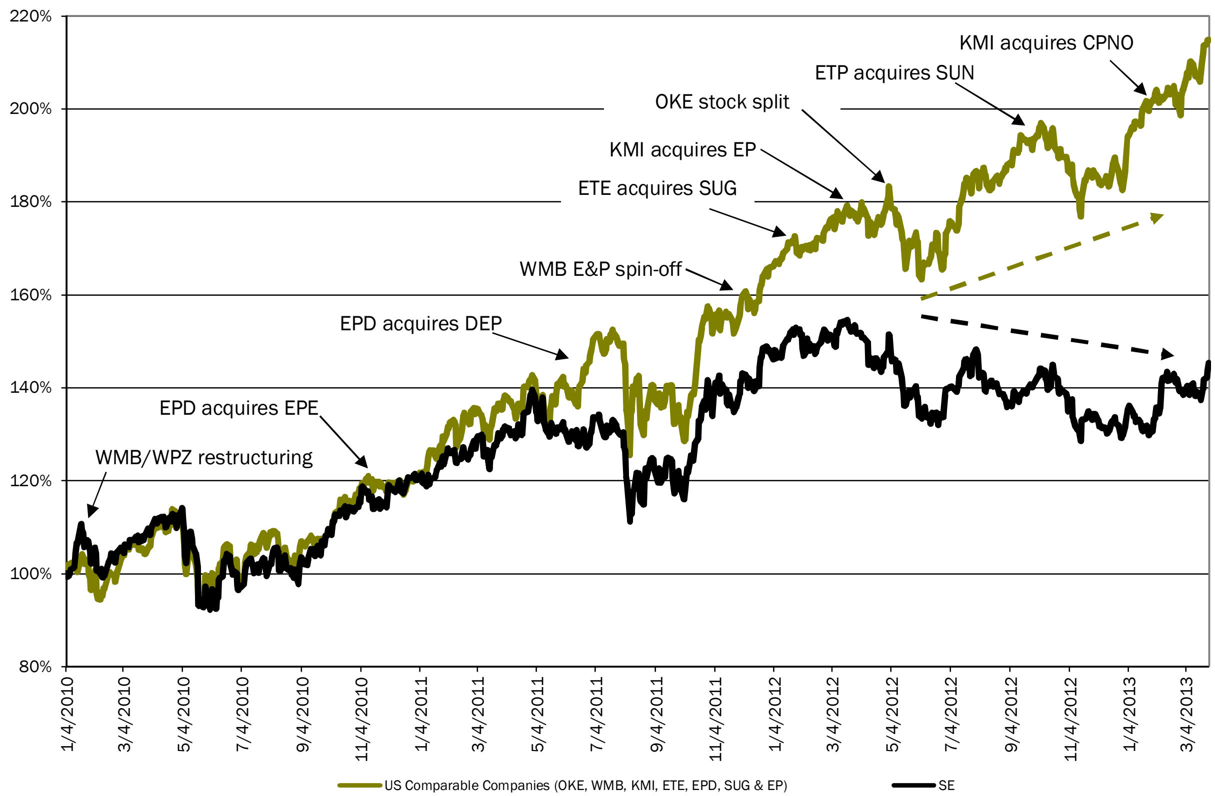
Spectra Energy Corp. SOTP Valuation*		Base Case	$ / % Uplift	High Case	$ / % Uplift
Spectra Energy Partners, LP (SEP)	LP Div / Share (1)	$2.48		$2.48	
(Full drop down of US Transmission	Yield (2)	5.4%		4.9%	
assets from SE, SEP assumes	SEP Price	$45.72		$50.35	
TET, SEC + Comml Paper,	SE shares owned (3)	187		187	
Other debt less $500m WE note)	Value of LP shares	8,565		9,433	
	IDR payment	169		169	
	GP Yield (4)	3.7%		3.7%	
	Value of IDR	4,561		4,561	
	Equity value to SE	13,126		13,994	
	per share	*$20.00*	*$5/50%*	*$21.00*	*$6/40%*
Westcoast Energy Inc. (WE)	EBITDA (5)	1,195		1,195	
(100% Canadian business;	Multiple (6)	12.6x		14.2x	
Distribution and Western Canada	Enterprise value	15,066		16,924	
segments + M&NLP)	Debt (7)	6,171		6,171	
	Equity value to SE	8,895		10,753	
	per share	*$14.00*	*$4/40%*	*$16.00*	*$6/40%*
DCP Midstream LLC (DCP)	EBITDA (8)	580		710	
(100% Field Services business,	less: interest & D+A (9)	(270)		(270)	
comprising 50% ownership	Distributable cash flow	310		440	
of DCP)	*Coverage ratio*	*1.10*		*1.10*	
	Dividend	282		400	
	Yield (10)	6.1%		5.6%	
	Equity value to SE	4,588		7,186	
	per share	*$7.00*	*$1/10%*	*$11.00*	*$5/20%*
NAV / Share		$41.00		$48.00	
% upside from current		*32%*		*55%*	

