



*Management's Discussion and Analysis*  
For the three months ended March 31, 2010

# *Forward-Looking Information*

The following Management Discussion and Analysis (MD&A) highlights significant business results and statistics for Inter Pipeline Fund's (Inter Pipeline) three month period ended March 31, 2010. This MD&A contains certain forward-looking statements or information (collectively referred to as "forward-looking statements") within the meaning of applicable securities legislation. Forward-looking statements often contain terms such as "may", "will", "should", "anticipate", "expect", "continue", "estimate", "believe", "project", and similar words suggesting future outcomes or statements regarding an outlook. Any statements herein that are not statements of historical fact may be deemed to be forward-looking statements. Forward-looking statements in this MD&A include, but are not limited to statements regarding: 1) Inter Pipeline's beliefs that it is well positioned to maintain its current level of cash distributions to its unitholders through 2011 and beyond; 2) the maintenance of Inter Pipeline's cash distribution level combined with the tax treatment of distributions to its unitholders effective in 2011 should result in a favourable after-tax treatment for Inter Pipeline's taxable unitholders; 3) Inter Pipeline being well positioned to operate and grow in the future; and, 4) cash flow projections, timing and completion of its Corridor expansion project, new Polaris diluent pipeline project for the Kearl oil sands development, Cochrane desulphurization facility and other capital forecasts.

Readers are cautioned not to place undue reliance on forward-looking statements, as there can be no assurance that the expectations, plans or intentions upon which they are based will occur. Inter Pipeline in no manner represents that actual results achieved will be the same in whole or in part as those set out in the forward-looking statements herein. Such information, although considered reasonable by Pipeline Management Inc., the general partner of Inter Pipeline (General Partner) at the time of preparation, may later prove to be incorrect and actual results may differ materially from those anticipated in the forward-looking statements. By their nature, forward-looking statements are subject to various risks, uncertainties and other factors, which are beyond Inter Pipeline's control, including, but not limited to: risks associated with operations, such as Inter Pipeline's ability to successfully implement its strategic initiatives and achieve expected benefits; the status, credit risk and continued existence of customers having contracts with Inter Pipeline and its subsidiaries; availability of energy commodities; volatility of and assumptions regarding prices of energy commodities; competitive factors, pricing pressures and supply and demand in the natural gas and oil transportation, ethane transportation and natural gas liquids (NGL) extraction and storage industries; assumptions based upon Inter Pipeline's current guidance; fluctuations in currency and interest rates; the ability to access sufficient capital from internal and external sources; product supply and demand; risks inherent in Inter Pipeline's Canadian and foreign operations; risks of war, hostilities, civil insurrection and instability affecting countries in which Inter Pipeline and its subsidiaries operate; severe weather conditions; terrorist threats; risks associated with technology; Inter Pipeline's ability to generate sufficient cash flow from operations to meet its current and future obligations; Inter Pipeline's ability to access external sources of debt and equity capital; general economic and business conditions; potential delays and costs of overruns on construction projects, including, but not limited to the Corridor and other pipeline system projects noted above; Inter Pipeline's ability to make capital investments and amount of capital investments; changes in laws and regulations, including environmental, regulatory and taxation laws, and the interpretation of such changes to laws and regulations; the risks associated with existing and potential future lawsuits and regulatory actions against Inter Pipeline and its subsidiaries; increases in maintenance, operating or financing costs; availability of adequate levels of insurance; political and economic conditions in the countries in which Inter Pipeline and its subsidiaries operate; difficulty in obtaining necessary regulatory approvals; and such other risks and uncertainties described from time to time in Inter Pipeline's reports and filings with the Canadian securities authorities.

**Readers are cautioned that the foregoing list of important factors is not exhaustive. See also the section entitled RISK FACTORS included in Inter Pipeline's MD&A for the year ended December 31 2009. The forward-looking statements contained in this MD&A are made as of the date of this document, and, except to the extent expressly required by applicable securities laws and regulations, Inter Pipeline assumes no obligation to update or revise forward-looking statements made herein or otherwise, whether as a result of new information, future events, or otherwise. The forward-looking statements contained in this document are expressly qualified by this cautionary note.**

# *Management's Discussion and Analysis*

## **For the first quarter ended March 31, 2010**

The MD&A provides a detailed explanation of Inter Pipeline's operating results for the three month period ended March 31, 2010 as compared to the three month period ended March 31, 2009. The MD&A should be read in conjunction with the unaudited interim consolidated financial statements and MD&A of Inter Pipeline for the quarterly periods ended March 31, June 30 and September 30, 2009, the audited consolidated financial statements for the year ended December 31, 2009, the Annual Information Form and other information filed by Inter Pipeline at [www.sedar.com](http://www.sedar.com).

Financial information presented in this MD&A is based on information in Inter Pipeline's consolidated financial statements prepared in accordance with Canadian generally accepted accounting principles (GAAP). This MD&A reports certain non-GAAP financial measures that are used by management to evaluate the performance of Inter Pipeline and its business segments. Since certain non-GAAP financial measures may not have a standardized meaning, securities regulations require that non-GAAP financial measures are clearly defined, qualified and reconciled with their nearest GAAP measure. See the NON-GAAP FINANCIAL MEASURES section for further information on the definition, calculation and reconciliation of non-GAAP financial measures. All amounts are in Canadian dollars unless specified otherwise.

Management determines if information presented in this MD&A is material based on whether it believes a reasonable investor's decision to buy, sell or hold securities in Inter Pipeline would likely be influenced or changed if the information was omitted or misstated.

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## **FIRST QUARTER HIGHLIGHTS**

- Funds from operations\* totalled \$85.5 million in the first quarter
- Attractive payout ratio before sustaining capital\* of 67%
- Cash distributions to unitholders totalled \$57.6 million, or \$0.225 per unit
- Generated net income of \$61.7 million or \$0.24 per unit, up \$18.3 million from the first quarter of 2009
- Throughput on Inter Pipeline's oil sands transportation and conventional oil pipeline systems averaged a record 800,300 barrels per day (b/d)
- Corridor capacity expansion project is mechanically complete; line fill activities commenced during the quarter
- Bow River segregation project entered into commercial service, generating approximately \$16.5 million in incremental EBITDA per year
- Inter Pipeline (Corridor) Inc. successfully completed a \$150 million debenture offering at attractive rates

\*Please refer to the NON-GAAP FINANCIAL MEASURES section

## PERFORMANCE OVERVIEW

	Three months ended	
	March 31	
<i>(millions, except per unit and % amounts)</i>	2010	2009
Revenues		
Oil sands transportation	\$ 34.9	\$ 33.6
NGL extraction	173.0	143.2
Conventional oil pipelines	37.6	38.7
Bulk liquid storage	26.0	30.1
	<b>\$ 271.5</b>	<b>\$ 245.6</b>
Funds from operations <sup>(1)</sup>		
Oil sands transportation	\$ 18.6	\$ 18.0
NGL extraction	47.6	26.2
Conventional oil pipelines	28.2	28.5
Bulk liquid storage	10.3	10.5
Corporate costs	(19.2)	(17.1)
	<b>\$ 85.5</b>	<b>\$ 66.1</b>
Per unit <sup>(1)</sup>	\$ 0.33	\$ 0.30
Net income	\$ 61.7	\$ 43.4
Per unit – basic and diluted	\$ 0.24	\$ 0.19
Cash distributions <sup>(2)</sup>	\$ 57.6	\$ 46.9
Per unit <sup>(2)</sup>	\$ 0.225	\$ 0.210
Units outstanding (basic)		
Weighted average	255.8	223.4
End of period <sup>(2)</sup>	256.3	223.7
Capital expenditures		
Growth <sup>(1)</sup>	\$ 31.2	\$ 57.0
Sustaining <sup>(1)</sup>	2.5	2.9
	<b>\$ 33.7</b>	<b>\$ 59.9</b>
Payout ratio before sustaining capital <sup>(1)</sup>	67.4%	71.0%
Payout ratio after sustaining capital <sup>(1)</sup>	69.4%	74.3%
	March 31	December 31
	2010	2009
Total assets	\$ 4,445.7	\$ 4,472.7
Total debt <sup>(3)</sup>	\$ 2,576.8	\$ 2,619.7
Total partners' equity	\$ 1,314.2	\$ 1,320.1
Enterprise value <sup>(1)</sup>	\$ 5,611.4	\$ 5,372.4
Total debt to total capitalization <sup>(1)</sup>	66.2%	66.5%
Total recourse debt to capitalization <sup>(1)</sup>	34.4%	35.7%

(1) Please refer to the NON-GAAP FINANCIAL MEASURES section of this MD&A.

(2) Cash distributions are calculated based on the number of units outstanding at each record date.

(3) Total debt includes long-term debt totalling \$2,567.7 million before discounts and debt transaction costs of \$9.1 million reported in the March 31, 2010 consolidated financial statements.

### **THREE MONTHS ENDED MARCH 31, 2010**

Inter Pipeline generated very strong financial results in the first quarter of 2010, led by the NGL extraction business segment. Frac-spreads were significantly higher this quarter compared to the first quarter of 2009 as related commodity prices have rebounded to pre 2009 levels. Consolidated funds from operations of \$85.5 million were \$19.4 million or 29.3% higher than the \$66.1 million generated in 2009, which resulted in an attractive payout ratio before sustaining capital of 67.4%. Operating results in the oil sands transportation business were also slightly higher in the quarter, primarily due to an increase in volumes transported on the Cold Lake pipeline system. Business results for the conventional oil pipelines and bulk liquid storage business segments were relatively consistent with 2009, while corporate costs increased in the period.

Net income of \$61.7 million in the first quarter of 2010 was \$18.3 million or 42.2% higher than the \$43.4 million earned in the same period in 2009. This increase was primarily due to the strong NGL extraction business results noted above. In addition, net income in the first quarter benefited from a favourable \$28.6 million unrealized change in the mark-to-market value of derivative financial instruments. However, this was more than offset by a \$32.3 million comparative increase in future taxes. In 2009, Inter Pipeline recorded a favourable \$24.0 million non-cash future tax accrual related to changes in provincial SIFT tax rates legislated in March 2009.

Total cash distributed to unitholders in the first quarter of 2010 increased \$10.7 million or 22.8% to \$57.6 million compared to \$46.9 million distributed in the first quarter of 2009. This increase is the result of a higher number of units outstanding in the first quarter of 2010 and a 7.1% per unit increase in monthly cash distributions to \$0.075 per unit effective December 2009. In 2009, Inter Pipeline issued new units pursuant to a successful public unit offering in June and new distribution reinvestment plan adopted in May 2009.

Inter Pipeline's total debt decreased \$42.9 million from \$2,619.7 million to \$2,576.8 million during the quarter even though \$33.7 million was expended on capital projects. Undistributed funds from operations and net proceeds from Inter Pipeline's distribution reinvestment plan were utilized to reduce indebtedness on Inter Pipeline's \$750 million revolving credit facility. As a result, Inter Pipeline's recourse debt to capitalization ratio dropped from 35.7% at December 31, 2009 to 34.4% at March 31, 2010. Adjusting for the inclusion of non-recourse debt of \$1,886.8 million held within the Corridor corporate entity, Inter Pipeline's total debt to capitalization ratio was 66.2%.

### **OUTLOOK**

In 2010, Inter Pipeline will continue to execute its long term strategy of developing long-life, high quality energy infrastructure assets that provide sustainable and predictable cash flows into the future. Activity in the current year will advance several major growth projects towards this objective. The central focus of activity will continue to be the \$1.8 billion Corridor pipeline capacity expansion project, now in the final commissioning stages. When in service, this project will add substantially to cash flows and become a key element in allowing Inter Pipeline to maintain its current distribution levels through 2011 and beyond, despite Inter Pipeline becoming fully taxable in 2011. Successful completion of the Corridor expansion will also enable further opportunities utilizing existing infrastructure, including the development of a diluent transportation system.

The Corridor expansion project, after four years of steady progress, is expected to be completed in 2010 on schedule and on budget. Upon completion, bitumen blend transport capacity on the Corridor system is expected to initially increase from 300,000 b/d to 465,000 b/d. This additional capacity will accommodate shipment of increased oil sands production from the Athabasca Oil Sands Project (AOSP), a joint venture between Shell Canada Energy, Chevron Canada Limited and Marathon Oil Canada Corporation. The same cost-of-service contractual arrangements used on the original Corridor pipeline system will govern the expansion, contributing additional stable long-term cash flows. The majority of the expansion is expected to be in-service mid-2010, with incremental revenue commencing no later than January 1, 2011.

