Ontario Energy Board

Commission de l'énergie de l'Ontario

EB-2012-0459

IN THE MATTER OF AN APPLICATION BY

Enbridge Gas Distribution Inc.

2014 - 2018 Rate Application

DECISION WITH REASONS

July 17, 2014

EB-2012-0459

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O.1998, c.15, (Schedule B);

AND IN THE MATTER OF an Application by Enbridge Gas Distribution Inc. for an order or orders approving or fixing rates for the sale, distribution, transmission and storage of gas commencing January 1, 2014.

BEFORE: Paula Conboy
Presiding Member

Cynthia Chaplin
Member

Emad Elsayed
Member

DECISION WITH REASONS

July 17, 2014

Table of Contents

Introduction

Enbridge Gas Distribution Inc. is a natural gas distributor serving about two million customers primarily in the Toronto, Ottawa, and Niagara areas of Ontario. Enbridge has applied to the Ontario Energy Board for approval of new distribution rates. The application relates to the costs for distribution infrastructure, pipelines, compressor stations, metering, customer service, and all the other activities of a distributor - everything except the commodity costs of the natural gas.[1]

Enbridge can only charge rates which are approved by the Board, but the company is responsible for proposing specific rates and supporting those proposals with evidence. After conducting a public hearing, which includes the participation of customer representatives and other interested stakeholders, the Board may approve the proposals, may reject the proposals and direct the company to re-apply, or may modify the proposals and implement different rates. The Board's authority in this area is set out in section 36 of the *Ontario Energy Board Act*.

In the past, Enbridge has applied for rates for one year, or for as long as 5 years using a formulaic adjustment mechanism. Enbridge's current application is quite different. The company has provided five years of forecast data and is seeking approval now for rates for each of those five years, although some adjustments would be made each year for certain pre-determined factors. If Enbridge's application were approved in full, residential ratepayers would see their rates decrease somewhat in 2014 and then increase each year between 2015 and 2018. The specific rate changes proposed by Enbridge are set out in the table below.

Residential Rate Impacts (Proposed)

	2014	**2015**	**2016**	**2017**	**2018**
Rate Increase (Proposed)	-1.7%	2.1%	4.6%	2.4%	2.5%

[1] Enbridge recently received approval to charge higher natural gas commodity charges. That was a separate application process, under EB-2014-0039.

Often Enbridge has been able to reach a negotiated settlement with the participants in its rates proceedings, most of whom represent different groups of ratepayers. The negotiations were not successful this time, so all of the issues are being decided by the Board through this decision. All of the information and evidence related to this hearing is available on the Board's website under the file number EB-2012-0459.

The Board has decided to approve Enbridge's proposed approach, but with a number of important modifications. The modifications will reduce the rate impacts, incent Enbridge to become more efficient, and reduce the risk to ratepayers if Enbridge's major capital projects go over budget. Details about each of the issues in this application are contained in this decision. Once the company has received the decision, it will make the necessary calculations to determine the final rates. Once those are available, the specific impacts on ratepayers will be known with greater certainty. However, the Board expects the results of its decision to be little or no change to the rate reduction in 2014 and somewhat lower rate increases in 2015 through 2018 than Enbridge proposed.

As part of this application, Enbridge also sought approval to change how it accounts for the costs to remove assets from service, known as "site restoration costs". In changing the method used, Enbridge and its advisors have concluded that more money has been collected from ratepayers than is now considered necessary. As a result, there will be a refund to ratepayers over the next five years, which is separate from the rate changes described above. The Board has decided to accept Enbridge's proposal but with modifications which will result in a somewhat larger refund to ratepayers.

A significant number of issues are addressed in this decision. The overarching issue is which rate setting mechanism should be used, and the Board addresses that issue first in the next section. Subsequent sections address the specific components of the rate plan, the budgets which support the plan, and the associated accounting, rate design and implementation issues.

Rate Setting Mechanism

Enbridge proposed a five-year Custom Incentive Rate-setting ("Custom IR") plan to begin January 1, 2014. If approved, the plan would fix Enbridge's allowed distribution revenue ("Allowed Revenue") for each year in the five-year term based on a forecast of capital and operating costs, inclusive of productivity savings. The proposed revenue requirement for 2014 is $1,009 million, rising to an estimated $1,292 million in 2018.

The concept of any incentive rate-setting approach is that it decouples costs from the rates that a distributor charges for its services. This is deliberate and is designed to incent more efficient performance. The approach provides the opportunity for a distributor to earn, and potentially exceed, the allowed rate of return on equity. The Board monitors the company's results over the term of the plan to ensure that the company is actually finding productivity improvements and not simply cutting costs in a way which compromises safety, reliability or other important customer metrics. The Board also monitors the company's financial results over the plan term to make sure that the company did not over-forecast its costs at the outset of the plan.

The Board has been regulating natural gas and electricity utilities under IR plans for years and the approach has been widely used in other jurisdictions such as the Great Britain and Australia. In 2005, the Board set out the criteria for natural gas utility IR plans in its Natural Gas Forum ("NGF") Report. Electricity distributors have been under some form of IR regulation since 2000. Most recently, the Board issued its Renewed Regulatory Framework for Electricity Distributors ("RRFE")[2] report in which the Board outlines a new five-year Custom IR option for electricity distributors, along with a traditional IR option and an Annual IR option.

Enbridge explained that in developing its proposal, it was guided by the NGF Report and the RRFE Report as well as a "building blocks" ratemaking model that has been used in Great Britain and Australia. Enbridge's proposed Custom IR plan and its last IR plan both relied on forecasts of costs and revenues. However, in the last IR ("traditional IR"), rates for the first year were set on a single forward test-year cost of service (or "base" year) basis. Rates for subsequent years of the plan were set using an index based on an externally derived inflation factor and productivity adjustment. These annual rate adjustments recognize that costs rise with inflation but also that a company should be

[2] *Report of the Board: Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach*, October 18, 2012.

striving for continuous improvement in productivity. In the current application, Enbridge proposed to set its rates for 2014 through 2018 based on a five-year forecast of its revenue requirement and sales volumes. Some annual adjustments are proposed for certain pre-determined factors; these are discussed further elsewhere in this decision.

Most parties opposed Enbridge's proposal and many argued that the Board should impose a traditional IR plan on the company.

Board Findings

Enbridge's application for a "Custom IR plan" is the first of its kind since the Board issued its RRFE Report. The RRFE Report was targeted explicitly to electricity distributors. However, the objectives and principles in the RRFE Report are consistent with those of the earlier NGF Report which focused exclusively on natural gas. In many important respects the Board's policy articulated in the RRFE Report is the natural evolution of the Board's thinking in the areas of both natural gas and electricity rate-setting. It is therefore appropriate that Enbridge looked to the RRFE Report for guidance on developing its plan.

Each Custom IR application will be considered on an individual basis. Indeed, one of the purposes of the Custom IR option is to provide a utility with the opportunity to tailor its rate profile to meet its specific needs. However, an applicant for Custom IR is also responsible for providing a robust plan which is properly documented and supported. This initial Custom IR application by Enbridge has been a significant learning experience for all parties and for the Board as it works to implement its new policy framework. It is the Board's expectation that this decision will provide further guidance on the interpretation and implementation of the Board's rate-setting policies.

