Examination in Chief
Panel 1
Opening Remarks

February 20, 2014

Customized IR Plan Overview

- Five-year revenue cap with annual adjustments
- Productivity built into O&M and capital forecasts
- Sustainable Efficiency Incentive Mechanism (SEIM) will incent the Company to find sustainable efficiencies
- Sharing of benefits through the Earnings Sharing Mechanism (ESM), but EGD absorbs 100% of downside
- Deferral and Variance accounts
- Performance Reporting and Monitoring
- Z-factor
- Off-ramps

Why this approach?

- Company’s extraordinary capital requirements
- Traditional I-X IRM will not recover costs nor provide EGD the opportunity to earn a Fair Return
- Revenue cap provides rate predictability
- Future revenues decoupled from future costs - Company accepts and will manage this risk
- The IRM is informed by the “Custom IR” model and “Building Blocks” approach
- Consistent with OEB’s objectives and embodies the fundamental elements of Incentive Rate plans

Consistent with OEB objectives

- Custom IR one of three methods for electric utilities in RRFE
  "… most appropriate for distributors with significantly large multi-year or highly variable investment commitments that exceed historical levels."
- Sets rates for five years, embeds productivity, provides incentives to find further efficiencies and to manage costs tightly
- Protects the interests of consumers with respect to price, reliability and quality of service
- Establishes incentives for sustainable efficiency improvements
- Creates an environment conducive to investment for the benefit of customers and shareholders

Other models do not work for Enbridge over this period

- We evaluated three primary alternatives to the proposed Plan
  - I-X
  - I-X plus Y factors for GTA and Ottawa
  - I-X plus a General Purpose Capital Tracker (ICM)
- Also examined the I-X approach embodied in the Union Settlement
- Reasonable I and X factors will recover projected operating expenses, but <u>none</u> of these approaches would recover capital and a fair return

Staff and Stakeholder Questions

- Evidence of Productivity?
  - Extensive evidence provided to explain how the operating and capital cost forecasts were developed, how the company iterated on those forecasts to trim them and prioritize expenditures, and why the requested budgets are reasonable
  - Productivity challenges are embedded within the cost forecasts
  - Third party validated the productivity of the company with benchmarking analysis, TFP analysis, and O&M projection vs. an I-X rate path

Staff and Stakeholder Questions

- Cost of Service or Targeted PBR Model?
  - Proposed plan is neither COS nor a targeted PBR plan
  - The Customized IR plan is a comprehensive model that addresses both O&M and Capital costs
  - EGD’s proposed plan is a multi-year revenue cap, with built-in productivity
  - With the revenue cap in place, future revenues are decoupled from future costs

Staff and Stakeholder Questions

- Shifting risk to ratepayers?
  - No, the establishment of five years of Allowed Revenues creates asymmetrical risks for the ratepayer and shareholder
  - Cost forecasts set today may differ from actual revenue requirements
  - EGD's shareholder bears risks associated with revenues falling short of approved amounts
  - If EGD performs well, it will share earnings with ratepayers

Staff and Stakeholder Concerns

- Adequacy of incentives and reasonableness of forecasts?
  – Allowed distribution revenue fixed for 5 years
  – Company at risk for additional capital spending or O&M
  – Company will be challenged to meet the budgeted cost forecasts
  – Additional incentives through ESM and SEIM
  – Thorough and complete evidence on capital spending required for a safe and reliable system

Customer interests are well served

- Substantial and necessary investments for safety and reliability
- Predictable rate path
- Customer distribution bills projected to increase on average by 1.4% annually, well below inflation
- EGD is incented to find sustainable efficiencies
- Lower gas costs from the GTA project