In conjunction with the completion of the Corridor expansion, Inter Pipeline will re-orient the current Corridor pipeline system into two distinct systems. The Corridor system will consist of a new 42-inch diameter bitumen blend pipeline installed as part of the Corridor expansion, the existing 24-inch diameter line which will provide diluent service to the AOSP, the existing 16-inch diameter feedstock pipeline and two 20-inch diameter products pipelines. As a result of the expansion, a new system, the Polaris pipeline system will be created consisting of the 12-inch diameter pipeline which previously provided diluent service to the AOSP. Polaris will be available to provide diluent service to other Alberta oil sands projects once the Corridor expansion is in service.

Anchoring the new Polaris pipeline system is a 25-year agreement, announced in 2009, to transport diluent for Imperial Oil Resources Ventures Limited (Imperial), a jointly owned venture between Imperial Oil Limited and ExxonMobil Canada, to their Kearl oil sands mining project (Kearl project) located northeast of Fort McMurray. Approximately \$135 million will be invested over the next three years to connect this existing 12-inch diameter pipeline to the Kearl project and to a diluent receipt point in the Edmonton area. Diluent volumes to be transported to the Kearl project under this agreement total 60,000 b/d, or half of the system's 120,000 b/d capacity. Inter Pipeline will pursue further opportunities to utilize the remaining capacity on the Polaris system, and anticipate transporting additional diluent volumes to either the Kearl project or other potential sites.

In late 2009, Inter Pipeline completed construction of the Bow River pipeline oil segregation project. The project, backed by a firm shipping commitment of 30,000 b/d for an initial term of seven years, involved the construction of 128 kilometres of new pipeline and associated facilities. These additions enable Inter Pipeline to segregate and ship distinct crude oil streams from the oil storage and marketing hub at Hardisty, Alberta to refining customers in Montana. Crude oil segregation service began in the first quarter of 2010, which will generate an estimated \$16.5 million in incremental EBITDA per year.

Turning to overall business fundamentals, Inter Pipeline continues to be in a positive financial and operating position despite the recent economic recession. Inter Pipeline's balance sheet is very strong with a total recourse debt to capitalization ratio of only 34.4% at March 31, 2010. A significant portion of cash flow is generated under long-term contracts that are not commodity price or volume sensitive, particularly in Inter Pipeline's oil sands transportation business segment. Cash flow underpinned by cost-of-service contracts are expected to become more predominant in future years as the Corridor expansion and Polaris pipeline system begin generating cash flow.

With recent strengthening of commodity prices, propane-plus frac-spreads continued to climb in the first quarter of 2010, the fifth consecutive quarterly increase. As a result, high frac-spreads contributed significantly to first quarter 2010 financial results, specifically in the NGL extraction business segment. Inter Pipeline's diversified revenue streams ensure that while beneficial commodity prices strongly help overall financial performance through high frac-spreads, the direct impact of weaker commodity prices is limited primarily to propane-plus sales at the Cochrane NGL extraction facility.

As a result of the federal government's Tax Fairness Plan, publicly-traded flow-through entities such as income trusts and limited partnerships will be subject to taxation commencing January 1, 2011. Discussions in the financial community with respect to these entities are focused on potential changes to corporate structure and possible changes to cash distribution levels when these entities become taxable.

In order to evaluate the implications of the Tax Fairness Plan on Inter Pipeline, the governance committee and the remaining independent directors of Inter Pipeline's board of directors engaged in a formal process to consider if an alternative business structure, such as converting to a corporation, would be beneficial. In evaluating alternative structures, consideration was given to possible impacts on Inter Pipeline including the level of income taxes to be paid, corporate conversion costs, counterparty consent issues and sustainability of distributions. The review of these impacts by the governance committee and the other independent directors did not reveal any material tangible benefit to Inter Pipeline's unitholders should it change its existing business structure. As a result, Inter Pipeline's board of directors has determined that Inter Pipeline will remain structured as a publicly traded limited partnership into the foreseeable future. The board of directors will continue to monitor future events which could affect this decision.

Since the Tax Fairness Plan was enacted, Inter Pipeline has stated that it is well positioned to maintain its current level of cash distributions to unitholders despite becoming fully taxable in 2011. This outlook remains unchanged. Strong fundamentals within each of Inter Pipeline's four business segments support distributions at current levels, as do expected cash flow increases from organic growth projects currently underway.

The change to a taxable entity will also lead to a more favourable tax treatment of Inter Pipeline's distributions in the hands of a taxable investor. In 2011, these distributions will be treated for tax purposes substantially similar to dividends from Canadian public corporations. This dividend treatment, when combined with Inter Pipeline's intent to maintain stable cash distributions at current levels through 2011 and beyond, should result in a taxable Canadian investor receiving a favourable after-tax return from owning Inter Pipeline units.

Inter Pipeline's credit position continues to be strong, anchored by a well-diversified banking syndicate. Central to Inter Pipeline's credit capacity are two fully committed credit facilities that are used to operate and grow the business. With approximately \$995 million in unutilized credit capacity and terms extending into 2012, these committed credit facilities provide Inter Pipeline with a solid financial base to support and grow the business.

Both Standard & Poor's (S&P) and DBRS Limited (DBRS) have assigned an investment grade, long-term corporate credit rating of BBB to Inter Pipeline. Inter Pipeline's 100% owned subsidiary, Inter Pipeline (Corridor) Inc. (Corridor), has been assigned investment grade credit ratings of A (low), A3 and A- from DBRS, Moody's Investor Services (Moody's) and S&P, respectively. Continued success advancing growth projects, infusions of equity capital in the past year, and continued strong financial results are all factors supporting continued investment grade credit ratings.

## RESULTS OF OPERATIONS

### OIL SANDS TRANSPORTATION BUSINESS SEGMENT

	Three months ended March 31		
<i>Volumes (000s b/d)</i>	2010	2009	% change
Cold Lake (100% basis)	447.6	386.8	15.7
Corridor	186.5	205.9	(9.4)
	634.1	592.7	7.0
<i>(millions)</i>			
Revenue <sup>(1)</sup>	\$ 34.9	\$ 33.6	3.9
Operating expenses <sup>(1)</sup>	\$ 13.4	\$ 12.4	8.1
Funds from operations <sup>(1)(2)</sup>	\$ 18.6	\$ 18.0	3.3
Capital expenditures <sup>(1)</sup>			
Growth <sup>(2)</sup>	\$ 25.6	\$ 44.2	
Sustaining <sup>(2)</sup>	-	0.1	
	\$ 25.6	\$ 44.3	

(1) Cold Lake pipeline system's revenue, operating expenses, funds from operations and capital expenditures are recorded on the basis of Inter Pipeline's 85% ownership interest.

(2) Please refer to the NON-GAAP FINANCIAL MEASURES section.

### Volumes

The Cold Lake pipeline system is a bitumen blend and diluent pipeline system that transports diluted bitumen from the Cold Lake oil sands area of Alberta to delivery points in the Hardisty and Edmonton areas. Average volume transported on the Cold Lake pipeline system increased approximately 60,800 b/d to an all time record of 447,600 b/d as the Cold Lake shippers continue to develop and expand their production base.

The Corridor pipeline system is also a bitumen blend and diluent pipeline system. It transports diluted bitumen from the Muskeg River mine near Fort McMurray, Alberta to the Scotford upgrader located northeast of Edmonton, Alberta. In the first quarter of 2010, average volume transported on the Corridor pipeline system decreased by approximately 19,400 b/d. These 2010 volumes were lower as in March 2010 over 1.0 million barrels of diluted bitumen was diverted to become line fill for the new 42-inch diameter pipeline as final commissioning of the Corridor pipeline expansion project commenced. This initial fill represents approximately 44% of the total line fill volume required with the balance to be provided early in the second quarter of 2010.

### **Revenue**

Oil sands transportation revenue was approximately \$1.3 million higher in the first quarter of 2010 compared to 2009. Cold Lake revenue increased by approximately \$1.9 million which offset a \$0.6 million decrease in Corridor revenue.

Growth in Cold Lake revenue was primarily attributable to a \$1.3 million increase in capital fee revenue. Operating expense recoveries and other revenue contributed to the remaining increase in Cold Lake revenue. The Cold Lake Transportation Services Agreement (Cold Lake TSA) provides a structured return on capital invested in pipelines and facilities that comprise the Cold Lake pipeline system and recovery of substantially all operating costs over the term of the agreement. The founding shippers' annual minimum ship-or-pay commitment under the terms of the Cold Lake TSA is \$27.8 million to the end of December 2011 based on Inter Pipeline's 85% ownership interest (\$32.7 million - 100% basis). Inter Pipeline receives additional capital fees for volumes shipped over and above the defined ship-or-pay amounts. Certain additional facilities on the Cold Lake pipeline system also produce an additional return on the capital invested and recovery of associated operating costs.

Corridor's revenue was approximately \$0.6 million lower in the first quarter of 2010. Compared to the first quarter of 2009, average short-term interest rates declined 37 basis points (bps) in the first quarter of 2010 which resulted in a decline in debt financing costs and related revenue recovery. Similarly, a decline in power consumption and power pool prices in 2010 resulted in lower power costs and related recoveries. The Corridor pipeline system is operated pursuant to a long-term Firm Service Agreement (Corridor FSA). The Corridor FSA utilizes a rate base cost-of-service approach to establish an annual revenue requirement which includes recovery of debt financing costs, all operating costs, rate base depreciation and taxes in addition to providing a return on equity. As a result of this cost-of-service arrangement, Corridor's funds from operations are not impacted by throughput volumes or commodity price fluctuations. The main drivers of any potential variation in Corridor's funds from operations are changes to long-term Government of Canada bond rates which are the basis for the annual return on equity, and changes to the underlying rate base.

### **Operating Expenses**

Operating expenses associated with the oil sands transportation business segment have a limited impact on Inter Pipeline's cash flow as almost all expenditures are recovered from shippers on both Cold Lake and Corridor pipeline systems.

Overall, power costs of \$4.9 million in the oil sands transportation business in 2010 were consistent with costs in the first quarter of 2009. Declines in average Alberta power pool prices offset higher costs arising from increased power consumption as a result of increased volumes on the Cold Lake pipeline system. Average published power prices decreased 35.6% from \$63.35 per megawatt hour (MWh) in the first quarter of 2009 to \$40.78/MWh in 2010.

Other operating expenditures in the oil sands transportation business increased approximately \$1.0 million in the first quarter of 2010. Both Cold Lake and Corridor's operating expenses increased slightly due to increases in property tax and the timing of certain pipeline integrity costs, respectively.

## Capital Expenditures

In the first quarter of 2010, approximately \$21.8 million of growth capital was spent on the Corridor pipeline expansion project for a total of \$1,615.6 million to date. The project is mechanically complete and has entered into its final commissioning phase.

In March 2010, final commissioning of the \$1.8 billion Corridor expansion project commenced as the new 42-inch diameter pipeline received over 1.0 million barrels of diluted bitumen as part of line fill activities. The final commissioning stage for the 42-inch diameter diluted bitumen and 24-inch diameter diluent pipelines is expected to be completed in the second quarter of 2010. The new 20-inch diameter product pipeline is expected to be fully commissioned in the fall of 2010. Total forecast costs for the Corridor expansion project remain unchanged from its original forecast. The project is comprised of two distinct cost components. The first is a pipeline and facility construction component wherein Inter Pipeline was exposed to potential cost overruns. Inter Pipeline estimates that these costs are approximately \$90 million under budget. The second cost component includes items such as storage tanks, interest during construction, line fill requirements and certain contingency cost factors. Inter Pipeline has no price risk exposure for these components as they will be added to the rate base at their actual cost.

Preliminary engineering for Inter Pipeline's Polaris diluent pipeline system began in 2009 and approximately \$1.1 million has been spent on this project in the first quarter of 2010 for a total of \$3.5 million to date. Beginning in late 2012, the Polaris system will provide diluent transportation services for Imperial's Kearl oil sands development utilizing the existing 12-inch diameter pipeline that will be idled once the Corridor expansion project is in service. After the Polaris pipeline goes into service for the Kearl project, its net book value will be deducted from Corridor's rate base. Total incremental costs to connect the Polaris pipeline to the Kearl oil sands development and diluent receipt points in the Edmonton area are currently estimated to be \$135 million.