Enbridge submitted that a Custom IR is appropriate given its extraordinary capital requirements, especially its GTA and Ottawa projects and its Work and Asset Management project. Together, these projects raise the capital expenditures over the 2014 to 2018 period by approximately 28% above what Enbridge termed its "core capital" requirements.[3] The company also noted that its increasing depreciation costs, productivity challenges and uncertainty about its other capital spending requirements contributed to the need for the Custom IR framework. Enbridge claimed that it would not be able to provide safe and reliable service to its customers if the company were subject to the formulaic adjustments approved under a traditional IR.

[3] Enbridge defines "core capital" as "…all capital spending, except for three identified major projects: the GTA and Ottawa Reinforcements and the Work and Asset Management Project (WAMS)."

Enbridge also maintained that the Custom IR plan will benefit customers by supporting necessary investment to ensure safe and reliable service. In Enbridge's view, customers and the company will benefit from the establishment of rates for a five-year period because it will produce fair and predictable rates while reducing regulatory burden. Under Enbridge's proposal customer distribution bills are projected to increase by an average of 2% annually, with an initial reduction followed by increases above expected inflation. The Board has indicated that distributors whose capital needs are expected to be comparatively stable over time should be able to operate under the traditional IR plan. Intervenors argued that there are provisions under the traditional IR that could accommodate the three major projects and that the company could operate safely and reliably under traditional IR because the company's core capital is relatively stable.

The Board finds that Enbridge's capital requirements are sufficient to support the request for a Custom IR. Other approaches could have been used, for example the Incremental Capital Module that is available to electricity distributors under traditional IR or the Y factor approach negotiated by Union Gas, but it is open to a utility to request a Custom IR if the expenditures are significant and if the application is adequately supported. As the Board stated in the RRFE Report:

> *The Custom IR method will be most appropriate for distributors with significantly large multi-year or highly variable investment commitments that exceed historical levels.*[4]

Many parties also argued that the traditional IR model contained in Union Gas' Settlement Agreement and subsequently approved by the Board (EB-2013-0202) should be applied to Enbridge. The Board does not accept this argument. The Board has long indicated its reluctance to impose a negotiated settlement from one utility to another without a thorough analysis of the circumstances for each utility. In accepting settlement agreements, the Board has made it clear that there is no precedential value in the individual components of a settlement agreement as all settlements contain trade-offs. The Board will not impose the Union Gas Settlement Agreement on Enbridge.

In its RRFE Report, the Board indicated that a distributor applying for Custom IR would need to file robust evidence and external benchmarking to support the reasonableness of its forecasts, especially given the recognized incentive to over-forecast, the uncertainties with long-term forecasting, and the level of rate increases projected (higher than under traditional IR). The Board also identified its expectation that a distributor would file a

[4] RRFE Report, p. 19.

comprehensive asset management plan that is linked to the capital budget and operationalized to support the prioritization of decisions and the optimization of utility assets. A distributor would need to demonstrate its ability to manage within the rates set, given that actual costs and revenues will ultimately vary from forecast.

Parties argued that Enbridge has not provided sufficiently robust evidence on its costs and revenues that would allow the Board to set rates that are just and reasonable for the next five years. Specifically parties criticized the benchmarking work which compared Enbridge to a number of peer US companies. Enbridge retained Concentric Energy Advisors Inc. ("Concentric") to undertake benchmarking analysis and Mr. Coyne from Concentric provided expert evidence at the oral hearing. The Concentric studies concluded that Enbridge is among the most efficient of its US peers in most categories measured. Enbridge argued that Concentric's benchmarking analysis confirms that the company is among the most efficient. Board staff retained Pacific Economics Group Research LLC ("PEG") to undertake analysis of the Enbridge proposal, and Dr. Kaufmann from PEG provided expert evidence at the oral hearing. Dr. Kaufmann was of the opinion that the benchmarking analyses were inadequate. Most parties supported Dr. Kaufmann's analysis and argued that the benchmarking analysis provided by Concentric was flawed and could not be relied upon to reach conclusions as to the efficiency level of Enbridge or the reasonableness of its budgets.

The Board finds that there are significant limitations to the benchmarking analysis. First, it is not a total cost benchmarking. Other than net plant per customer the Concentric analysis did not include capital costs in its benchmarking and yet capital represents approximately 65% of the total costs in this case. The RRFE Report is clear that the Board will use total cost benchmarking. Mr. Coyne and Dr. Kaufmann did prepare ad hoc measures of total unit cost during the proceeding. In the case of Dr. Kaufmann, the results suggest that Enbridge is not as efficient as Enbridge claims to be. Second, there are significant concerns with the comparator group developed by Concentric, which was driven significantly by weather considerations. Dr. Kaufmann disagreed that weather would be a significant factor. The evidence was not conclusive one way or the other regarding the importance of weather, however, because of its reliance on the weather factor, the Concentric comparator group included companies which in other important respects are not comparable to Enbridge and excluded companies which in other important respects are comparable to Enbridge. In particular, the comparator group contains a number of older northeast utilities which still have large amounts of cast iron and bare steel pipe, which Enbridge has mostly replaced, and the group excludes almost all the rapidly growing utilities, of which Enbridge is one. The Concentric analysis did not adequately examine the impact of using other criteria for its selection process.

The Board finds that because of these limitations the benchmarking evidence does not support a conclusion that Enbridge is particularly efficient. Without this external analysis, the Board must rely on the internal analysis of the budget and the company's own plans for productivity improvements. This is discussed further in later sections of this decision.

Enbridge, however, has committed to developing a benchmarking study that attempts to address both capital and operating costs and to holding a consultation with stakeholders that will allow for review of and feedback on the benchmarking study. Based on the results of the consultation, Enbridge proposed to develop a benchmarking study to be filed on rebasing which, Enbridge intends, will use a methodology that has been accepted by all parties, including Board staff and its expert. The Board views this as an important and valuable commitment and therefore will not reject the Custom IR proposal on the grounds of insufficient benchmarking. The Board will accept Enbridge's proposal but expects that Enbridge's benchmarking work will be supported by independent expert opinion. In addition, the Board will require Enbridge to report on its progress in this area as part of its annual reporting. For purposes of current rate setting, the Board will address the shortcomings in the current benchmarking through suitable modifications to the Custom IR plan.

The Board also finds that there is limited external analysis of Enbridge's capital and operating and maintenance budgets. Enbridge maintained that there is no requirement in the Board's RRFE Report that benchmarking evidence must be filed by an applicant.

Enbridge interpreted the RRFE Report's wording to mean that an applicant, Board staff, or any other party may provide benchmarking evidence. However, the RRFE Report is quite clear that the Board expects such analysis to be presented in the application:

> *In addition, the Board sees merit in receiving the evidence of third party experts as part of a distributor's application, or retaining its own third party experts, in relation to the review and assessment of distributor asset management and network investment plans (along with other evidence filed by the distributor).*[5]

Enbridge submitted, however, that it did engage experts who rendered opinions on specific programs which have been filed in evidence (e.g. WAMS, AMP Fitting

[5] RRFE Report, p. 37.