(1) Assumes dropdown of SE US Transmission assets, current IDR waterfall structure
(2) Base: SEP yield; High: assumes SEP current yield less 50bps for size premium
(3) Total PF LP shares out of 224m, SE owns 82%of the LP + 4m GP shares
(4) C-corp owned GP IDRs: Base & High: WMB div yield
(5) Distribution + Western Canada 2013 EBITDA estimates from SE, not considering M&NLP (incl in US Transmission)
(6) Base Case using 2013 TRP trading multiples; High Case using avg of TRP + ENB + KEY multiples
(7) Westcoast + Union Gas subsidiary debt + $500m SE debt + $459m pfds + CP less: M&NLP debt (cash collateralized)
(8) Base: Field Services EBITDA estimate for 2013 (NGL/bbl of 80c); High: assumes higher NGL and Nat Gas prices
(9) 2013 estimates from SE
(10) Base case: avg div yield of comps & High Case: DPM Yield
* - excl Express-Platte, Sand Hills & Southern Hills, $85m/yr of corp costs + pens underfunding of $430m in US/Can, s/o of 658m, Dec 2012 debt figures

Unlocking Shareholder Value at Spectra Energy Corp

- SE stock returns have been poor compared to comparable energy infrastructure companies with similar growth profiles
  - Stock underperformance acute over past several years as industry peers have engaged in several value-enhancing strategic actions, acquisitions, splits and spin-offs driven by low interest rate environment, strong credit conditions, desire to be tax-efficient and the targeting of specific investor criteria

Over the past year, SE has traded down 5% versus comps which were up 21% - a 26% underperformance
Over a 3 year period, SE's underperformance has been much more dramatic – 72% below comps



Absolute Price Performance

	Comps	SE	Diff
1 YR	21%	-5%	-26%
2 YR	57%	12%	-46%
3 YR	106%	34%	-72%

Step 1: Drop down SE's US Transmission assets to Spectra Energy Partners, LP (SEP), an MLP

- Dropping US Transmission assets into SEP yields SE value of $20-$21/share
  - Drop down of SE US Transmission assets into SEP would allow SE to benefit from SEP's lower cost of capital; SEP would also be able to fund capex and growth directly with debt and public equity raises, while leaving SE as a 'GP HoldCo', a nimble, highly-strategic entity reserved for overall capital allocation decisions
  - After the completion of the drop-down, SEP would become one of the largest MLPs (comparable to WPZ and KMP), thus benefiting from a premium valuation and a well-defined organic growth trajectory - over time, SEP's liquidity would increase through new equity issuances, reducing SE's 82% ownership

- We believe this transaction would be significantly accretive to SEP and simultaneously increase SEP's IDR payout by almost 6x
  - SEP's distribution would increase from $1.98/share to $2.48/share (25%+), based on elimination of cash taxes paid on SE's UST assets
  - Assuming current IDR structure, the IDR cash flow to SE shareholders would increase from an estimated $29m annually to approximately $169m annually – given SEP's organic growth prospects, this IDR payment should increase exponentially as SEP continues to grow with initial accretion to SE's dividend of 20%+
  - This transaction leaves SEP conservatively capitalized and given SE's subsidiary level financing for most of its debt (i.e., current debt will travel with assets) and SEP stock consideration, eliminates any capital gains tax
  - We estimate this process will take 2-3 months with SEP assuming all subsidiary level debt and tendering for SE's FinCo unsecured debt