On the Cold Lake pipeline system, approximately \$2.7 million was spent during the first quarter of 2010 on a quarter-point booster station expansion on the south leg of the Cold Lake pipeline system. The project is substantially complete at an estimated cost to Inter Pipeline of \$55 million. Two new quarter-point pump stations were commissioned in the first quarter of 2009 and are available to transport additional volumes from the Cold Lake shippers. Modifications were also made to two existing pump stations. This project increased the capacity of the Cold Lake pipeline system from 460,000 b/d to approximately 560,000 b/d.

## NGL EXTRACTION BUSINESS SEGMENT

	Three months ended March 31							
	2010				2009			
	<i>mmcf/d</i>	<i>(000s b/d)</i>		<i>mmcf/d</i>	<i>(000s b/d)</i>			
	Throughput	Ethane	Propane-plus	Total	Throughput	Ethane	Propane-plus	Total
Cochrane	2,023	52.5	28.3	80.8	2,067	53.9	30.2	84.1
Empress V (100% basis)	1,042	20.1	12.0	32.1	159	2.5	1.9	4.4
Empress II	141	2.5	1.6	4.1	1,281	23.6	15.1	38.7
	3,206	75.1	41.9	117.0	3,507	80.0	47.2	127.2

<i>(millions)</i>	Three months ended March 31		
	2010	2009	% change
Revenue <sup>(1)</sup>	\$ 173.0	\$ 143.2	20.8
Shrinkage gas <sup>(1)</sup>	\$ 99.4	\$ 83.1	19.6
Operating expenses <sup>(1)</sup>	\$ 25.9	\$ 33.9	(23.6)
Funds from operations <sup>(1) (2)</sup>	\$ 47.6	\$ 26.2	81.7
Capital expenditures <sup>(1)</sup>			
Growth <sup>(2)</sup>	\$ 0.5	\$ 4.1	
Sustaining <sup>(2)</sup>	0.5	1.4	
	\$ 1.0	\$ 5.5	

(1) Revenue, shrinkage gas, operating expenses, funds from operations and capital expenditures for the Empress V NGL extraction facility are recorded based on Inter Pipeline's 50% ownership.

(2) Please refer to the NON-GAAP FINANCIAL MEASURES section.

## Volumes

Inter Pipeline's NGL extraction plants processed an average of 3,206 million cubic feet per day (mmcf/d) of natural gas during the three months ended March 31, 2010. This was approximately 301 mmcf/d lower than the comparative period in 2009 primarily due to lower volumes of eastbound natural gas exports being available for processing at the Empress facilities. Also in the first quarter of 2009, the Empress V facility was shut down for construction of an ethane recovery improvement project which resulted in increased throughput volumes at the Empress II facility. Lower throughput volumes at the Empress II facility in 2010 did not impact operating results significantly due to the cost-of-service processing arrangements at this facility. Throughput volume at the Cochrane facility declined only marginally in 2010, as demand for Canadian natural gas into the western US remained strong.

## Revenue

The NGL extraction business earns revenue from a combination of commodity based, fee-based and cost-of-service arrangements. Commodity based contracts provide for a sharing of profits from the sale of NGL products between the NGL extraction business and the purchaser. The profit share calculation consists of revenue from the sale of NGL products less costs to bring the NGL product to market, including extraction, shrinkage gas, fractionation and marketing costs. NGL commodity based contracts are exposed to frac-spread and volume risks. Fee-based contracts provide a fixed fee associated with each barrel of NGL produced and recovery of operating costs, including shrinkage gas costs. There is no commodity price exposure associated with this type of contract; however fee-based contracts are exposed to volume fluctuations. Cost-of-service contracts provide a structured return on new capital invested utilizing a rate base approach and a recovery of operating costs, including shrinkage gas. This form of contract provides the most stable cash flow of the three contract types, as there is minimal volume risk and no commodity price exposure.

In the first quarter of 2010, revenue was approximately \$29.8 million higher than in 2009 due to higher realized frac-spreads and increased production at the Empress V facility. These higher revenues were partially offset by lower shrinkage, fuel gas and electricity cost recoveries in cost-of-service and fee-based arrangements as a result of lower natural gas and power pool prices.

## Frac-spread

<i>(dollars)</i>	Three months ended March 31			
	2010		2009	
	USD/USG <sup>(1)</sup>	CDN/USG <sup>(1)</sup>	USD/USG <sup>(1)</sup>	CDN/USG <sup>(1)</sup>
Market frac-spread	\$ 0.876	\$ 0.912	\$ 0.323	\$ 0.402
Realized frac-spread	\$ 0.816	\$ 0.849	\$ 0.446	\$ 0.555

(1) The differential between USD/USG and CDN/USG frac-spreads is due to fluctuations in exchange rates between US and Canadian dollars.

Market frac-spread is defined as the difference between the weighted average propane-plus price at Mont Belvieu, Texas and the monthly index price of AECO natural gas purchased for shrinkage calculated in US dollars per US gallon (USD/USG). This price is converted to Canadian dollars per US gallon (CDN/USG) based on the average monthly Bank of Canada CDN/USD noon rate. Realized frac-spread is defined in a similar manner and is calculated on a weighted average basis using market frac-spread for unhedged production and fixed-price frac-spread prices for the remaining hedged production. Propane-plus market price differentials, natural gas transportation and extraction premium costs have not been significant historically, therefore are not included in the calculation of realized frac-spread. See the RISK MANAGEMENT AND FINANCIAL INSTRUMENTS section for further discussion of frac-spread hedges.

Realized frac-spreads increased \$0.37 USD/USG in the first quarter from \$0.45 USD/USG in 2009 to \$0.82 USD/USG in 2010. Frac-spreads in the three month period ended March 31, 2010 were well above the 5-year and 15-year simple average market frac-spread of \$0.59 USD/USG and \$0.34 USD/USG, respectively, calculated at December 31, 2009.

### **Shrinkage**

Shrinkage gas represents natural gas bought by Inter Pipeline to replace the heat content of liquids extracted from natural gas processed at the Cochrane and Empress V facilities. The price for shrinkage gas is based on a combination of daily and monthly index AECO natural gas prices. In the first quarter of 2010, shrinkage gas expense increased approximately \$16.3 million as a result of increased production at Empress V which was partially offset by a decline in AECO natural gas prices. The weighted average monthly AECO price<sup>1</sup> was \$5.07 per gigajoule (GJ) in the first quarter of 2010, which was approximately 5.1% lower than the weighted average price<sup>1</sup> of \$5.34/GJ in the same period in 2009.

### **Operating Expenses**

Operating expenses were approximately \$8.0 million lower in the first quarter of 2010 compared to the same period in 2009. Fuel and power costs decreased approximately \$7.3 million in the first quarter of 2010 compared to 2009 due to lower average Alberta power pool and AECO natural gas prices as well as a decline in volumes through the Empress II facility. Maintenance expenses at the Cochrane facility increased approximately \$1.7 million as a result of non-routine major maintenance associated with facility equipment. This increase in operating costs was more than offset by lower operating costs at the Empress facilities when compared to 2009. In 2009, operating costs at the Empress facilities were higher due to repair of weld defects in pressure vessels at Empress V.

### **Capital Expenditures**

In the first quarter of 2010, approximately \$0.5 million was spent on a variety of growth capital projects at the Empress facilities while an additional \$0.5 million was spent on various sustaining capital projects at the Cochrane facility.

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<sup>1</sup> Weighted average price calculated from one-month spot prices at AECO as reported in the *Canadian Gas Price Reporter*.

## CONVENTIONAL OIL PIPELINES BUSINESS SEGMENT

	Three months ended March 31		
Volumes (000s b/d)	2010	2009	% change
Bow River	112.5	119.2	(5.6)
Central Alberta / Mid-Saskatchewan / Valley <sup>(1)</sup>	53.7	62.9	(14.6)
	166.2	182.1	(8.7)
<i>(millions)</i>			
Revenue	\$ 37.6	\$ 38.7	(2.8)
Operating expenses	\$ 8.8	\$ 10.1	(12.9)
Funds from operations <sup>(2)</sup>	\$ 28.2	\$ 28.5	(1.1)
Revenue per barrel <sup>(3)</sup>	\$ 2.51	\$ 2.36	6.4
Capital expenditures			
Growth <sup>(2)</sup>	\$ 2.5	\$ 1.4	
Sustaining <sup>(2)</sup>	1.4	0.5	
	\$ 3.9	\$ 1.9	

(1) Valley pipeline system was sold in April 2009.

(2) Please refer to the NON-GAAP FINANCIAL MEASURES section.

(3) Revenue per barrel represents total revenue of the conventional oil pipelines business segment divided by actual volumes.

### Volumes

Conventional oil pipeline volumes were approximately 15,900 b/d lower in the first quarter of 2010 compared to 2009. Transportation volumes on the Central Alberta pipeline system were approximately 8,600 b/d lower in 2010 as various producers transferred crude oil volumes away from Inter Pipeline's truck terminal facilities to other facilities to capitalize on a narrowing of heavy crude oil pricing differentials. On the Bow River pipeline system, volumes were approximately 6,700 b/d lower due to natural declines and a minor impact of truck-redirected volumes. However these lower volumes were partially offset by an increase in volumes on the Bow River Hardisty south pipeline due to completion of the Bow River segregation project. The remaining decline in volumes related to the sale of the Valley pipeline system in the second quarter of 2009 and natural production declines in the areas serviced by these conventional pipelines.

### Revenue

Conventional oil pipeline revenues were approximately \$1.1 million lower in the first quarter of 2010 as heavy crude oil pricing trends noted above resulted in lower marketing revenue compared to 2009. Lower marketing revenue was partially offset by higher tariff revenues due to mainline toll increases and incremental Hardisty south revenue as the Bow River segregation project commenced service. Mainline toll increases averaging approximately 6% were implemented in both January 2010 and July 2009, generating approximately \$1.8 million in incremental revenue.

### Operating Expenses

Operating expenses in 2010 were approximately \$1.3 million lower compared to 2009 primarily due to the timing of pipeline integrity and tank maintenance projects.

### Capital Expenditures

Growth capital expenditures include costs for the Bow River pipeline crude oil stream segregation project completed in the first quarter of 2010. Sustaining capital expenditures relate to corporate capital projects.

## BULK LIQUID STORAGE BUSINESS SEGMENT

	Three months ended March 31		
	2010	2009	% change
Utilization	95.4%	97.3%	(2.0)
<i>(millions)</i>			
Revenue	\$ 26.0	\$ 30.1	(13.6)
Operating expenses	\$ 13.5	\$ 17.1	(21.1)
Funds from operations <sup>(1)</sup>	\$ 10.3	\$ 10.5	(1.9)
Capital expenditures			
Growth <sup>(1)</sup>	\$ 2.6	\$ 7.3	
Sustaining <sup>(1)</sup>	0.6	0.9	
	\$ 3.2	\$ 8.2	

(1) Please refer to the NON-GAAP FINANCIAL MEASURES section.

### Utilization

Inter Pipeline, through its wholly owned subsidiary Simon Storage Limited (Simon Storage), owns eight deep-water bulk liquid storage terminals primarily servicing the petrochemical, petroleum and biofuel industries in the UK, Germany and Ireland. In spite of recent negative trends in the European economic environment, tank utilization remained strong averaging more than 95% in the first quarter of 2010. Demand for storage fluctuates historically due to market conditions within industry sectors and Simon Storage manages these fluctuations through customer and product diversification.

### Revenue

The business activities of Simon Storage consist primarily of bulk liquid storage and handling services. Simon Storage also offers a range of ancillary services to its customers through its engineering, training and facilities management divisions.

In the first quarter of 2010, revenue was approximately \$4.1 million lower than in 2009. Foreign currency translation adjustments and sale of the bulk liquid trucking business in the fourth quarter of 2009 accounted for the decline in revenue. Storage and handling revenue increased approximately \$1.4 million primarily due to the commencement of storage services related to additional tankage completed and in-service in the latter part of 2009, increases in storage rates and additional handling and heating services.

### Operating Expenses

Operating expenses were also lower by approximately \$3.6 million in the first quarter of 2010 compared to 2009. Foreign currency translation adjustments and sale of the bulk liquid trucking business accounted for the majority of the decline in operating expenses. Storage and handling operating expenses were consistent with the same period in 2009.