Replacement program). Those studies were useful, but the Board's evaluation of the reasonableness of Enbridge's proposed capital forecasts would have greatly benefited from more extensive external independent analysis. The Board does not accept Enbridge's view that such independent assessment cannot be conducted. It is the Board's expectation in a Custom IR application with a significant capital component that the applicant will provide the necessary support, including independent total-cost benchmarking and independent assessment. Enbridge also argued that the hearing process itself provides a form of third-party expert assessment. While the analysis and arguments presented through the public hearing process are an important part of the Board's decision making process, independent expert opinion is a different sort of analysis and equally valuable to the Board.

As a result of the lack of an independent expert assessment as well as shortcomings related to the benchmarking analyses, the Board has concluded that there is insufficient evidence to support the proposed allocation of risk between the company and ratepayers in the area of capital expenditures and insufficient productivity in the area of operating and maintenance expenditures. Each of these is addressed in detail later in this decision.

However, the Board recognizes that this is the first Custom IR application which the Board has received. Being the first, Enbridge has had to deal with a high level of uncertainty as to how the parties and the Board would apply the policy principles in the NGF Report and RRFE Report to a specific case.

The Board concludes that it better serves the public interest to approve Enbridge's Custom IR plan, with appropriate modifications, than to reject the application or impose an alternative model. The Board reaches this conclusion for two reasons: Enbridge's willingness to modify its proposals and the Board's ability to remedy the shortcomings of the plan through suitable modifications.

Enbridge has continued to show a willingness to address the concerns raised throughout the proceeding and to propose alternatives. In particular, the original application included a proposal that the company's 2017 and 2018 capital budgets would be determined midway through the Custom IR term. In response to stakeholder concerns, the company agreed to assume greater capital risk by updating its application to use the 2016 capital budget (excluding the Work and Asset Management System project) as the forecast for 2017 and 2018. Enbridge also agreed to additional stakeholder consultation and annual reporting. The Board concludes that each of these modifications represents a significant improvement in the Custom IR plan.

The Board will make further modifications to the plan to enhance customer benefits during the Custom IR plan and reduce the risks to customers. The modifications include the following:

- The Earnings Sharing Mechanism has been modified to provide greater benefits to ratepayers.
- The Sustainable Efficiency Incentive Mechanism proposal has not been approved as proposed.
- A variance account for the GTA Project will not be established, thereby reducing the risk to ratepayers.
- A threshold will be applied to the Mains Relocations and Mains Replacement Variance Accounts, to reduce the risk to ratepayers.
- Operating and Maintenance costs have been reduced to allocate more efficiency benefits to ratepayers.
- The Cost of Capital will be re-set each year using the Board’s established approach.

Each of these modifications is discussed in detail later in this decision. The Board will also implement a number of reporting requirements in order to monitor Enbridge’s performance against the plan. Other modifications have been made as well, which are not directly related to the specific rate-setting mechanism. Detail on those subjects also appear later in this decision.

It is the Board’s intention that this decision will provide guidance to future applicants, although the Board recognizes that each Custom IR application will have unique characteristics.

The remaining sections of this decision address the following major topics:

- The Custom IR components
- The volume and revenue forecast underpinning Enbridge’s plan
- Capital expenditures

- Operating and maintenance expenditures
- Cost of capital
- Site Restoration Costs
- Deferral and variance accounts
- Cost allocation and rate design
- Reporting
- Implementation

Plan Components

Enbridge's proposed Custom IR includes a number of factors which are also used in traditional IR. These include an Earnings Sharing Mechanism, a Z Factor, and an off-ramp. Enbridge proposed an additional factor, a Sustainable Efficiency Incentive Mechanism. Each of these will be addressed in this section. Parties also made proposals regarding adjustments for 2013 results for purposes of setting rates going into the Custom IR. The Board will address that issue first.

Adjustments for 2013 Results

Enbridge's 2013 financial results show that the company earned 148 basis points above the return on equity that underpins Enbridge's 2013 Board approved rates (or $31.2 million gross basis inclusive of tax). Intervenors argued that the Board should reduce the 2014 base by the $31.2 million 2013 revenue sufficiency. They submitted that this would result in a more realistic base year starting point for the Custom IR which limits the recovery in rates to the Board approved return. Without the adjustment, intervenors argued, Enbridge would build up significant overearnings over the 5 year plan. The Association of Power Producers of Ontario ("APPrO") claimed that Enbridge's 2013 over earnings imply that the 2013 Board approved revenues and cost projections were conservative in Enbridge's favour. The Building Owners and Managers Association (Toronto) ("BOMA") pointed to the recent Union Gas 2014-2018 IRM Settlement Agreement (EB-2013-0202), in which Union Gas agreed to reduce its 2014 revenue requirement by $4.5 million to compensate for 2013 over earnings.

Enbridge provided explanations for the factors that contributed to the 2013 revenue sufficiency and stated that the sufficiency does not change the forecast risk in the 2014 through 2018 forecasts. In Enbridge's view, these factors were either one-time events or beyond the company's ability to control. In all instances, according to Enbridge, the factors are not indications of expected future revenue sufficiency.

Enbridge also argued that by advocating for a $31.2 million adjustment, the intervenors were essentially inappropriately introducing an earnings sharing mechanism into a cost of service year (which typically does not have an earnings sharing mechanism) and attributing ratepayers with 100% of the benefits.

Board Findings

The Board does not accept that Enbridge is necessarily starting its custom IR period with a built in revenue sufficiency from 2013. A Custom IR is not set based on a single cost of service year the way Enbridge's prior traditional IR plan was. A Custom IR is based on five-year forecasts of costs. Once set, the company is then required to operate within that envelope for the next 5 years. This proceeding provides a complete look at all the costs for the next 5 years and therefore adjustments for whether the company over- or under-earned in the previous year would not be appropriate. However, the fact that Enbridge has been able to consistently over-earn in every year under its last IR plan will inform the Board's thinking on what is required to operate the business going forward.

Parties noted that Union Gas agreed to a reduction in 2014 to compensate for over-earnings in 2013. However, Union Gas adopted a traditional IR plan, not a Custom IR plan. At the time of Enbridge's 2013 settlement, the parties may have expected that 2013 would be followed by a traditional IR plan. However, the 2013 settlement agreement made no provision for an alternative outcome and did not include an earnings sharing mechanism. The Board subsequently issued its RRFE Report that provided for a Custom IR option. Enbridge used the report as guidance and submitted a Custom IR plan. It would be inappropriate to impose an Earnings Sharing Mechanism for 2013 after the fact.