Key Valuation Metrics			
Metric	SEP	PF SEP	Change
Adjusted EBITDA	305	1,397	
EBIT	109	945	
Distributable Cash Flow	239	775	
Annual dividend to LPs	$1.98	$2.48	25%
IDR Cash Flow for SE (1)	29	169	5.8x
SE ownership of SEP	61%	82%	
EV / EBITDA	16.3x	12.6x	
Debt / EBITDA	3.5x	5.2x	

(1) Assume no change in IDR structure
(2) Base: SEP current dividend; High: SEP yield less 50bps
(3) Base/High: WMB div yield

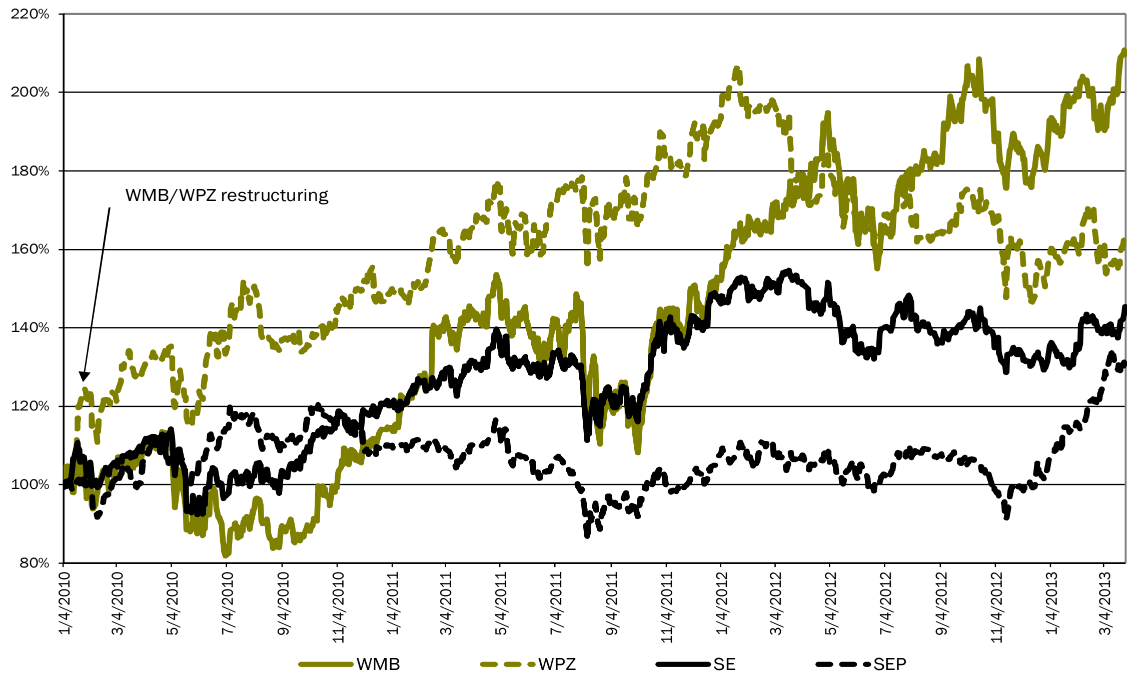
Valuation for SE		
	Base	High
Appropriate dividend yield (2)	5.4%	4.9%
Implied share price for SEP	$45.72	$50.35
Units owned by SE	187	187
Value to SE shareholders: SEP	8,565	9,433
IDR cash flow	169	169
IDR dividend yield (3)	3.7%	3.7%
Value to SE shareholders: IDR	4,561	4,561
Total value to SE shareholders	13,126	13,994
per share	*$20.00*	*$21.00*

Unlocking Shareholder Value at Spectra Energy Corp

Step 1: WPZ/WMB transaction provides a successful case study

- Williams Companies (WMB) dropped down all of its midstream and pipeline assets into Williams Partners (WPZ) in January 2010
  - The $12bn in asset drop downs increased WPZ's EV 5x+ from approximately $2.6bn to $14.2bn, increasing its capacity for growth and reducing its cost of capital
  - The transaction was financed through WPZ stock (50%, taking WMB ownership to 80% from 24%), new debt (25%) and assumed debt at the asset level (25%), minimizing any capital gains tax consequences for WMB and was completed in under 1 month (announced January 19th, closed February 17th)
  - Transaction successfully targeted MLP and 'GP HoldCo' shareholder bases and unlocked significant value for WMB shareholders