### Capital Expenditures

Inter Pipeline spent approximately \$2.6 million in growth capital expenditures during the first quarter of 2010 related to a number of tank replacements, tank life extensions and tank modification projects at Immingham and other terminals. Growth capital expenditures included approximately \$0.6 million for a total of \$7.2 million spent on two tank conversion projects to support a new ten-year contract with Total UK Limited to store molten sulphur at the Immingham terminal. This project is substantially complete.

Sustaining capital expenditures consisted of a variety of small projects relating to improvements in terminal infrastructure, maintenance and safety focused initiatives.

## OTHER EXPENSES

<i>(millions)</i>	Three months ended	
	March 31	
	2010	2009
Depreciation and amortization	\$ 24.8	\$ 25.2
Financing charges	9.3	10.9
General and administrative	10.9	9.9
Unrealized change in fair value of derivative financial instruments	(7.1)	21.5
Fees to General Partner	2.0	1.6
Provision for (recovery of) income taxes	9.0	(23.5)

### Depreciation and Amortization

Depreciation and amortization of tangible and intangible assets in the first quarter of 2010 was lower than the same period in 2009. In 2009, amortization of intangible assets included a \$1.8 million charge related to customer contracts that either expired or were terminated in the bulk liquid storage business. Overall depreciation was slightly higher due to depreciation of new assets now in service.

### Financing Charges

<i>(millions)</i>	Three months ended	
	March 31	
	2010	2009
Interest on credit facilities	\$ 4.8	\$ 8.6
Interest on loan payable to General Partner	5.8	6.0
Interest on debentures	1.6	1.6
Total financing charges	12.2	16.2
Capitalized interest	(3.1)	(5.3)
Amortization of transaction costs on long-term debt	0.2	-
	\$ 9.3	\$ 10.9

In the first quarter of 2010, average short-term interest rates decreased substantially compared to the first quarter of 2009. The weighted average interest rate on Inter Pipeline's credit facilities declined approximately 90 bps from 1.8% in the first quarter of 2009 to approximately 0.9% in 2010. Inter Pipeline's weighted average credit facility debt outstanding increased approximately \$234.7 million to \$1,942.2 million in the first quarter of 2010 compared to \$1,707.5 million in the same period in 2009 due to expenditures on the Corridor expansion project.

Interest expense on the loans payable to the General Partner decreased approximately \$0.2 million in the first quarter of 2010. The decrease is due to the expiration on January 1, 2010 of a temporary 25 bps increase that was added to the loans to accommodate the Corridor expansion. Fixed interest rates on each of the \$91.2 million and \$288.6 million loans outstanding decreased 25 bps to 5.85% and 6.15%, respectively.

Debenture interest expense in the first quarter of 2010 was consistent with 2009. Interest rates on these debentures are fixed, however Inter Pipeline had swap agreements in place on each of the \$150.0 million series A and B debentures that exchanged the fixed rates for variable rates. On February 2, 2010, the series A debentures matured and the associated interest rate swap agreement was terminated. On the same day, Corridor issued \$150.0 million of 4.897% fixed rate series C senior, unsecured debentures that mature February 3, 2020 without acquiring a corresponding swap agreement.

See the LIQUIDITY AND CAPITAL RESOURCES section for further information about Inter Pipeline's debt facilities and interest rate swaps.

## General and Administrative

<i>(millions)</i>	Three months ended	
	March 31	
	2010	2009
Canada	\$ 9.4	\$ 7.8
Europe	1.5	2.1
	\$ 10.9	\$ 9.9

In Canada, general and administrative expenses increased \$1.6 million in the first quarter of 2010 due to annual increases in employee compensation and other administrative costs. The increase in employee compensation primarily results from the revaluation of Inter Pipeline's long term deferred unit rights incentive plan.

In Europe, general and administrative expenses were down approximately \$0.6 million in the first quarter in 2010 as a result of foreign currency translation adjustments and sale of the bulk liquid trucking business.

### Unrealized Change in Fair Value of Derivative Financial Instruments

Inter Pipeline's mark-to-market valuation of its derivative financial instruments impacted net income favourably by \$7.1 million in the first quarter of 2010. Of this amount, changes in NGL forward prices between January and March of 2010 combined with changes in volumes of NGLs under purchase and sale swap contracts resulted in a favourable net income impact of \$14.6 million. In addition, changes in forward prices of foreign currency swaps between January and March of 2010 contributed a favourable \$4.3 million. These adjustments were partially offset by \$13.7 million of changes in forward prices of natural gas and volumes of natural gas under swap contracts between the same periods.

See the RISK MANAGEMENT AND FINANCIAL INSTRUMENTS section for additional information on Inter Pipeline's risk management initiatives.

### Fees to General Partner

In the first quarter of 2010, Inter Pipeline paid management fees to the General Partner of \$2.0 million (Q1 2009 - \$1.6 million). These fees are equivalent to 2% of "Operating Cash," as defined in the Limited Partnership Agreement (Partnership Agreement).

### Income Taxes

Consolidated income tax expense increased \$32.5 million from an income tax recovery of \$23.5 million in the first quarter of 2009 to an income tax expense of \$9.0 million in the first quarter of 2010. On March 4, 2009, the Government of Canada substantively enacted legislation that repealed the "provincial SIFT tax factor" and replaced it with a "provincial SIFT tax rate." Inter Pipeline calculated the "provincial SIFT tax rate" based on the general provincial corporate income tax rate for each province where it has a permanent establishment. For Inter Pipeline, this legislation reduced the provincial income tax rate for non-corporate entities from 13.0% to approximately 10.0% effective January 1, 2011 onward. This also reduced Inter Pipeline's estimated effective tax rate to 26.5% and 25.0% effective January 1, 2011 and January 1, 2012, respectively. As a result of this rate reduction, future income tax liabilities of non-corporate entities were reduced by \$24.0 million in the first quarter of 2009. The remainder of the variance results from changes in temporary differences relating to non-taxable Canadian partnership income.

## SUMMARY OF QUARTERLY RESULTS

	2008				2009				2010
(millions, except per unit and % amounts)	Second Quarter	Third Quarter	Fourth Quarter	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	First Quarter	
<b>Revenue</b>									
Oil sands transportation	\$ 38.5	\$ 35.2	\$ 35.1	\$ 33.6	\$ 30.6	\$ 32.2	\$ 34.1	\$ 34.9	
NGL extraction <sup>(1)</sup>	198.4	231.4	149.8	143.2	98.1	127.3	160.5	173.0	
Conventional oil pipelines	35.4	39.3	39.4	38.7	39.8	36.1	34.3	37.6	
Bulk liquid storage	33.8	34.9	35.5	30.1	28.8	28.9	28.2	26.0	
	\$ 306.1	\$ 340.8	\$ 259.8	\$ 245.6	\$ 197.3	\$ 224.5	\$ 257.1	\$ 271.5	
<b>Funds from operations<sup>(2)</sup></b>									
Oil sands transportation	\$ 19.0	\$ 15.1	\$ 17.3	\$ 18.0	\$ 17.9	\$ 18.6	\$ 19.4	\$ 18.6	
NGL extraction <sup>(1)</sup>	29.9	47.8	13.1	26.2	25.2	40.9	40.8	47.6	
Conventional oil pipelines	25.6	30.1	26.3	28.5	31.8	27.3	23.1	28.2	
Bulk liquid storage	10.1	10.9	11.3	10.5	9.9	10.6	10.4	10.3	
Corporate costs	(17.7)	(18.2)	(15.9)	(17.1)	(16.3)	(16.1)	(15.5)	(19.2)	
	\$ 66.9	\$ 85.7	\$ 52.1	\$ 66.1	\$ 68.5	\$ 81.3	\$ 78.2	\$ 85.5	
Per unit <sup>(2)</sup>	\$ 0.30	\$ 0.39	\$ 0.23	\$ 0.30	\$ 0.30	\$ 0.33	\$ 0.31	\$ 0.33	
Net income	\$ 10.3	\$ 76.8	\$ 102.5	\$ 43.4	\$ 39.3	\$ 51.9	\$ 23.1	\$ 61.7	
Per unit – basic & diluted	\$ 0.05	\$ 0.34	\$ 0.46	\$ 0.19	\$ 0.18	\$ 0.21	\$ 0.08	\$ 0.24	
Cash distributions <sup>(3)</sup>	\$ 46.6	\$ 46.7	\$ 46.8	\$ 46.9	\$ 48.6	\$ 52.4	\$ 54.5	\$ 57.6	
Per unit <sup>(3)</sup>	\$ 0.210	\$ 0.210	\$ 0.210	\$ 0.210	\$ 0.210	\$ 0.210	\$ 0.215	\$ 0.225	
Units outstanding (basic)									
Weighted average	221.8	222.3	222.8	223.4	227.0	248.7	252.8	255.8	
End of period	222.1	222.5	223.1	223.7	246.5	250.8	254.6	256.3	
Capital expenditures									
Growth <sup>(2)</sup>	\$ 118.7	\$ 151.6	\$ 101.0	\$ 57.0	\$ 46.0	\$ 417.0	\$ 53.5	\$ 31.2	
Sustaining <sup>(2)</sup>	3.1	3.5	5.2	2.9	3.6	4.0	7.4	2.5	
	\$ 121.8	\$ 155.1	\$ 106.2	\$ 59.9	\$ 49.6	\$ 421.0	\$ 60.9	\$ 33.7	
Payout ratio before sustaining capital <sup>(2)</sup>	69.7%	54.5%	89.7%	71.0%	71.0%	64.4%	69.6%	67.4%	
Payout ratio after sustaining capital <sup>(2)</sup>	73.1%	56.9%	99.7%	74.3%	75.0%	67.7%	76.9%	69.4%	
Total debt <sup>(4)</sup>	\$ 2,146.3	\$ 2,264.8	\$ 2,349.2	\$ 2,406.5	\$ 2,246.0	\$ 2,610.8	\$ 2,619.7	\$ 2,576.8	
Total partners' equity	\$ 1,064.9	\$ 1,075.7	\$ 1,130.2	\$ 1,130.5	\$ 1,315.5	\$ 1,319.3	\$ 1,320.1	\$ 1,314.2	
Enterprise value <sup>(2)</sup>	\$ 4,374.2	\$ 4,376.7	\$ 3,921.8	\$ 4,064.0	\$ 4,392.9	\$ 5,038.2	\$ 5,372.4	\$ 5,611.4	
Total recourse debt to capitalization <sup>(2)</sup>	42.7%	42.6%	41.6%	42.2%	32.3%	35.2%	35.7%	34.4%	
Total debt to total capitalization <sup>(2)</sup>	66.8%	67.8%	67.5%	68.0%	63.1%	66.4%	66.5%	66.2%	

(1) Significant changes in propane-plus commodity prices and foreign exchange rates resulted in lower revenue and funds from operations in the fourth quarter of 2008 through to the third quarter of 2009.

(2) Please refer to the NON-GAAP FINANCIAL MEASURES section of this MD&A.

(3) Cash distributions are calculated based on the number of units outstanding at each record date.

(4) Total debt includes long-term debt, short-term borrowings on demand loans before discounts and debt transaction costs.

## **LIQUIDITY AND CAPITAL RESOURCES**

Inter Pipeline's capital management objectives are aligned with its commercial growth strategies and long term outlook for the business. The primary objectives are to maintain:

- (i) stable cash distributions to unitholders over economic and industry cycles;
- (ii) a flexible capital structure which optimizes the cost of capital within an acceptable level of risk; and
- (iii) an investment grade credit rating.

Management may make adjustments to the capital structure for changes in economic conditions or the risk characteristics of the underlying assets. To maintain or modify the capital structure, Inter Pipeline may adjust the level of cash distributions paid to unitholders, issue new partnership units or new debt, renegotiate new debt terms or repay existing debt.

Inter Pipeline maintains flexibility in its capital structure to fund organic growth capital and acquisition programs throughout market and industry cycles. Funding requirements are projected to ensure appropriate sources of financing are available to meet future financial obligations and capital programs. Inter Pipeline generally relies on committed credit facilities and cash flow from its operations to fund capital requirements. At March 31, 2010, Inter Pipeline had access to committed credit facilities totaling \$2.9 billion, of which approximately \$995 million remains unutilized. Inter Pipeline also had access to unutilized demand facilities of approximately \$60 million. These facilities are available to fund foreseeable obligations, with certain amounts available to specific subsidiaries of Inter Pipeline.

Inter Pipeline also ensures a base of equity capital is available for some of its recently announced growth capital projects. Approximately \$17.5 million of equity was issued through the distribution reinvestment plan during the first three months of 2010.