Earnings Sharing Mechanism ("ESM")

An Earnings Sharing Mechanism ("ESM") is a tool which provides for benefit sharing between ratepayers and shareholders if the company earns more than its allowed return during the IR term. The form of ESM that Enbridge has proposed going forward is similar to that approved in its prior IR plan and includes three components:

- Under-earnings: if the weather normalized return is less than the allowed ROE, the under-earnings will be borne entirely by the shareholders.
- A "dead band": if the weather normalized return is less than 100 basis points above the allowed ROE, then ratepayers receive no benefit and all of the extra earnings flow to the shareholders.
- A sharing ratio above the "dead band": if the weather normalized return is more than 100 basis points above the allowed ROE, the extra earnings will be shared 50:50 between ratepayers and shareholders.

None of the parties disputed that an ESM plan was appropriate. However, views differed as to the operation of the dead band and the sharing ratio.

Board Findings

The Board will establish an ESM for Enbridge's Custom IR. The ESM will provide a performance incentive to Enbridge while at the same time ensuring that ratepayers share in the benefits for that performance.

All parties, including Enbridge, agreed that the "allowed" ROE for purposes of calculating the ESM should be the ROE used to determine the allowed revenue requirement. The Board will adopt this approach because it ensures that the earnings sharing is based on weather normalized actual results compared to what is embedded in rates.

Many parties argued that ratepayers are bearing greater risks under Enbridge's proposed Custom IR plan relative to its prior plan, and that the ESM should be adjusted so that the ratepayers' share of the benefits is larger. The parties argued that the lack of independent third-party cost benchmarking leads to an incentive for Enbridge to over-forecast costs and under-forecast earnings. Intervenors recommended a variety of approaches:

- Energy Probe Research Foundation ("Energy Probe"), with the support of School Energy Coalition ("SEC") and Canadian Manufacturers and Exporters ("CME") proposed that there be no dead band and that the first 100 basis points of over-earnings should accrue entirely to ratepayers while the next 100 basis points of over-earnings should accrue entirely to Enbridge. Any earnings over 200 basis points should be shared 90:10 in favor of ratepayers.
- Consumers Council of Canada ("CCC") proposed the elimination of the dead band and a 50:50 sharing of all of the over-earnings.
- APPrO also recommended a 50:50 sharing of all of the over-earnings for the first 100 basis points, beyond which, the benefits should be shared 90:10 in favour of the ratepayer.

Enbridge argued that changing the parameters of an already asymmetrical ESM further in favour of ratepayers should be balanced against the fact that an IR plan is meant to incent a utility to find and implement sustainable efficiencies. In reply, Enbridge proposed an approach that would still allow the company to retain the first 100 basis points of over-earnings, but then it would share any over-earnings beyond that level on a 90:10 basis in favour of ratepayers.

The Board finds that the dead band should be eliminated and that all over-earnings will be shared 50:50 between ratepayers and shareholders. The Board agrees that the central issue is that the sharing with ratepayers needs to be balanced with an incentive to find and retain efficiencies. The Board also agrees with CCC that a key consideration is the overall IR framework and the other parameters. The Board is approving a Custom IR for Enbridge, but must address the shortcomings of the plan. The lack of total cost benchmarking and the lack of independent budget assessments result in a greater risk that costs have been over-forecast. Therefore, the Board concludes that additional ratepayer protection is warranted. A 100 basis point dead band provides insufficient protection for ratepayers, and therefore the Board finds that the dead band should be eliminated for this Custom IR plan. However, the Board is also concerned that there be suitable performance incentives for Enbridge and finds that a sharing ratio of 90:10 in favour of ratepayers largely eliminates the performance incentive for Enbridge. The Board finds that a sharing ratio of 50:50 provides a suitable incentive level for the company while still ensuring significant benefits for ratepayers. The Board also addresses risk sharing and efficiency levels further in the capital expenditure and O&M expenditure sections of this decision.

Sustainable Efficiency Incentive Mechanism (“SEIM”)

Enbridge proposed a Sustainable Efficiency Incentive Mechanism (“SEIM”) which it claims will promote long-term sustainable efficiencies within the custom IR framework, including near the end of the IR term. Enbridge explained that IR plans tend to incent short-term cost cutting and discourage the adoption of new productivity measures near the end of the plan term. The SEIM is an attempt to address these issues by providing a financial reward to the company for undertaking sustainable efficiency improvements.

The proposed SEIM has three steps, which would be undertaken within Enbridge’s rebasing application for 2019:

- Calculating the potential reward: The potential reward would equal one half of the difference between the average ROE achieved during the IR term and the average ROE allowed during the IR term. The potential reward would form a premium on the ROE that applies to rates for the rebasing year and the following year (2019 and 2020). The potential reward for each year would be capped at 50 basis points above the allowed ROE. The ROE premium would be expressed as a dollar amount, based on the forecast 2019 rate base.

- Determining whether the potential reward is justified: To qualify for the SEIM reward, Enbridge must show that the net present value of the long-term benefits generated by productivity initiatives undertaken during the IR term is greater than the reward. The company must also show that its Service Quality Reporting performance has been maintained at or above the 2013 level for at least three of the five years of the IR term.

- Implementing the reward: If Enbridge is successful in establishing its entitlement to a SEIM reward, then the reward would be administered within the 2019 rebasing case and the 2020 rates case. The reward amount would be added to the revenue requirement in the rebasing year for collection in that year. The same amount would be applied to the 2020 rates.

Board staff and intervenors opposed the proposal. While a number of parties supported the objectives of the SEIM and commended Enbridge on its efforts, they concluded that the flaws were too significant to go forward as proposed. APPrO, Energy Probe and SEC each proposed alternatives.

Board Findings

The Board will not accept the current SEIM proposal. The Board finds that there are significant flaws in the proposal which make it likely that the objectives will not be achieved. The Board does see merit in a mechanism which serves to incent long-term sustainable productivity improvements. The Board is also encouraged by Enbridge’s ongoing commitment to improving the proposal and addressing the concerns raised. The Board concludes that Enbridge should undertake a consultation process over the next year, in order to address the concerns identified below (and in parties’ submissions) and to develop a revised proposal to bring forward as part of its 2015 or 2016 rates application.

CME argued that there is no need for a SEIM because it is redundant in an IR plan which already includes incentives. CME submitted that a more appropriate way of ensuring the achievement of sustainable efficiencies during an IR plan is to penalize a distributor for creating efficiencies which are not sustainable. Enbridge responded that it is a reasonable inference from the importance attached to the discussion of “incentives for sustainable efficiency improvements" within the NGF Report that the Board recognized the need for a specific incentive for sustainable efficiencies. The Board finds merit in two approaches to encouraging greater efficiency: robust forecasts which incorporate expected efficiency improvements during the IR term and the potential for carry-over incentives for sustainable efficiency improvements near the end of the IR term. Dr. Kaufmann and Ms. Frayer[6] each acknowledged that one of the shortcomings of IR is a focus on short-term cost-cutting rather than sustainable efficiency improvements, particularly at the end of the plan term. The Board finds that it is appropriate in a Custom IR plan to attempt to address this shortcoming.

A number of parties argued that the SEIM issue should be considered and determined in a generic proceeding because it has application to all distributors. The Board is examining this issue through its electricity rate-setting policy consultations. However, the Board finds that it is appropriate to address Enbridge's proposal within the context of the current application and to allow Enbridge to undertake a focussed consultation to develop a revised proposal within the overall framework of its Custom IR.