WMB has considerably outperformed SE in the relevant time frame
with sell-side valuing WMB's GP IDR at 25x+ Cash Flow



Absolute Price Performance

	WMB	SE	Diff
1 YR	19%	-5%	-25%
2 YR	46%	12%	-34%
3 YR	99%	34%	-65%

Unlocking Shareholder Value at Spectra Energy Corp

Step 2: IPO/Sell Westcoast Energy Inc. (WE)

- The IPO of WE will highlight its $14 to $16/share value based on trading multiples for comparable Canadian infrastructure companies
  - WE was purchased in 2002 by Duke Energy (DUK), former parent of SE, for $8.5bn and was primarily comprised of Canadian natural gas pipeline, storage, processing and retail distribution (Union Gas) business
  - DUK enhanced the WE acquisition in 2005 through an asset swap with ConocoPhillips (COP), whereby DUK swapped 19.7% of DCP (giving COP an equal 50% stake in DCP) for the Empress NGL system in Canada (among other asset exchanges); DUK spun out SE in 2006 with WE as a fully-owned subsidiary
  - Canadian infrastructure companies currently trade at a premium due to global interest in Canadian energy (shale, oil sands, LNG export, NGLs), competitively low corporate tax rates (15%-20%) and large, yield-driven institutional investors
  - IPO will result a re-rating of the valuation of WE as Canadian investors highly value consistency and dividends; proceeds can be used to pay-off interco loans or preferreds

- Since debt is at the subsidiary level and the subsidiary publicly files financials, an IPO of WE should be quick and efficient
  - We estimate this process will take 3-6 months
  - With a management team in place to operate assets and a compensation scheme more closely tied to WE stock performance, WE should operationally outperform, providing upside for shareholders; WE currently reimburses SE for all centralized corporate functions and files with SEDAR i.e., we expect no significant dis-synergies
  - Given size / scale of WE (and its ability to raise debt and equity capital directly from investors), WE should be able to finance growth projects in the Horn River, Montney and North Montney, as well as other long term LNG projects (e.g., Prince Rupert with BG Group) at a cheaper cost of capital

Large Cap Canadian Infrastructure Comparables								
Ticker	Name		Mkt cap	EV	Rating	EV/EBITDA	P/E	Div yield
ENB	ENBRIDGE INC		39,261	68,644	A-	16.2x	22.8x	2.6%
TRP	TRANSCANADA CORP		34,951	60,177	A-	12.6x	19.7x	3.7%
KEY	KEYERA CORP		4,863	5,681	N/A	13.7x	26.3x	3.5%
Average						14.2x	22.9x	
Westcoast Energy Inc. Valuation								
		per share	Mkt cap	EV	Rating	EV/EBITDA	P/E	Div yield
Base case: TRP EBITDA x		*$14.00*	8,895	15,066	BBB+	12.6x	26.9x	3.4%
High case: Avg EBITDA x		*$16.00*	10,753	16,924	BBB+	14.2x	32.5x	2.8%

Assumes 2013 guidance from SE for Distribution + Western Canada, 20% tax rate, 1.1x coverage ratio
M&NLP debt not included in analysis given cash collateralization of debt

Unlocking Shareholder Value at Spectra Energy Corp

Step 3: IPO/Sell DCP Midstream LLC (DCP)

- IPO/Sale of DCP Midstream yields $7/share, plus an additional $4/share from normalization of natural gas and NGL prices
  - Highlights tax-efficient nature of DCP and its value to public shareholders or other potential tax-efficient acquirers; current structure hides DCP's cash tax distribution payments made, approximately 50% of which goes to SE to pay taxes on DCP's pass-thru income (remaining goes to co-owner, PSX)
  - IPO'ing DCP would allow a) the market to value those tax distributions as part of DCP and/or b) an MLP acquirer to value those tax-efficient cash flows
  - As a separate entity, DCP management could engage in value-enhancing strategies either through operational actions (e.g., hedge NGL prices, grow more aggressively) or strategic actions (e.g., partnering with adjacent operators to maximize value)
  - We estimate this process will take 3-6 months, as DCP is currently audited and files financials with the SEC and will require negotiations/discussions with co-owner PSX
- Over the last decade, DCP has been forced to dividend cash generated to its JV owners allowing competitors to gain market share and competitive advantage in its basins, as shale discoveries have revolutionized the gathering and processing business
  - DCP has dividended more than its net income to cover JV owners' operating/growth cash needs and tax payments – in some years dividending 125%-130% of its net income (note: given that DCP is an LLC, it does not pay taxes and therefore its net income is EBT)
  - Going forward, DCP should be encouraged to invest cash generated as opposed to distributing it to take advantage of the many growth opportunities