Taking future market trends into consideration, Inter Pipeline regularly forecasts its operational requirements and expected funds from operations to ensure that sufficient funding is available for future sustaining capital programs and distributions to unitholders.

Inter Pipeline utilizes derivative financial instruments to minimize exposure to fluctuating commodity prices, foreign exchange and interest rates. Inter Pipeline's risk management policy defines and specifies the controls and responsibilities to manage market exposure to changing commodity prices (crude oil, natural gas, NGL and power) and changes within financial markets relating to interest rates and foreign exchange exposure. Further details of the risk management program are discussed in the RISK MANAGEMENT AND FINANCIAL INSTRUMENTS section.

## CAPITAL STRUCTURE

<i>(millions, except % amounts)</i>	Recourse	Non-recourse	March 31 2010	December 31 2009
<b>Credit facilities available</b>				
Corridor syndicated facility	\$ 488.0	\$ 1,654.0	\$ 2,142.0	\$ 2,142.0
Inter Pipeline syndicated facility	750.0	-	750.0	750.0
	1,238.0	1,654.0	2,892.0	2,892.0
Demand facilities <sup>(1)</sup>	20.0	40.0	60.0	60.0
	\$ 1,258.0	\$ 1,694.0	\$ 2,952.0	\$ 2,952.0
<b>Total debt outstanding</b>				
Recourse				
Corridor syndicated facility			\$ 138.2	\$ 123.6
Inter Pipeline syndicated facility			172.0	230.0
Loan payable to General Partner			379.8	379.8
Non-recourse				
Corridor syndicated facility			1,586.8	1,586.3
Corridor debentures			300.0	300.0
<b>Total debt</b> <sup>(1)(2)</sup>			2,576.8	2,619.7
Total partners' equity			1,314.2	1,320.1
<b>Total capitalization</b> <sup>(3)</sup>			\$ 3,891.0	\$ 3,939.8
Total debt to total capitalization <sup>(3)</sup>			66.2%	66.5%
Total recourse debt to capitalization <sup>(3)</sup>			34.4%	35.7%

(1) At December 31, 2009, outstanding Corridor letters of credit were approximately \$0.3 million which are not included in the demand loan facilities or total debt outstanding in the table above.

(2) At March 31, 2010, total debt includes long-term debt of \$2,567.7 million including discounts and debt transaction costs of \$9.1 million.

(3) Please refer to the NON-GAAP FINANCIAL MEASURES section of this MD&A.

Inter Pipeline's capital under management includes financial debt and partners' equity. Capital availability is monitored through a number of measures, including total recourse debt to capitalization and recourse debt to EBITDA. Capital management objectives are to provide access to capital at a reasonable cost while maintaining an investment grade long-term corporate credit rating and ensure compliance with all debt covenants. Financial covenants on Inter Pipeline's credit facilities are based on the amount of recourse debt outstanding. Management's objectives are to remain well below its maximum target ratio of 65% recourse debt to capitalization and maximum recourse debt to EBITDA ratio of 4.25. Recourse debt is attributed directly to Inter Pipeline and used in the calculation of its financial covenants. Inter Pipeline's recourse debt to capitalization ratio was a favourable 34.4% at March 31, 2010. Adjusting for the impact of non-recourse debt of \$1,886.8 million, Inter Pipeline's consolidated debt to total capitalization ratio was 66.2%.

At March 31, 2010, approximately \$2,005 million or 77.8% of Inter Pipeline's total consolidated debt was exposed to variable interest rates, however the debt financing costs related to \$1,875 million of variable rate Corridor credit facilities and debentures outstanding are directly recoverable through the terms of the Corridor FSA. Therefore, Inter Pipeline's direct interest rate risk associated with variable rate debt is only attributable to \$130 million or 5.0% of total outstanding debt. When deemed appropriate, Inter Pipeline enters into interest rate swap agreements to manage its interest rate risk exposure. In 2001, Inter Pipeline entered into two fixed interest rate swap agreements to manage a portion of its variable interest rate risk exposure. In 2007, Inter Pipeline acquired two variable interest rate swap agreements to manage fixed interest rate exposure on Corridor's 5 and 10-year debentures. The interest rate swap associated with Corridor's 5-year debentures was terminated when the underlying debenture matured on February 2, 2010.

	March 31 2010		December 31 2009	
Maturity date	Fixed Rate Per Annum (excluding applicable margin)	Notional Balance (millions)	Fixed Rate Per Annum (excluding applicable margin)	Notional Balance (millions)
Corridor debentures				
- Fixed to floating rate swap				
Series A - February 2, 2010	4.240%	\$ -	4.240%	\$ 150.0
Series B - February 2, 2015	5.033%	150.0	5.033%	150.0
		\$ 150.0		\$ 300.0
Inter Pipeline syndicated facility				
- Floating to fixed rate swap				
December 30, 2011 <sup>(1)</sup>	6.300%	\$ 27.0	6.300%	\$ 27.0
December 31, 2011	6.310%	15.0	6.310%	15.0
		\$ 42.0		\$ 42.0

(1) The notional principal balance of the \$27.0 million interest rate swap is reduced by \$1.0 million each year for the term of the arrangement.

Inter Pipeline has maintained its investment grade, long-term corporate credit rating of BBB with S&P since 2003. DBRS assigned Inter Pipeline an investment grade, long-term corporate credit rating of BBB coinciding with its acquisition of Corridor in 2007. Corridor's series B and C debentures have been assigned investment grade credit ratings of A(low), A3 and A- from DBRS, Moody's and S&P, respectively. In 2009, DBRS issued a revised outlook on both Corridor and Inter Pipeline, increasing the trend outlook from stable to positive, while S&P also increased the outlook on Corridor from stable to positive.

## CONTRACTUAL OBLIGATIONS, COMMITMENTS AND GUARANTEES

The following table summarizes Inter Pipeline's commitment profile and future contractual obligations at March 31, 2010. Management intends to finance these commitments through existing credit facilities and cash flow from operations. Longer term commitments will be funded through Inter Pipeline's capital management polices as discussed in the section above.

(millions)	Total	Less than one		
		year	1 to 5 years	After 5 years
<b>Capital expenditure projects</b>				
Oil sands transportation	\$ 354.0	\$ 247.4	\$ 78.0	\$ 28.6
NGL extraction	49.5	13.5	24.0	12.0
Conventional oil pipelines	6.5	6.5	-	-
Bulk liquid storage	14.4	14.4	-	-
Growth capital <sup>(1)</sup>	424.4	281.8	102.0	40.6
Sustaining capital <sup>(1)</sup>	15.5	15.5	-	-
	439.9	297.3	102.0	40.6
<b>Total debt<sup>(2)</sup></b>				
Corridor syndicated facility	1,725.0	138.2	1,586.8	-
Inter Pipeline syndicated facility	172.0	-	172.0	-
Loan to General Partner	379.8	-	379.8	-
Corridor debentures	300.0	-	150.0	150.0
	2,576.8	138.2	2,288.6	150.0
<b>Other obligations</b>				
Derivative financial instruments	23.7	18.9	4.8	-
Operating leases <sup>(3)</sup>	83.1	6.6	25.0	51.5
Purchase obligations <sup>(3)</sup>	22.6	4.2	10.7	7.7
Long term portion of incentive plan	2.5	2.5	-	-
Working capital deficit <sup>(1)</sup>	42.2	42.2	-	-
	\$ 3,190.8	\$ 509.9	\$ 2,431.1	\$ 249.8

(1) Please refer to the NON-GAAP FINANCIAL MEASURES section of this MD&A.

(2) Outstanding Corridor letters of credit of approximately \$0.3 million are not included in the total \$2,576.8 million of debt outstanding in the table above.

(3) Operating lease maturities and purchase obligations are based on contract terms as presented at December 31, 2009.

Inter Pipeline plans to invest approximately \$424.4 million in organic growth capital projects over the 2010 to 2012 period which includes final costs on the Corridor pipeline expansion project, capital costs for the recently announced \$135 million Polaris oil sands diluent transportation project and \$50 million sweetening project at the Cochrane NGL extraction facility. Inter Pipeline is also committed to investing capital in the bulk liquid storage business to comply with the UK's post Buncefield regulations. Potential solutions are being evaluated and expenditures are estimated to be in the range of \$4.6 million to \$9.3 million phased over the next ten years. Funding of significant capital projects is managed as discussed in the capital structure section.

At March 31, 2010, Inter Pipeline's debt matures at various dates up to February 2020. Corridor's series A debentures matured February 2, 2010 and Corridor's series B debentures will mature in February 2015. Corridor's series C debentures mature February 3, 2020. Amounts drawn on tranches A and B of Corridor's syndicated facility will mature in 2012. Amounts drawn on tranches C and D of this facility will mature the earlier of August 2012 and the commencement or suspension true-up date of the Corridor expansion project. Inter Pipeline's loan payable to the General Partner and Inter Pipeline syndicated facility mature in periods between 2012 and 2014.

The following future obligations resulting from the normal course of operations would be primarily funded from operations in the respective periods that they become due or may be funded through long-term debt.

- (i) Derivative financial instruments are utilized to manage market risk exposure to changes in commodity prices, foreign currencies and interest rates in future periods. This future obligation is an estimate of the fair value liability on an undiscounted basis for financially net settled derivative contracts outstanding at March 31, 2010, based upon the various contractual maturity dates.
- (ii) Operating leases and purchase obligations represent minimum payment obligations associated with leases and normal operating agreements for periods up to 2038.
- (iii) Working capital deficiencies arise primarily from capital expenditures outstanding in accounts payable at the end of a period, and fluctuate with changes in commodity prices.
- (iv) Inter Pipeline has obligations of \$16.7 million under its employee incentive plan, of which \$14.2 million is included in the working capital deficit.
- (v) Undiscounted asset retirement obligations of \$55.2 million at December 31, 2009 represent an estimate of future obligations for the retirement of NGL extraction and bulk liquid storage assets. Similarly, long term environmental liabilities of \$12.0 million represent an estimate of projects that Inter Pipeline is obligated to remediate in the future. Defined benefit pension obligations of \$11.1 million represent the unfunded portion of the European retirement plans at December 31, 2009. Since there is no specified timing for payment of these obligations, they were excluded in the table above.

On June 15, 2007, pursuant to the Corridor FSA, Inter Pipeline entered into a guarantee in favour of the Corridor shippers for the payment and performance of all obligations of Corridor, the General Partner or the operator (if the operator was not Inter Pipeline). This guarantee does not include those obligations for repayment of borrowed money or similar financial obligations incurred by these entities (except for funding certain cost overruns). The guarantee may be exercised in the event that Corridor, the General Partner or the operator (if the operator was not Inter Pipeline) fails to pay or perform such obligations for any reason.

## CASH DISTRIBUTIONS TO UNITHOLDERS

	Three months ended	
	March 31	
<i>(millions, except per unit and % amounts)</i>	2010	2009
Cash provided by operating activities	\$ 126.2	\$ 66.8
Net change in non-cash working capital	(40.7)	(0.7)
Less sustaining capital expenditures <sup>(1)</sup>	(2.5)	(2.9)
Cash available for distribution <sup>(1)</sup>	83.0	63.2
Change in discretionary reserves	(25.4)	(16.3)
Cash distributions	\$ 57.6	\$ 46.9
Cash distributions per unit <sup>(2)</sup>	\$ 0.225	\$ 0.210
Payout ratio before sustaining capital <sup>(1)</sup>	67.4%	71.0%
Payout ratio after sustaining capital <sup>(1)</sup>	69.4%	74.3%
Capital expenditures		
Growth <sup>(1)</sup>	\$ 31.2	\$ 57.0
Sustaining <sup>(1)</sup>	2.5	2.9
	\$ 33.7	\$ 59.9

(1) Please refer to the NON-GAAP FINANCIAL MEASURES section of this MD&A.

(2) Cash distributions are calculated based on the number of units outstanding at each record date.

It is the policy of the General Partner to provide unitholders with stable cash distributions over time. As a result, not all cash available for distribution is distributed to unitholders. Rather, a portion of cash available for distribution is reserved and reinvested in the business to effectively manage its capital structure, and in particular, debt levels. The General Partner makes its cash distribution decisions based on the underlying assumptions in each year's annual operating and capital budget and long term forecast, consistent with its policy to provide unitholders with stable cash distributions.