The Board finds that the following aspects of the current SEIM proposal are of particular concern:

- The reward will be cash to the utility while the benefits to ratepayers are in the form of forecast future savings, which are not verified. This is an imbalance which should be addressed.
- The proposal does not appear to distinguish between early term productivity measures and late-term productivity measures, and therefore may not adequately address the concern about diminishing incentives to invest in productivity toward the end of an IR term.
- The SEIM has the potential to reward inflated forecasts for capital or operating expenditures.
- It is not clear whether grossing up the reward for taxes is a balanced approach given the method by which the ratepayer benefits are determined.

Both APPrO and Energy Probe made a number of specific proposals. The Board encourages parties to consider these, as well as other alternatives, as part of the consultation process.

[6] Enbridge retained London Economics International LLC ("LEI") to provide analysis of incentive regulation, and Ms. Frayer of LEI testified at the oral hearing.

SEC proposed that the Board indicate that when Enbridge files its rebasing application, it may be eligible for an additional incentive if it can demonstrate that its costs going forward have been reduced by initiatives implemented during IR. The method for calculating the incentive would be decided in the rebasing application, taking into consideration the amount, nature and certainty of the future savings, the savings already achieved during the IR plan, and the level of increase or decrease in revenue requirement being proposed by the company on rebasing. Enbridge was not opposed to this suggestion. The Board concludes that if the consultation does not reach a proposal which is supported by the parties, then the company may proceed as suggested by SEC.

Z-Factor

Enbridge proposed that the Z-factor should continue to apply to protect the company and ratepayers from unexpected costs, and proposed that it should apply where the revenue requirement impact is more than $1.5 million per year and the costs are outside of management control. Enbridge proposed to modify the description and criteria from what was approved in the prior IR plan. In Enbridge's view, the criteria in the company's prior IR plan were difficult to interpret and apply, and the proposed changes would make the evaluation of Z-factor requests more clear and consistent.

Currently, Z-factors must be linked to a specific "event"; Enbridge proposed to change that to specific "cause". The company maintained that this was appropriate because it changes the focus from a singular event to all the costs at issue when there may be a combination of related events all linked to one cause. Under the proposed wording, it would be necessary for the company to demonstrate that the causes that led to cost increases or decreases were unexpected, non-routine and outside of management control.

Enbridge's witnesses expressed concern that with the original wording there did not appear to be anything that would qualify as a Z-factor. Enbridge cited the Board's denial of its application for two Z-factors (EB-2011-0277) under the prior IR plan as evidence that the wording of the Z-factor criteria was inappropriate.

Dr. Kaufman expressed concern that the linkage to a "cause" would often be subtle, complex and difficult to identify, whereas an "event" would be discrete, concrete and readily identifiable. He concluded that the result of Enbridge's proposal would be to expand the scope of Z-factor and to potentially lead to expensive regulatory investigations.

For example, under the proposed wording, Enbridge could file a Z-factor application whenever a cause arose that the company had not anticipated when preparing its plan.

Dr. Kaufman also suggested that the criteria related to “management control” should be amended using clearer language such as “the cost must be beyond what the company management could reasonably control or prevent through the exercise of due diligence”.

Intervenors did not support Enbridge’s proposal.

Board Findings

The two primary areas of dispute are the change from “event” to “cause” in the criteria, and the maintenance of the threshold at $1.5 million.

With respect to the criteria, the Board has been clear in its approach to Z-factors. Z-factors are intended to provide for unforeseen events outside of management’s control, regardless of the multi-year rate-setting mechanism at the time of the event. The cost to a distributor must be material and its causation clear. The Board does not agree with Enbridge’s suggestion that previous Z-factor applications were denied because the wording was unclear or the language was so stringent that nothing would qualify. The Board has approved Z-factor applications for electricity distributors under similar wording to what was used in Enbridge’s prior IR plan. The Board concludes that it is appropriate to have similar criteria across all regulated entities to facilitate consistent outcomes in specific applications. For that reason, the Board will not adopt Enbridge’s proposal to use “cause” as the reference. The Board will retain the reference to “event”. In reply, Enbridge submitted that if the Board does not adopt its proposal, then the approach proposed by Board staff is the most appropriate of the alternative positions. The Board will adopt Board’s staff’s proposed wording as it is sufficiently similar to the criteria for Union Gas and for electricity distributors and transmitters. The criteria will be as follows:

(i) Causation: The cost increase or decrease, or a significant portion of it, must be demonstrably linked to an unexpected, non-routine event.

(ii) Materiality: The cost at issue must be an increase or decrease from amounts included within the Allowed Revenue amounts upon which rates were derived. The cost increase or decrease must meet a materiality threshold, in that its effect on the gas utility’s revenue requirement in a fiscal year must be equal to or greater than $1.5 million.

(iii) Management Control: The cause of the cost increase or decrease must be: (a) not reasonably within the control of utility management; and (b) a cause that utility management could not reasonably control or prevent through the exercise of due diligence.

(iv) Prudence: The cost subject to an increase or decrease must have been prudently incurred.

With respect to the materiality threshold, intervenors argued that the threshold should be increased from $1.5 million to $4 million, which is comparable to that approved in the Union Gas Settlement Agreement. Parties argued that the companies are similar in terms of revenue requirement and risk and that Z-factor relief should only be granted in very exceptional circumstances. Staff noted that even the $4 million Z-factor threshold is well under 1% of Enbridge's annual revenue requirement. In reply, Enbridge objected to assigning any precedential value to provisions that were the subject of an overall negotiated package from another company. Enbridge argued that there has been no evidence in this case as to how the Union Gas Z-factor wording would apply to and impact Enbridge. Enbridge also noted that its proposed threshold is 50% higher than the maximum Z-factor threshold for electricity distributors including Toronto Hydro and Hydro One.

The Board has expressed reluctance to impose a negotiated model on to a different company. As with other provisions of the Union Gas Settlement, the Z-factor provision was the subject of an overall package and the Board agrees with Enbridge that it should not be considered to have precedential value for other distributors. The Board has articulated its policy on Z-factors for electricity distributors in the *Filing Requirements for Electricity Distribution Rate Applications* July 17, 2013. The policy sets a materiality threshold of $1 million for a distributor with a distribution revenue requirement of more than $200 million. To the extent that this provides a Board policy for a company this size and until the Board changes its policy on a principled basis, the Board finds no reason to change Enbridge's current threshold. The materiality threshold for Z-factor applications will remain at $1.5 million.

Energy Probe, with the support of SEC, proposed that Z-factor treatment should not be available when Enbridge has over-earned its allowed ROE. In Energy Probe's view, it would not be reasonable to expect ratepayers to pay for a Z-factor event at the same time the utility has over-earned due to other factors that could include bad forecasting on the part of the utility. For the same reasons the Board is not changing the threshold, it will not at this time prohibit Z-factor applications when there are over-earnings available to pay the additional cost. Intervenors will be free to advance those arguments in specific Z-factor applications.