Valuation for SE's 50% ownership of DCP

	Base Case	High Case
EBITDA (1)	580	710
Interest expense & D&A (2)	(270)	(270)
Distributable cash flow	310	440
Coverage ratio	*1.10*	*1.10*
Dividend	282	400
DPM dividend yield	6.1%	5.6%
Total value to SE shareholders	4,588	7,186
per share	*$7.00*	*$11.00*

(1) Base case uses 2013 guidance, High case assumes higher NGL and Nat Gas prices
(2) SE estimates

NGL Midstream Comparables / Valuation

Name	Mkt Cap	EV	Ratings	2013 EBDA x	Div Yield
MARKWEST ENERGY	10,005	13,081	BB	13.4x	4.9%
TARGA RESOURCES	5,047	7,551	BB	12.0x	5.7%
COPANO ENERGY-UN	3,323	4,555	B+	13.6x	5.7%
ATLAS PIPELINE P	3,001	4,379	B+	9.7x	6.0%
CROSSTEX ENERGY	1,614	2,757	B+	8.8x	6.5%
PVR PARTNERS LP	3,328	4,915	B+	11.6x	8.5%
DCP MIDSTREAM PA	3,863	5,767	BBB-	11.6x	5.6%
Averages				11.5x	6.1%
DCP - Spectra Base	9,176	14,976	BBB	12.9x	6.1%
DCP - Spectra High	14,371	20,171	BBB	14.2x	5.6%

Unlocking Shareholder Value at Spectra Energy Corp

None of management comments on MLP opportunities are correct

- Management comment #1: Assets with a low tax basis may not be efficient for MLP drop down
  - If SE takes partnership units in exchange of cash or employs a LevPar structure (below), there is no tax impact to MLP drop down
  - The tax impact on an asset sale from a ‘GP HoldCo’ to an MLP can be minimized by utilizing the leveraged partnership (LevPar) structure. This structure enables the C-corp to avoid upfront tax payments so long as it guarantees the debt issued by the MLP in conjunction with the asset acquisition and as part of the consideration, accepting some amount of LP equity issued by the MLP; a LevPar structure was employed in Energy Transfer’s acquisition of Southern Union
  - Additionally, in SE’s case, since the majority of the debt is funded at the subsidiary level, most of the financing of the asset can travel with the assets

- Management comment #2: MLP value incrementally unclear given commodity exposure and significant Canadian presence
  - Management had made these comments in Q1-12 when questioned about whether they would be at a competitive disadvantage if they did not utilize the MLP structure. Implementing Step 2 and Step 3 removes this concern as these steps will isolate the inherent value of SEP and the asset drop down strategy (Step 1)
    - Step 1 of our value maximization plan would clearly target MLP and ‘GP HoldCo’ shareholders, lowering cost of capital
    - Step 2 of our value maximization plan includes IPO’ing Westcoast Energy, which would include all of SE’s Canadian businesses
    - Step 3 of our value maximization plan states that SE should IPO/Sell DCP as it would highlight its MLP-qualifying income