"Cash available for distribution" is a non-GAAP financial measure that the General Partner uses in managing Inter Pipeline's business and in assessing future cash requirements that impact the determination of future distributions to unitholders. Inter Pipeline defines cash available for distribution as cash provided by operating activities less net changes in non-cash working capital and sustaining capital expenditures. The impact of net change in non-cash working capital is excluded in the calculation of "Cash available for distribution" primarily to compensate for the seasonality of working capital throughout the year. Certain Inter Pipeline revenue contracts dictate an exchange of cash that differs, on a monthly basis, from the recognition of revenue. Within a 12-month calendar year, there is minimal variation between revenue recognized and cash exchanged. Inter Pipeline therefore excludes the net change in non-cash working capital in its calculation of cash available for distribution to mitigate the quarterly impact this difference has on cash available for distribution. The intent is to not skew the results of Inter Pipeline in any quarter for exchanges of cash, but to focus the results on cash that is generated in any reporting period.

In addition, in determining actual cash distributions, Inter Pipeline applies a discretionary reserve to cash available for distribution, which is designed to ensure stability of distributions over economic and industry cycles and to enable Inter Pipeline to absorb the impact of material one-time events. Therefore, not all cash available for distribution is necessarily distributed to unitholders. The reconciliation is prepared using reasonable and supportable assumptions, reflecting Inter Pipeline's planned course of action in light of management and the board of directors' judgment regarding the most probable set of economic conditions. Investors should be aware that actual results may vary, possibly materially, from such forward-looking adjustments.

The discretionary reserve increased approximately \$25.4 million in the first quarter of 2010 due primarily to the strong operating results of Inter Pipeline's business segments. Inter Pipeline will continue to manage the discretionary reserve and future cash distributions in accordance with its policy of attempting to manage the stability of distributions through industry and economic cycles.

The tables below show Inter Pipeline's cash distributions paid relative to cash provided by operating activities and net income (loss) for the periods indicated. See the OUTLOOK section of this report and RISK FACTORS section for further information regarding the sustainability of cash distributions.

<i>(millions)</i>	Three months ended March 31			Years ended December 31		
	2010	2009	2009	2008	2007	2006
Cash provided by operating activities	\$ 126.2	\$ 66.8	\$ 281.8	\$ 321.1	\$ 234.1	\$ 201.6
Cash distributions	(57.6)	(46.9)	(202.4)	(186.6)	(171.7)	(160.8)
Excess	\$ 68.6	\$ 19.9	\$ 79.4	\$ 134.5	\$ 62.4	\$ 40.8

<i>(millions)</i>	Three months ended March 31			Years ended December 31		
	2010	2009	2009	2008	2007	2006
Net income (loss)	\$ 61.7	\$ 43.4	\$ 157.7	\$ 249.7	\$ (80.0)	\$ 130.6
Cash distributions	(57.6)	(46.9)	(202.4)	(186.6)	(171.7)	(160.8)
Excess (shortfall)	\$ 4.1	\$ (3.5)	\$ (44.7)	\$ 63.1	\$ (251.7)	\$ (30.2)

Cash distributions in all periods are less than cash provided by operating activities and in the first quarter of 2010 and year ended 2008 were less than net income. Net income (loss) includes certain non-cash

expenses such as depreciation, future income taxes and unrealized changes in the fair value of derivative financial instruments therefore cash distributions may exceed net income.

The overall cash distributions of Inter Pipeline are governed by the Partnership Agreement, specifically section 5.2 of the Partnership Agreement, that specifies the terms for Inter Pipeline to make distributions of cash as defined in the Partnership Agreement (Distributable Cash) on a monthly basis, provided that Inter Pipeline has cash available for such payment (thereby excluding any cash withheld as a reserve). Distributable Cash is defined to generally mean cash from operating, investing and financing activities, less certain items, including any cash withheld as a reserve that the General Partner determines to be necessary or appropriate for the proper management of Inter Pipeline and its assets. As a result of the General Partner's discretion to establish reserves under the Partnership Agreement, cash distributed to unitholders is always equal to Distributable Cash.

## **OUTSTANDING UNIT DATA**

Inter Pipeline's outstanding units at March 31, 2010 are as follows:

<i>(millions)</i>	Class A	Class B	Total
Units outstanding	256.0	0.3	256.3

Inter Pipeline has 31,500 units reserved for issuance upon the exercise of vested Unit Incentive Options as at March 31, 2010. At May 4, 2010 Inter Pipeline had 256.2 million Class A units and 0.3 million Class B units for a total of 256.5 million units outstanding.

## **RISK MANAGEMENT AND FINANCIAL INSTRUMENTS**

### **MARKET RISK MANAGEMENT**

Inter Pipeline utilizes derivative financial instruments to manage liquidity and market risk exposure to changes in commodity prices, foreign currencies and interest rates. Risk management policies are intended to minimize the volatility of Inter Pipeline's exposure to commodity price, foreign exchange and interest rate risk to assist with stabilizing funds from operations. Inter Pipeline endeavours to accomplish this primarily through the use of derivative financial instruments. Inter Pipeline's policy prohibits the use of derivative financial instruments for speculative purposes. All hedging policies are authorized and approved by the board of directors through Inter Pipeline's risk management policy.

Inter Pipeline has the following types of derivative financial instruments: commodity price swap agreements, foreign currency exchange contracts, power price hedges, heat rate and interest rate swap agreements. The mark-to-market or fair value of these financial instruments are recorded as an asset or liability and any change in the fair value recognized as an unrealized change in fair value of these derivative financial instruments in the calculation of net income. When the financial instrument matures, any realized gain or loss is recorded in net income.

In the following sections, sensitivity analyses are presented to provide an indication of the amount that an isolated change in one variable may have on earnings<sup>1</sup>. Changes in fair value generally cannot be extrapolated based on one variable because the relationship with other variables may not be linear. In reality, changes in one variable may magnify or counteract the impact of another variable which may result in a significantly different conclusion. The sensitivity analyses in the following sections are based on the value of derivative financial instruments and long-term debt outstanding at March 31, 2010. The analyses are hypothetical and should not be considered to be predictive of future performance.

<sup>1</sup> Some of the sensitivity analyses presented below present the effect of reasonably possible changes in risk variables on essentially a pre-tax basis since prior to 2011, Inter Pipeline is only taxable on corporations within its organizational structure. Therefore the analyses in some of the sections below assume nil income tax impact.

## NGL Extraction Business

### Frac-spread Risk Management

Inter Pipeline is exposed to frac-spread risk which is the difference between the weighted average propane-plus price at Mont Belvieu, Texas and the monthly index price of AECO natural gas purchased for shrinkage calculated in USD/USG. Derivative financial instruments are utilized to manage frac-spread risk. Inter Pipeline transacts with third party counterparties to sell a notional portion of its NGL products and related notional quantities of natural gas at fixed prices. NGL price swap agreements are transacted in US currency therefore Inter Pipeline also enters into foreign exchange contracts to sell US dollars to convert notional US dollar amounts in the NGL swaps.

The following table presents the proportion of future propane-plus volumes hedged under contracts outstanding and the average net price of the frac-spread hedges at March 31, 2010 and May 4, 2010. The CDN/USG average prices would approximate the following USD/USG prices based on the average USD/CDN forward curve at March 31, 2010 and May 4, 2010, respectively.

	May 4, 2010				March 31, 2010			
	% Forecast Propane-plus Volumes Hedged	Average Price (CDN/USG)	Average Price (USD/USG)	% Forecast Propane-plus Volumes Hedged	Average Price (CDN/USG)	Average Price (USD/USG)	Average Price (USD/USG)	
April to December 2010	51%	\$ 0.74	\$ 0.72	51%	\$ 0.74	\$ 0.73	\$ 0.73	
January to December 2011	31%	\$ 0.75	\$ 0.73	21%	\$ 0.74	\$ 0.73	\$ 0.73	

Based on propane-plus volume hedges outstanding at March 31, 2010, the following table illustrates how a 10% change in NGL and AECO natural gas commodity prices or foreign exchange rates in isolation could individually impact the mark-to-market valuation of Inter Pipeline's derivative financial instruments and consequently after-tax income assuming rates associated with each of the other components and all other variables remain constant:

	Fair value of derivative financial instruments	Change in net income based on 10% increase in prices/rates <sup>(1)</sup>	Change in net income based on 10% decrease in prices/rates <sup>(1)</sup>
NGL <sup>(2)</sup>	\$ 5.3	\$ (12.7)	\$ 12.7
AECO natural gas	(19.6)	4.1	(4.1)
Foreign exchange	3.5	(13.2)	13.2
Frac-spread risk management	\$ (10.8)		

(1) Negative amounts represent a liability increase or asset decrease. Changes related to 2011 contracts are net of tax of 26.5%.

(2) Assumes that a commodity price change will impact all propane, normal butane, isobutane and pentanes-plus products linearly.

### Power Price Risk Management

Inter Pipeline uses derivative financial instruments to manage power price risk in its NGL extraction and conventional oil pipelines business segments. In 2009, Inter Pipeline entered into financial heat rate swap and electricity price swap contracts to manage electricity price risk exposure in these businesses.

Based on heat rate swaps outstanding in the NGL extraction business at March 31, 2010, a 10% change in Alberta power pool commodity prices in isolation with all other variables held constant, could potentially change the mark-to-market valuation of Inter Pipeline's derivative financial instruments used to manage power price risk and consequently after-tax income by approximately \$0.7 million. A 10% change in AECO natural gas prices in isolation with all other variables held constant, could potentially

change the mark-to-market valuation of Inter Pipeline's derivative financial instruments used to manage power price risk and consequently after-tax income by approximately \$0.6 million.

Based on electricity price swap agreements outstanding in the conventional oil pipelines business at March 31, 2010, a 10% change in Alberta power pool commodity prices in isolation with all other variables held constant, could potentially change the mark-to-market valuation of Inter Pipeline's derivative financial instruments used to manage power price risk and consequently after-tax income by approximately \$0.1 million.

## **Bulk Liquid Storage Business**

### **Foreign Exchange Risk Management**

Inter Pipeline is exposed to currency risk resulting from the translation of assets and liabilities of its European bulk liquid storage operations and transactional currency exposures arising from purchases in currencies other than Inter Pipeline's functional currency, the Canadian dollar. Transactional foreign currency risk exposures have not been significant historically, therefore are generally not hedged; however, Inter Pipeline may decide to hedge this risk in the future.

## **Corporate**

### **Interest Rate Risk Management**

Inter Pipeline's exposure to interest rate risk primarily relates to its long-term debt obligations and fair valuation of its floating-to-fixed interest rate swap agreements. Inter Pipeline manages its interest rate risk by balancing its exposure to fixed and variable rates while minimizing interest costs. When deemed appropriate, Inter Pipeline enters into interest rate swap agreements to manage its interest rate price risk exposure.

Based on the variable rate obligations outstanding at March 31, 2010, a 1% change in interest rates at this date could affect interest expense on credit facilities and consequently pre-tax income by approximately \$4.7 million, assuming all other variables remain constant. Of this amount, \$4.3 million relates to the \$2.1 billion Corridor credit facility and are also recoverable in pre-tax income through the terms of the Corridor FSA. A 1% change in interest rates at March 31, 2010 could also affect the mark-to-market valuation of Inter Pipeline's derivative financial instruments used to manage interest rate risk and consequently after-tax income by approximately \$0.5 million, assuming all other variables remain constant.

## **Realized and Unrealized Gain (Loss) on Derivative Instruments - Held-for-Trading**

Derivative financial instruments designated as "held-for-trading" are recorded on the consolidated balance sheet at fair value. Any gain or loss upon settlement of these contracts is recorded as a realized gain or loss in net income. Prior to settlement, any change in the fair value of these instruments are recognized in net income as an unrealized change in fair value of derivative financial instruments.

The fair values of derivative financial instruments are calculated by Inter Pipeline using a discounted cash flow methodology with reference to actively quoted forward prices and/or published price quotations in an observable market and market valuations provided by counterparties. Forward prices for NGL swaps are less transparent because they are less actively traded. Forward prices are assessed based on available market information for the time frames for which there are derivative financial instruments in place. Fair values are discounted using a risk-free rate plus a credit premium that takes into account the credit quality of the instrument.