Off-Ramp

An off-ramp serves as a trigger for the Board to review whether a company should remain on its IR plan. The off-ramp is set in order to trigger that review process if the company significantly over-earns or under-earns the allowed ROE. Enbridge proposed a symmetrical off-ramp, with the trigger being when weather normalized earnings are more than 300 basis points different from the ROE determined annually through the application of the Board's ROE Formula.

Board Findings

Energy Probe and CME questioned whether an off-ramp is required. However, the Board accepts Enbridge's proposal and agrees with CCC that in a five-year Custom IR plan an off-ramp is an important component. The Board will monitor Enbridge's results and carry out a review if Enbridge over-earns or under-earns more than 300 basis points. Parties agreed that the reference ROE should be the level of ROE which underpins rates. The Board agrees with this approach.

Energy Probe submitted that the off-ramp should only be applicable the second year that the utility under-earns more than 300 basis points. Enbridge responded that the off-ramp does not amount to an automatic termination of the Custom IR plan but rather an application to review the plan. Enbridge noted that parties such as Energy Probe would be free to argue that the company should live with the Custom IR plan for additional time. The off-ramp triggers further review but not necessarily a change in rates. The Board agrees with Enbridge that at the time of such a review, it will be open to the parties to argue what action, if any, should be taken.

Volumes and Revenues

Enbridge develops its budgets for capital expenditures and operating and maintenance expenditures based partially on its forecast of customer numbers and volumes. In addition, the Board determines how much the current rates will need to change by applying the current rates to the forecast of customers and volumes and calculating whether the resulting revenues are sufficient to recover the costs. Enbridge presented a forecast of customer additions and volumes. The company also proposed to update the volume forecast each year as part of the annual rate setting process.

The following table sets out Enbridge's forecast of total volumes.

Gas Volumes

	2013 Board Approved	2014	2015	2016	2017	2018
Total Gas Volume(10^6m^3)	11,504.4	11,156.0	11,249.5	11,348.4	11,348.4	11,348.4

Several aspects of the volume forecasts were disputed by the parties:

- The annual forecast update process
- The forecast of customer additions
- The forecast of average use by Rate 1 and Rate 6 customers
- The forecast for contract market customer volumes
- The change to the heating degree day forecast
- The forecast of other revenue

Each of these will be addressed in turn.

Annual Forecast Update Process

Enbridge developed its 2014 volume forecast using its proposed updated Heating Degree Day methodology and the existing methodologies for forecasting average use and large volume customer use. Although Enbridge also provided a forecast for 2015 to2018, the company proposed that the forecast be updated each year.

Enbridge proposed that in advance of each year (2015 to 2018) it would provide updated volume forecasts as part of its application. These updated forecasts would include an updated meter unlocks forecast, current economic data, and the application of the methodologies and processes for Heating Degree Days, average use, and large volume forecasts. The updated forecast would be used to derive final rates for each year from 2015 to 2018. Enbridge submitted that it would appropriately balance the risk between the company and ratepayers to update the volumetric projections annually to reflect actual data reflecting the current economic environment and the impact of the GTA Project.

Board Findings

The Board will accept the annual forecast update process proposed by Enbridge, but will make some modifications, which are detailed in the following sections. The Board's Custom IR framework did not contemplate annual updates, but the Board finds that such an approach is a reasonable approach for one of the first Custom IR plans. It is also the Board's expectation that this annual process need not be particularly contentious, and might well be appropriate for a settlement process.

Forecast of Customer Additions

The table below presents Enbridge’s gross customer additions forecast for 2014 and beyond.

Gross Customer Additions

	2013 Board Approved	2013	2014	2015	2016	2017	2018
Residential	36,025		34,188	35,931	37,030	**Not in evidence**	**Not in Evidence**
Commercial	2,544		2,455	2,555	2,612		
Industrial	10		4	3	3		
TOTAL	**38,579**	**36,644**	**36,647**	**38,489**	**39,645**		

Enbridge proposed that the customer additions forecast should be approved in this proceeding and should not be updated annually. In Enbridge's view, this would streamline the process and would be consistent with its cost forecasts, which are based in part on the customer additions forecasts.

Energy Probe submitted that the 2014 customer additions forecast for Rate 1 should be increased by 1,386 and Rate 6 should be increased to 1,500. Energy Probe argued that these increases are justified given the level of under-forecasting in 2013. Energy Probe further argued that the customer additions forecast should be part of the annual updating process.

Enbridge disagreed with the proposed adjustments. The company noted that it is using the same methodology which has been accepted either through settlement or decision in previous cases. Enbridge submitted that Energy Probe was referencing the average customer meters forecast, which is not comparable to the gross customer additions, and that actual customer additions were below the 2013 Board approved level. Enbridge also noted that there have been declines in housing starts since the original forecast and that current forecasts show worsening outlook for 2014. Enbridge concluded that there was no basis to change the methodology or increase the customer additions for Rate 1 and Rate 6.

Board Findings

The Board will not adjust the gross customer addition forecast for 2014. The Board finds that the forecast for 2014 is reasonable in light of the evidence regarding current economic indicators and Enbridge's reliance on a consistent methodology. However, the Board will require the customer addition forecast to be updated on an annual basis as part of the volume forecast update process. Enbridge resisted this approach due to concerns about complicating the process and creating a misalignment with cost forecasts which would not be updated. The Board finds that as part of the volume forecast update process, it is reasonable to examine the major components, including customer additions. The methodology for forecasting customer additions is well established so the Board does not expect that adding this component will unduly complicate the process. Enbridge has indicated that if the customer addition forecast changes, there would be implications for the capital expenditure forecast. However, the Board finds that Enbridge will be able to accommodate the expected modest level of variability in the associated capital costs without any adjustment.

Average Use Forecast for Rate 1 and Rate 6

The following factors influence average use for Rate 1 (residential) and Rate 6 (commercial and light industrial): new customers (both new construction and replacement customers); the timing of customer additions; rate migration; gas prices; economic conditions; and the company's Demand Side Management ("DSM") programs. Enbridge uses econometric models to forecast average use for Rates 1 and 6. Enbridge explained that the models have been subjected to many diagnostic tests which have demonstrated that the results are statistically valid.

Enbridge maintained that average use changes for Rate 1 are fairly reflective of regression model results because of the homogenous nature of customers within this class, but that modeled Rate 6 average uses may require adjustment to account for rate migration or specific changes in usage patterns for customers within this class. Approximately 2,000 contract market customers migrated to Rate 6 over the period 2006 through 2010, which resulted in increases in the average use per customer during that period. Enbridge observed that in the past few years migration has stabilized.

Energy Probe noted that the forecast decrease of 2.21% in 2014 for Rate 1 average use is higher than historical or forecast decreases. Energy Probe submitted that the average use forecast for Rate 1 should use a decrease of 1.3% instead. Energy Probe further argued that it was not reasonable to forecast a decline for Rate 6 of 2.81% because average use for this class has increased over the historical period and is forecast to be flat for 2015-2016. Energy Probe concluded the 2014 average use for Rate 6 in 2014 should be kept at the 2013 Board approved level of 29,204m^3. BOMA supported Energy Probe.