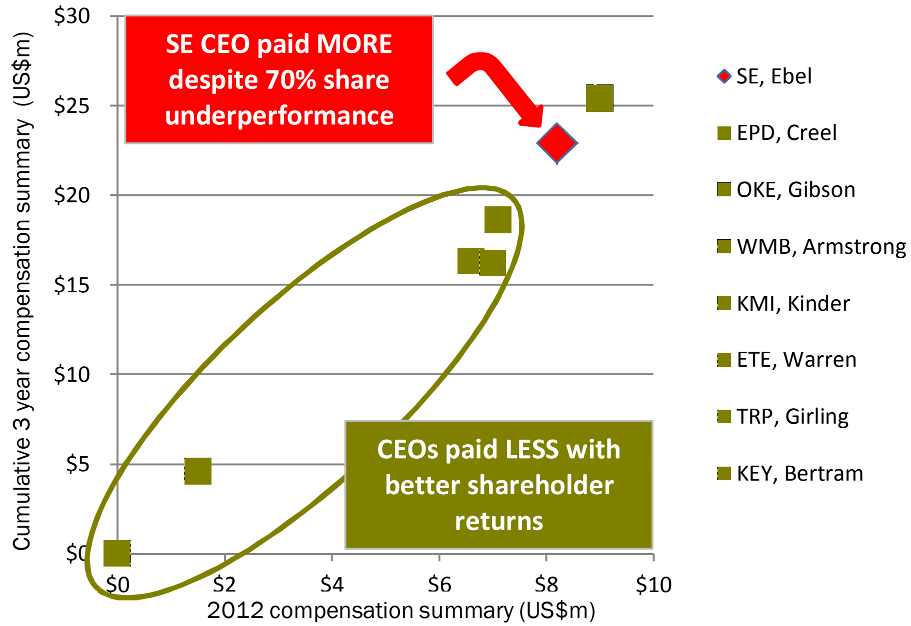
- Management comment #3: Path towards U.S. tax reform remains unclear
  - While this has been an understandable concern given the lack of clarity on a fiscal cliff resolution in the past year, lawmakers ultimately reached an agreement and enacted legislation, which did not include any tax reform impacting MLPs
  - Given that US lawmakers have proposed several recent initiatives to expand the MLP structure to help lower the cost of capital for alternative energy projects, we believe there is very little significant risk to the MLP structure

Unlocking Shareholder Value at Spectra Energy Corp

Management compensation has limited alignment to shareholder returns

Despite the underperformance of SE shares, CEO compensation ranks as one of the highest among comparable company CEOs

- Surprisingly, in 2012, after missing expectations and stock underperformance, SE CEO's compensation increased from 2011
  - Other than John Gibson at Oneok, Greg Ebel out-earned all other CEOs for 2012 and for the 3 years ending 2012
  - SE also has duplicative management teams at each of its subsidiary operations (SEP, WE and DCP) with a CEO at its MLP (note: no other comparable company has a separate CEO for their 'GP HoldCo' and MLP entity) and full executive teams at WE and DCP
  - Lastly, SE routinely compares itself from a performance standpoint to regulated US utilities (e.g., PEG, ED, PCG, XEL) – we do not believe these are the right comps for SE and neither do any of the other energy infrastructure companies listed below



SANDELL ASSET MANAGEMENT

Unlocking Shareholder Value at Spectra Energy Corp

Management compensation has limited alignment to shareholder returns

- Insiders only own less than 1% of SE US shares
  - Directors + management own 1.3m shares out of 658m shares o/s
    - Management alone own ~0.8m shares
  - In addition, directors + management own ~29k units of SEP US
- Management compensation is a mixture of both short and long-term remuneration
  - Total compensation: ~1/3 base salary (19% for CEO); ~20% short-term incentives; remainder as long-term incentives (split between time-based and performance-based)
    - Short-term incentive pay is based on a mixture of measures (incl. EPS, EBIT and ROCE)
    - Long-term incentive program consists of performance share unit awards that vest on achievement of performance goals in combination with phantom units that vest over a 3-year period
  - Over the past 3 years (2010-12), CEO Gregory L. Ebel has received compensation of ~$22.9m; the other named executives have received a combined $26.6m

Management Compensation

Name	Title	2010	2011	2012	2010-12
Gregory L. Ebel	President and CEO	6,864,886	7,782,334	8,225,957	22,873,177
J. Patrick Reddy	CFO	2,482,225	2,513,081	2,391,525	7,386,831
Alan N. Harris	Chief Development and Operations Officer	2,540,124	2,547,879	2,361,008	7,449,011
Reginald D. Hedgebeth	General Counsel	2,202,875	2,171,154	2,216,586	6,590,615
Dorothy M. Ables	Chief Administrative Officer	1,753,904	1,767,974	1,691,852	5,213,730

Top executives paid almost $50m over past 3 years despite 70%+ underperformance of SE share price versus comparables

Sandell Asset Management

Castlerigg Master Investments