Gains (losses) on derivative financial instruments recognized in the calculation of net income are as follows:

	Three months ended	
	March 31	
(millions)	2010	2009
<b>Realized (loss) gain on derivative financial instruments</b>		
Revenues		
NGL swaps	\$ (1.4)	\$ 18.8
Foreign exchange swaps (frac-spread hedges)	0.1	(6.3)
	(1.3)	12.5
Shrinkage gas expense		
Natural gas swaps	(2.1)	(5.2)
Operating expenses		
Electricity price swaps	(0.1)	-
Heat rate swaps	(0.1)	0.5
	(0.2)	0.5
Financing charges		
Interest rate swaps	1.4	1.3
<b>Total realized (loss) gain on derivative financial instruments</b>	<b>(2.2)</b>	<b>9.1</b>
<b>Unrealized gain (loss) on derivative financial instruments</b>		
NGL swaps	14.6	(13.2)
Natural gas swaps	(13.7)	(8.2)
Foreign exchange swaps (frac-spread hedges)	4.3	0.6
Electricity price swaps	(0.1)	-
Heat rate swaps	1.5	(0.7)
Interest rate swaps	0.7	0.2
Transitional transfers <sup>(1)</sup>	(0.2)	(0.2)
<b>Total unrealized gain (loss) on derivative financial instruments</b>	<b>7.1</b>	<b>(21.5)</b>
<b>Total gain (loss) on derivative financial instruments</b>	<b>\$ 4.9</b>	<b>\$ (12.4)</b>

(1) Transfer of gains and losses on derivatives previously designated as cash flow hedges from accumulated other comprehensive income.

## CREDIT RISK

Inter Pipeline's credit risk exposure relates primarily to customers and financial counterparties holding cash and derivative financial instruments, with a maximum exposure equal to the carrying amount of these instruments. Credit risk is managed through credit approval and monitoring procedures. The creditworthiness assessment takes into account available qualitative and quantitative information about the counterparty including, but not limited to, financial status and external credit ratings. Depending on the outcome of each assessment, guarantees or some other credit enhancement may be requested as security. Inter Pipeline attempts to mitigate its exposure by entering into contracts with customers that may permit netting or entitle Inter Pipeline to lien or take product in kind and/or allow for termination of the contract on the occurrence of certain events of default. Each business segment monitors outstanding accounts receivable on an ongoing basis.

Concentrations of credit risk associated with accounts receivable relate to a limited number of principal customers in the oil sands transportation and NGL extraction business segments, the majority of which are affiliated with investment grade corporations in the energy and chemical industry sectors. At March 31, 2010, accounts receivable associated with these two business segments were \$76.0 million or 71% of total accounts receivable outstanding. Inter Pipeline believes the credit risk associated with the remainder of accounts receivable is minimized due to diversity across business units and customers.

With respect to credit risk arising from cash, deposits and derivative financial instruments, Inter Pipeline believes the risk of non-performance of counterparties is minimal as cash, deposits and derivative financial instruments outstanding are predominantly held with major financial institutions or investment grade corporations.

Inter Pipeline actively monitors the risk of non-performance of its customers and financial counterparties. At March 31, 2010, accounts receivable outstanding meeting the definition of past due and impaired is immaterial.

## **TRANSACTIONS WITH RELATED PARTIES**

No revenue was earned from related parties in the quarters ended March 31, 2010 or 2009.

Upon acquisition of the General Partner in 2002, Pipeline Assets Corp. (PAC), the sole shareholder of the General Partner, assumed the obligations of the former general partner of Inter Pipeline under a support agreement. The support agreement obligates the affiliates controlled by PAC to provide certain personnel and services if requested by the General Partner, to fulfill its obligations to administer and operate Inter Pipeline's business. Such services are incurred in the normal course of operations and amounts paid for such services are at cost for the services provided. No amounts have been paid under the terms of the support agreement since PAC acquired its interests in the General Partner.

The General Partner's 0.1% interest in Inter Pipeline, represented by Class B units, is controlled by PAC. The General Partner is a wholly owned subsidiary of PAC, a corporation controlled solely by the Chairman of the Board of the General Partner. Certain officers and directors of the General Partner have non-voting shares in PAC that entitle them to dividends. The entitlement to retain these shares of PAC and to receive dividends is tied, in part, to the continuing employment or service as a director or officer of the General Partner. Officers and directors of the General Partner received \$0.2 million (Q1 2009 - \$0.3 million) in dividends in the first quarter of 2010 from PAC pursuant to their ownership of non-voting shares.

Under the Partnership Agreement, the General Partner is entitled to recover all direct and indirect expenses, including general and administrative expenses, incurred on behalf of Inter Pipeline. The General Partner also receives an annual base fee equal to 2% of Inter Pipeline's annual "Operating Cash" as defined in the Partnership Agreement. In addition, the General Partner is entitled to earn an annual incentive fee of between 15% and 35% of Inter Pipeline's annual Distributable Cash as defined in the Partnership Agreement in excess of \$1.01 per unit to \$1.19 per unit respectively; an acquisition fee of 1.0% of the purchase price of any assets acquired by Inter Pipeline (excluding the pipeline assets originally acquired); and a disposition fee of 0.5% of the sale price of any assets sold by Inter Pipeline. See the Other Expenses section of RESULTS OF OPERATIONS for details of fees paid to the General Partner during the period.

In 2004, Inter Pipeline entered into a loan agreement with the General Partner for \$379.8 million. At the same time, the General Partner had received \$379.8 million by way of a Private Placement note issuance to a combination of American and Canadian institutional investors and immediately loaned the funds to Inter Pipeline. At March 31, 2010, interest payable to the General Partner on the loan was \$10.0 million (March 31, 2009 - \$10.3 million). This loan to Inter Pipeline from the General Partner has the identical repayment terms and commitments as the notes payable by the General Partner to the institutional note holders, except for an interest rate increase of 0.05% over the rates payable on the notes issued by the General Partner. Inter Pipeline has guaranteed the notes issued by the General Partner to the note holders. The guarantee may be exercised in the event of default by the General Partner pursuant to the terms of the Note Purchase Agreement and is equal to the amount of principal outstanding at the time of default, including a premium of 50 bps over the implied yield to maturity, accrued interest and, if applicable, swap breakage costs.

Amounts due to/from the General Partner and its affiliates related to services are non-interest bearing and have no fixed repayment terms with the exception of the loan agreement with the General Partner

as noted above. At March 31, 2010, there were amounts owed to the General Partner by Inter Pipeline of \$0.7 million (March 31, 2009 – \$0.6 million).

## **CONTROLS AND PROCEDURES**

Management has made no material changes to the design of Inter Pipeline's internal control over financial reporting during the first quarter of 2010.

## **CRITICAL ACCOUNTING ESTIMATES**

The preparation of Inter Pipeline's consolidated financial statements requires management to make critical and complex judgments, estimates and assumptions about future events, when applying GAAP, that have a significant impact on the financial results reported. These judgments, estimates, and assumptions are subject to change as future events occur or new information becomes available. Readers should refer to note 1 *Summary of Significant Accounting Policies* of the December 31, 2009 consolidated financial statements for a list of Inter Pipeline's significant accounting policies.

There were no changes in Inter Pipeline's critical accounting estimates as disclosed in its annual 2009 MD&A that affected the disclosure or the accounting for its operations for the quarter ended March 31, 2010.

## **CHANGES IN ACCOUNTING POLICIES**

### **FUTURE**

#### **International Financial Reporting Standards (IFRS)**

All Canadian publicly accountable enterprises will be required to adopt IFRS for interim and annual reporting periods for fiscal years beginning on or after January 1, 2011. Inter Pipeline commenced its IFRS conversion project in 2008 and established a project team to successfully manage the transition to IFRS within the required timeframe. The project team consists of a steering committee, project and functional team leaders that include management from finance, investor relations, tax, compliance and information technology, among others. Quarterly updates are provided to the audit committee.

Cross functional teams have been established to focus on assessing IFRS accounting policy options, generate appropriate recommendations and identify the related implications throughout the assessment process. The project plan has been designed with some flexibility to be able to adapt to standard changes as new accounting developments are made by the Canadian Accounting Standards Board and International Accounting Standards Board (IASB) to ensure full compliance on adoption of IFRS.

The two key elements of the project plan are: financial statement compliance with IFRS and the related business impact. Financial statement compliance with IFRS consists of four phases as discussed in the table below. The related business impact element of the project will ensure that teams consider, on a timely basis, the implication of any prospective change in accounting standards on other areas of the business. This includes, but is not limited to, information system infrastructure and processes, business agreements and financing arrangements, key metrics and the control environment.

Financial Statement Compliance with IFRS	Milestones / Deadlines
<p>Initial impact assessment phase</p> <ul style="list-style-type: none"> <li>➤ Initial identification of the major differences between current Canadian GAAP and IFRS standards and assessment of the impact of these differences into high, medium and low categories in terms of the complexity of implementation and prospective timelines.</li> </ul>	Completed.
<p>Research and planning phase</p> <ul style="list-style-type: none"> <li>➤ Research specific differences between the standards, long-term and transitional options available and prospective changes to the IFRS standards prior to 2011. Identify potential implications on accounting policies and processes, business management, information systems, control environment and educational requirements. Develop a formal plan and timeline to meet project objectives.</li> </ul>	Research substantially completed subject to monitoring updates as IFRS standards change.
<p>Solution development phase</p> <ul style="list-style-type: none"> <li>➤ Quantify and evaluate transitional and long-term options available and select the most appropriate policies.</li> </ul>	In process with financial statements to be fully compliant with IFRS for the 2011 fiscal year.
<p>Implementation phase</p> <ul style="list-style-type: none"> <li>➤ Integrate solutions into the underlying financial processes and systems.</li> </ul>	

The project is progressing according to plan. The initial impact assessment, research and planning phases are largely complete based on current IFRS standards. Inter Pipeline has not yet determined the full accounting effects of adopting IFRS as some accounting policy alternatives and implementation decisions are still being evaluated. Based on the work completed to date and since all potential changes to IFRS that will be effective at December 31, 2011 are not yet known, Inter Pipeline cannot reasonably quantify the full impact that adopting IFRS may have on its current and future financial results and key financial metrics.

Inter Pipeline will continue to present its results for fiscal 2010 using GAAP. In fiscal 2011, Inter Pipeline will present its results under the principles of IFRS, with the 2010 results restated for comparative purposes. A summary of IFRS standards expected to have an impact on Inter Pipeline's financial reporting are discussed in the following sections. This summary is not intended to be an exhaustive list of all actual or potential differences between IFRS and Canadian GAAP that will result from transition to IFRS. It should also be noted that the International Accounting Standards Board (IASB) have significant ongoing projects that could affect the ultimate differences between GAAP and IFRS and the impact on Inter Pipeline's consolidated financial statements on transition and in future. The project team will continue to monitor changes to existing IFRS standards through to the IFRS convergence date.

#### **Exposure Draft - Joint Arrangements**

Exposure Draft 9 – “*Joint Arrangements*” (ED 9) is expected to become an IFRS standard in the second quarter of 2010 replacing IAS 31 *Interests in Joint Ventures*. ED 9 sets out the basis of accounting required for arrangements whereby assets, operations or entities are under joint control. The exposure draft currently proposes that entities account for interests in jointly controlled entities using the equity method of accounting and proposes elimination of the option to proportionately consolidate these entities.

Currently, Inter Pipeline uses the proportionate consolidation method to account for its 85% interest in the Cold Lake LP and 50% interest in the assets of the Empress V facility. Under proportionate consolidation, an entity recognizes a proportionate share of the results of operations, financial position and cash flows on a line by line basis in the respective financial statements. Although consolidated net income and partners' equity would be the same under both accounting methods, reported assets, liabilities, operating results and cash flows reported under an equity method of accounting would be significantly different. The equity method of accounting requires all individual asset and liability line items, such as cash and cash equivalents, accounts receivable, property, plant and equipment, accounts

payable and accrued liabilities to be netted as an “investment” in one line on the statement of financial position. Similarly, revenues and expenses would be combined in one line on the statement of net income. The statement of cash flows would reflect only cash distributions received and contributions made by Inter Pipeline rather than funds from operations. As a result, there would be a difference between consolidated cash provided by operating activities and funds from operations reported when there is a difference between Inter Pipeline’s reported share of the net income and cash distributions received in a period.

Under the proposed ED 9, Cold Lake LP may be considered a jointly controlled entity, therefore may be required to be accounted for under the equity method of accounting versus proportionate consolidation. Empress V assets would be considered jointly controlled assets, therefore would continue to be accounted for under an accounting method similar to proportionate consolidation. As this is an exposure draft, the full extent of the impact of applying ED 9 cannot be made at this time, pending further certainty as to the final standard on accounting for joint arrangements.