Enbridge responded that its econometric methodology has been used since 2001, and the forecasts have been accepted through settlement or Board decisions. Enbridge maintained that the decline in Rate 1 for 2014 is 1.8% compared to 2013 actual and is reasonable in light of expected gas prices and economic conditions. Enbridge argued that Energy Probe's proposals were without an evidentiary or methodological foundation.

Board Findings

The Board will not adjust the average use forecast for 2014. The Board finds that the forecast for 2014 is reasonable in light of current economic indicators and the consistent application of the long-standing methodology and reflects the impact due to Rate 6 migration. The Board will require the average use forecast to be updated on an annual basis as part of the volume forecast update process. As part of the volume forecast update process, it is reasonable to examine the major components, including average use.

Contract Market Volume Forecast

Enbridge generates the contract market volume budget using a “grass roots” approach. Volumes are forecast on an individual customer basis by Enbridge account executives in consultation with customers during the budget process. Current economic and industry conditions and degree days are also factored into the volume determination. Unless a customer has signed a contract, no volumes are included in the forecast. This forecast would be updated each year as part of the annual rate application.

APPrO argued that the contract customer additions were historically under-forecast and that therefore the 2014 contract customer additions forecast should be increased by 5%. Enbridge responded that APPrO appeared not to have accounted for the migration of customers between Rate 6 and the Large Volume classes in doing its analysis.

Energy Probe submitted that the 2014 forecast should be revised to include the two contract customers added since the forecast was made. Enbridge opposed this addition arguing that continual updating was “endless and time consuming” and could go in either direction.

Energy Probe also submitted that the forecast should be increased to include the potential for further contract customers using a probability-weighted approach. Energy Probe argued that not including any volume forecast for potential customers is a flaw and noted that a probability weighted approach would be consistent with Union Gas’ approach. Enbridge opposed this approach, stating:

> *Where the customer is known and there are arrangements for a new customer to come online, that customer’s volumes would be included in the forecast. However, it is not possible to incorporate incremental volumes mid-year arising from new customers that were not foreseen or expected to come online.*[7]

[7] Enbridge, Reply Argument, p. 101

Enbridge also argued that it would be inappropriate to include every possible customer given the uncertainty as to timing and volumes.

Board Findings

The Board finds that the contract customer volume forecast for 2014 should be adjusted to include the two customers who have been added. Enbridge is directed to adjust the volume forecast accordingly. This is a reasonable reflection of current circumstances and does not represent a complex adjustment.

Enbridge intends to update the contract market volume forecast on an annual basis as part of the volume forecast update process. The Board accepts this approach. The Board sees merit in a probability-weighted forecast approach proposed by Energy Probe. The Board finds that Enbridge's method of only including volumes for signed customers is unduly conservative. The Board concludes that the company can make an assessment of the probability of potential customers coming online for the forward year and use this to create a volume forecast which is reasonable. Enbridge will adopt this approach for purposes of the 2015 rate application and for the balance of the IR term.

Heating Degree Days Forecast

Enbridge proposed to change the method used to forecast heating degree days for its Central weather zone to a "50:50 Hybrid" method. The 50:50 Hybrid is the average of two existing models: the 10-year Moving Average model and the 20-year Trend Based model. Enbridge's evidence showed that the 50:50 Hybrid ranks first among its models in predictive accuracy using actual data for the Central weather region. Enbridge proposed no change to the methods used to forecast heating degree days for the Eastern weather zone, where the "deBever with Trend" method is used, and the Niagara weather zone, where the "10-year Moving Average" method is used.

Energy Probe supported the company's proposal, while SEC submitted that the heating degree day forecast should only change at rebasing. Enbridge responded that there was no reason to wait for until the next rebasing and noted that an updated approach was contemplated in 2013 settlement proposal.

Board Findings

The Board accepts the proposed change to the heating degree days forecast method for the Central weather zone. The Board does not agree with SEC that such a change should only be considered in a rebasing application. The evidence is clear that the change, which is an application of existing methods, results in a more reliable forecast.

Other Revenue

Enbridge earns "other" revenue from a variety of sources, including service charges, late payment penalties, open bill revenue and transactional services.[8] The following table shows actual and forecast Other Revenue.

Other Revenue
($ millions)

	2013 Board Approved	2013 Actual	2014	2015	2016	2017	2018
Other Revenue	45.0	42.8	40.6	41.0	41.3	41.3	41.3

Energy Probe argued that the 2014 Other Revenue forecast should be $42.8 million, which is the actual for 2013, because that level reflects the impact of reduced late payment penalty revenue and customer service rule changes. Enbridge responded that the 2013 actual level was lower than the 2013 Board approved due to the decline in late payment penalty revenue, new account and red lock charges.

Energy Probe submitted that the flat forecast for Other Revenue during 2015-2018 suggests an under-forecast. In Energy Probe's view, either the forecast should be updated annually like volume forecast or the Board should increase forecasts for 2015, 16, 17 and 18 by $2.2 million/year. Energy Probe maintained that updating the forecast would not add much complexity. Energy Probe noted that the 2013 actual was $2.2 million higher than forecast and used that as the basis for its proposed adjustment. BOMA supported Energy Probe.

[8] Transactional services revenue is addressed separately in the section on deferral and variance accounts.

Enbridge responded that if Other Revenue is to be updated annually, then bad debt expense should be updated as well. Enbridge also argued that this additional level of updating would reduce forecast risk on the company, which was already a criticism raised by some parties.

Board Findings

The Board finds that the forecast of Other Revenue for 2014 through 2018 is unduly conservative. The forecast is essentially flat, even though the company is forecasting customer and volume increases over the period, and the level for 2014 is below the 2013 actual. The Board acknowledges that reductions have taken place in late payment penalty revenue, however the 2013 actual incorporates that change. The Board concludes that it is reasonable to set the 2014 forecast at the 2013 actual level ($42.8 million). Having increased the 2014 level, the Board will use that level for the balance of the Custom IR term. The Board concludes that this represents a reasonable balance in forecast risk. The Board will not require the Other Revenue forecast to be updated on an annual basis.

Capital Expenditures

Enbridge's proposed capital program for 2014 to 2018 is a critical part of its application and is the primary reason, according to Enbridge, that it chose a Custom IR as opposed to the traditional IR structure.

The proposed capital program consists of a core capital component, the Work & Asset Management Solution (WAMS) project, as well as the GTA and Ottawa projects. The core capital is intended to meet customer growth, the operational and business needs of the company, and the integrity management programs that the company has been mandated to undertake. The amounts for each component are summarized in the following table.

Capital Expenditures
2012 – 2018
($ millions)

	2012 Actual	2013 Board Approved	2013 Actual	2014 Forecast	2015 Forecast	2016 Forecast	2017 Forecast	2018 Forecast
Core Capital	418.7	386.1	441.6	443.8	446.6	441.9	441.9	441.9
WAMS		0.5		36.3	25.7	8.1		
GTA / Ottawa	19.1	63.3	76.2	202.2	359.7			
TOTAL	**437.8**	**449.9**	**517.8**	**682.3**	**832.0**	**450.0**	**441.9**	**441.9**

Enbridge explained that the significant increase in the proposed total capital expenditures in 2014 and 2015 relative to other years is due to the GTA, Ottawa, and WAMS projects. If these projects are excluded, the forecast is basically flat and consistent with the 2012 and 2013 actual expenditures ($418.7 million and $441.6 million, respectively). Enbridge proposed to hold its core capital budget for 2017 and 2018 at the same level as 2016 even though its asset plan forecasts higher spending in those years.