#### **Property, plant and equipment**

IAS 16 – “*Property, plant and equipment*” (IAS 16) contains the same basic principles of accounting as GAAP, however differences in application exist. For example, capitalization of directly attributable costs in accordance with IFRS may include additional costs or exclude certain costs previously recognized under GAAP, such as the mandatory capitalization of directly attributable borrowing costs as required by IAS 23 – “*Borrowing costs.*” IFRS also provides specific guidance on capitalizing items such as spare parts, inspection costs and major overhauls. IAS 16 requires an entity to allocate items of property, plant and equipment into significant components and depreciate each component separately. This method of componentizing property, plant and equipment may result in an increase in the number of component parts recorded and change in the calculation of depreciation expense.

The major difference between IFRS and GAAP is an option under IAS 16 to choose either a cost or fair value model to value each class of property, plant and equipment. In addition, IFRS 1 – “*First time adoption of IFRS*” (IFRS 1) allows an entity to measure an item of property, plant and equipment at fair value on the IFRS transition date and use this value as deemed cost in future periods. Pursuant to current GAAP requirements, Inter Pipeline uses an historical cost model to value property, plant and equipment. Inter Pipeline intends to continue with a cost valuation model for its more significant assets on transition to IFRS as management considers cost to be a more consistent measure of value given the nature of its assets.

#### **Provisions, Contingent Liabilities and Contingent Assets**

IAS 37 – “*Provisions, contingent liabilities and contingent assets*” (IAS 37) requires a provision to be recognized when: (i) there is a present obligation (legal or constructive) as a result of a past transaction or event; (ii) it is probable that an outflow of resources will be required to settle the obligation; and (iii) a reliable estimate can be made of the obligation. Based on the guidance, IAS 37 is more specific in its requirement to record provisions including provisions for asset retirement and abandonment obligations. Inter Pipeline has not historically recorded an asset retirement obligation associated with its conventional oil pipelines and oil sands transportation business assets as the timing of settlement and magnitude of the future obligation is not determinable. In January 2010, the IASB issued an exposure draft “*Measurement of Liabilities in IAS 37*” with proposed amendments to IAS 37 expected to become an IFRS standard in the second half of 2010. The impact of IAS 37 on Inter Pipeline has not been fully determined at this time and is pending further review.

#### **Asset Impairment**

GAAP generally uses a two-step approach to impairment testing: first comparing asset carrying values with undiscounted future cash flows to determine whether impairment exists; and then measuring any impairment by comparing asset carrying values with fair values. IAS 36 – “*Impairment of Assets*” (IAS 36) uses a one-step approach for both testing for and measurement of impairment, with asset carrying values compared directly with the higher of fair value less costs to sell and value in use (which uses discounted future cash flows). This may potentially result in more write downs where carrying values of assets were previously supported under GAAP on an undiscounted cash flow basis, but could not be supported on a discounted cash flow basis. The extent of any write downs may be partially offset by the

requirement under IAS 36 to reverse any previous impairment losses where circumstances have changed such that the impairments have been reduced. GAAP prohibits reversal of impairment losses.

#### **Income Taxes**

IAS 12 - "Income Taxes" (IAS 12) prescribes that an entity account for the tax consequences of transactions and other events in the same way that it accounts for the transactions and other events themselves. Therefore, where transactions and other events are recognized in earnings, the recognition of deferred tax assets or liabilities which arise from those transactions should also be recorded in earnings. For transactions that are recognized outside of the statement of earnings, either in other comprehensive income or directly in equity, any related tax effects should also be recognized outside of the statement of earnings.

The most significant impact of IAS 12 on Inter Pipeline will be derived from accounting policy decisions made under other IFRS standards. Therefore, the impact on Inter Pipeline of accounting for the tax consequences of transactions and other events under IFRS versus GAAP cannot be fully determined at this time and is pending further review.

#### **IFRS 1 First-Time Adoption of International Financial Reporting Standards**

IFRS 1 provides a framework for the first time adoption of IFRS with a number of one-time optional exemptions and mandatory exceptions to retrospective application of a number of IFRS standards. In general, an entity is required to apply the principles under IFRS on the basis that an entity has prepared its financial statements in accordance with IFRS since its formation. These one-time optional exemptions and mandatory exceptions are provided to assist entities overcome difficulties associated with reformulating historical accounting information from GAAP to IFRS. IFRS 1 also specifies that adjustments that arise on retrospective conversion to IFRS should be directly recognized in opening retained earnings or partners' equity in Inter Pipeline's case. Inter Pipeline is considering these transitional elections concurrent with the review of the respective IFRS standards and transitional elections are pending further review.

## **2009**

### **Goodwill and Intangible Assets**

In February 2008, the CICA issued Section 3064 - "Goodwill and Intangible Assets" and amended Section 1000 - "Financial Statement Concepts" to clarify the criteria for the recognition of assets, intangible assets and internally developed intangible assets. Items that no longer meet the definition of an asset are no longer recognized as assets. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. Standards concerning goodwill and research and development costs are unchanged from the standards included in the previous Section 3062. The standards are applicable on a retrospective basis with restatement to financial statements relating to fiscal years beginning on or after October 1, 2008. The adoption of this standard in 2009 had no impact on Inter Pipeline's consolidated financial statements.

### **Credit risk and the Fair Value of Financial Assets and Financial Liabilities**

In January 2009, the Emerging Issues Committee (EIC) issued a new abstract EIC-173 "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities". The EIC concluded that an entity's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and liabilities, including derivative financial instruments. Inter Pipeline had previously incorporated the credit risk of counterparties in fair value calculations.

### **Financial Instrument Disclosures**

During 2009, CICA Handbook Section 3862 "Financial Instruments - Disclosures" (HB 3862) was amended to include enhanced disclosures about inputs to fair value measurement, including their classification within a hierarchy that prioritizes the inputs to fair value measurement. The three levels of the fair value hierarchy are as follows:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices in active markets that are observable for the asset or liability either directly or indirectly; and
- Level 3 – Inputs that are not based on observable market data.

The amendments to HB 3862 also clarify and enhance liquidity risk disclosures for financial and derivative financial liabilities and strengthen the relationship between qualitative and quantitative disclosures about liquidity risk. HB 3862 was adopted by Inter Pipeline in the financial statements for the year ended December 31, 2009. The amendments are to be applied prospectively, and comparative information was not required in the first year of adoption.

## RISK FACTORS

During the first quarter of 2010, there were no significant changes to Inter Pipeline’s operating activities that would affect the disclosure of risk factors as discussed in its 2009 annual MD&A.

## NON-GAAP FINANCIAL MEASURES

Certain financial measures referred to in this MD&A, namely “adjusted working capital deficiency”, “cash available for distribution”, “EBITDA”, “enterprise value”, “funds from operations”, “funds from operations per unit”, “payout ratio after sustaining capital”, “payout ratio before sustaining capital”, “growth capital expenditures”, “sustaining capital expenditures”, “total debt to total capitalization” and “total recourse debt to capitalization” are not measures recognized by GAAP. These non-GAAP financial measures do not have standardized meanings prescribed by GAAP and therefore may not be comparable to similar measures presented by other entities. Investors are cautioned that these non-GAAP financial measures should not be construed as alternatives to other measures of financial performance calculated in accordance with GAAP.

The following non-GAAP financial measures are provided to assist investors with their evaluation of Inter Pipeline, including their assessment of its ability to generate cash and fund monthly distributions. Management considers these non-GAAP financial measures to be important indicators in assessing its performance.

**Adjusted working capital deficiency** is calculated by subtracting current liabilities from current assets including cash and excluding the fair value of derivative financial instruments, short-term borrowings and current portion of long-term debt.

<i>(millions)</i>	March 31 2010	December 31 2009
Current assets		
Cash and cash equivalents	\$ 23.2	\$ 18.2
Accounts receivable	108.1	122.1
Prepaid expenses and other deposits	16.7	17.9
Current liabilities		
Cash distributions payable	(19.2)	(19.1)
Accounts payable and accrued liabilities	(138.5)	(136.9)
Deferred revenue	(32.5)	(12.3)
Adjusted working capital deficiency	\$ (42.2)	\$ (10.1)

**Cash available for distribution** includes cash provided by operating activities less net changes in non-cash working capital and sustaining capital expenditures. This measure is used by the investment community to calculate the annualized yield of the units.

**EBITDA and funds from operations** are reconciled from the components of net income as noted below. Funds from operations are expressed before changes in non-cash working capital. **Funds from operations**

**per unit** are calculated on a weighted average basis using basic units outstanding during the period. These measures, together with other measures, are used by the investment community to assess the source and sustainability of cash distributions.

<i>(millions)</i>	Three months ended	
	March 31	
	2010	2009
Net income	\$ 61.7	\$ 43.4
Depreciation and amortization	24.8	25.2
Non-cash expenses	(2.2)	-
Unrealized change in fair value of derivative financial instruments	(7.1)	21.5
Future income tax expense	8.3	(24.0)
Funds from operations	85.5	66.1
Financing charges	9.1	10.9
Current income tax expense	0.7	0.5
EBITDA	\$ 95.3	\$ 77.5

**Enterprise value** is calculated by multiplying the period-end closing unit price by the total number of units outstanding and adding total debt (excluding discounts and debt transaction costs). This measure, in combination with other measures, is used by the investment community to assess the overall market value of the business. Enterprise value is calculated as follows:

<i>(millions, except per unit amounts)</i>	March 31	December 31
	2010	2009
Closing unit price	\$ 11.84	\$ 10.81
Total closing number of Class A and B units	256.3	254.6
Market capitalization	3,034.6	2,752.7
Total debt	2,576.8	2,619.7
Enterprise value	\$ 5,611.4	\$ 5,372.4

**Growth capital expenditures** are generally defined as expenditures which incrementally increase cash flow or earnings potential of assets, expand the capacity of current operations or significantly extend the life of existing assets. This measure is used by the investment community to assess the extent of discretionary capital spending.

**Sustaining capital expenditures** are generally defined as expenditures which support and/or maintain the current capacity, cash flow or earnings potential of existing assets without the associated benefits characteristic of growth capital expenditures. This measure is used by the investment community to assess the extent of non-discretionary capital spending.

<i>(millions)</i>	Three months ended March 31			
	2010		2009	
	Growth	Sustaining	Total	Total
Oil sands transportation	\$ 25.6	\$ -	\$ 25.6	\$ 44.3
NGL extraction	0.5	0.5	1.0	5.5
Conventional oil pipelines	2.5	1.4	3.9	1.9
Bulk liquid storage	2.6	0.6	3.2	8.2
	\$ 31.2	\$ 2.5	\$ 33.7	\$ 59.9

**Payout ratio after sustaining capital** is calculated by expressing cash distributions declared for the period as a percentage of cash available for distribution after deducting sustaining capital expenditures for the period. This measure, in combination with other measures, is used by the investment community to assess the sustainability of the current cash distributions.

**Payout ratio before sustaining capital** is calculated by expressing cash distributions paid for the period as a percentage of cash available for distribution before deducting sustaining capital. This measure, in combination with other measures, is used by the investment community to assess the sustainability of the current cash distributions.

**Total debt to total capitalization** is calculated by dividing the sum of total debt, including short-term borrowings and demand facilities and excluding discounts and debt transaction costs, by total capitalization. Total capitalization includes the sum of total debt (as above) and partners' equity. Similarly, **total recourse debt to capitalization** is calculated by dividing the sum of debt facilities outstanding with recourse to Inter Pipeline (excluding discounts and debt transaction costs) by total capitalization excluding outstanding debt facilities with no recourse to Inter Pipeline. These measures, in combination with other measures, are used by the investment community to assess the financial strength of the entity.

## **ELIGIBLE INVESTORS**

Only persons who are residents of Canada, or if partnerships, are Canadian partnerships, in each case for purpose of the Income Tax Act (Canada) are entitled to purchase and own Class A units of Inter Pipeline.

## **ADDITIONAL INFORMATION**

Additional information relating to Inter Pipeline, including Inter Pipeline's Annual Information Form, is available on SEDAR at [www.sedar.com](http://www.sedar.com). Inter Pipeline's Statement of Corporate Governance is included in Inter Pipeline's Annual Information Form.

The MD&A has been reviewed and approved by the Audit Committee and the Board of Directors of the General Partner.

**Dated at Calgary, Alberta this 6th day of May, 2010.**