Enbridge maintained that the 2013 Board-approved capital budget of $386.1 million (excluding WAMS, GTA and Ottawa projects) was not reflective of the company's capital spending requirements for the past couple of years, or the anticipated requirements during the Custom IR term.

In the following sections, the Board will address the four aspects of Enbridge's proposed capital expenditures plan:

- magnitude of the proposed capital budget,
- asset planning process,
- productivity, and
- proposed capital-related variance accounts.

Magnitude of the Proposed Capital Budget

As stated in the RRFE Report:

> *The Custom IR method will be most appropriate for distributors with significantly large multi-year or highly variable investment commitments that exceed historical levels.*[9]

In this case, and as stated earlier, the main reason for the significant increase in proposed capital expenditure in 2014 and 2015 relative to other years is the inclusion of the GTA, Ottawa and WAMS projects. If these projects are excluded, the proposed capital budgets for the plan duration are fairly consistent with historical levels.

The Ottawa project has been completed and is in-service. The GTA project received leave to construct approval from the Board in a separate proceeding (EB-2012-0451), with construction starting in 2014 and a forecast in-service date of October 2015.

The evidence is that the WAMS project is going through a public tendering process; the first stage is completed (software vendor selected) and the second stage (system integrator selection) is expected by mid-year. WAMS is expected to go live at the end of 2015. Enbridge retained Sync Energy to undertake an independent third-party review of the WAMS budget and the direction that Enbridge proposed to take. Sync Energy's report concludes that the budget developed by Enbridge is in the expected range, and the approach being proposed by the company is appropriate.

[9] RRFE Report, p. 19.

The main concerns raised about Enbridge's capital forecasts are:

- Lack of independent support for the cost forecasts, including the proposed significant increase in the integrity management spending within the core capital program.
- Lack of rationale for using the Custom IR approach given that the core capital expenditures are forecast to remain at the 2012 and 2013 levels throughout the IR period.

Enbridge submitted that it has developed capital budgets which it believes represent the reasonable minimum cost to continue to operate its system safely, reliably and in compliance with all applicable regulatory requirements. According to Enbridge, its budgets are intended to provide the Board and ratepayers with confidence that there has been no over-forecasting and that it will be the company that will be at risk if there is over-spending.

Board Findings

Earlier in this decision, the Board determined that Enbridge's capital requirements are sufficient to support the request for a Custom IR if adequately supported. Although a traditional IR approach could have been used, the Board acknowledges that it is open to a utility to request a Custom IR if the expenditures are significant and if the application is adequately supported. Although the Board is prepared to accept a Custom IR approach, the Board agrees with the various parties that the magnitude of the core capital budget is not sufficiently supported either by an independent third-party review, benchmarking or by a strong direct linkage to Enbridge's asset management plan. These aspects have been addressed earlier in this decision (in the Rate Mechanism section) and are addressed further below.

The Board also emphasizes the expectation that, under a Custom IR plan, the company is expected to bear a greater proportion of the forecast risk in exchange for the advance approval of higher capital expenditures for inclusion in rates.

More specifically for the large components of the capital program, the Board findings are summarized below:

- GTA project: Given the advanced status of the project, the Board finds that Enbridge should bear the risk of cost and schedule variances until rebasing (see variance account section). The Board will require Enbridge to report on cost and schedule status of this project as part of the annual reporting process.

- WAMS project: Given the independent third-party review of Enbridge's approach and budget for this project, as well as Enbridge's use of a competitive public tendering process for vendor selection, the Board is satisfied with the approach taken and will require Enbridge to report on the project's progress as part of the annual reporting process.
- System Integrity Program: The Board shares SEC's and the Industrial Gas Users Association's ("IGUA") concerns about the uncertainty and lack of external evidence regarding the program drivers and cost estimates. The Board expects these concerns to be addressed through future refinements in Enbridge's asset planning and benchmarking processes, including risk assessment, prioritization, and examination of industry trends (see corresponding sections below). The Board will require Enbridge to report on the progress of this program as part of its annual reporting process.

The Board will, therefore, accept the proposed capital expenditure plan as submitted subject to the conditions outlined in the variance accounts and reporting sections of this decision.

The Board notes Enbridge's acknowledgement and understanding of the RRFE Report's approach to annual reporting of capital spending versus plan under the Custom IR method. The RRFE Report states that if actual spending is significantly different from plan, the Board will investigate and may, if necessary, terminate the distributor's rate setting method.

Asset Planning Process

Several parties argued that Enbridge's Custom IR plan lacks a robust asset management plan which includes all its assets and is directly linked to its capital budget.

In response, Enbridge described the rigour which the company exercised in the development of its capital budgets and objected to the assertion that its asset plan is not clearly linked to the filed capital budgets. Enbridge explained that the final capital budgets differ from the asset plan due to the fact that after having considered the relevant inputs from the asset plan, Enbridge went through further prioritization and rationalization exercises to finalize the capital spending requirements set out in the evidence.

Enbridge acknowledged that its asset plan does not include its non-distribution assets (storage, facilities, fleet, IT), but suggested that this does not mean that there is no long-term planning or good asset management for these items. Enbridge also acknowledged that its asset management practices will continue to evolve.

Enbridge concluded that it has demonstrated the fundamental principles of good asset management and coordinated longer term optimized planning as expected by the Board. Enbridge submitted that its asset plan was a fundamental input into its capital budget process, and was a key determinant of the capital spending forecasts.

Board Findings

The Board acknowledges the work done by Enbridge to develop its asset management plan, but finds that there are some shortcomings. The Board believes that a robust asset management plan should include all the company's assets and be based on a comprehensive process of condition assessment, risk evaluation, and prioritization. A comprehensive asset management plan is a critical part of a Custom IR application. The evidence is clear that Enbridge's asset management plan does not include all of the company's assets. An asset management plan should also be directly linked to the proposed budget, in order to provide the Board with robust evidence that the proposed capital expenditures have been through the necessary optimization and prioritization process. One of the stated objectives of Enbridge's asset plan is to:

> *Serve as a mechanism to communicate EGD's asset management priorities and planned investments with internal and external parties including EGD's regulators.*[10]

This implies that the "planned investments" contained in the asset plan should be consistent with those communicated through the proposed capital budget. However, the evidence does not describe the linkage between the estimated capital costs included in the asset plan and those proposed in the Custom IR plan. The explanation provided by Enbridge is that it did consider the inputs from the asset plan, and then went through separate prioritization and rationalization exercises to finalize the capital spending requirements. The Board would have expected that the asset plan would actually be the vehicle that Enbridge would use to perform the necessary prioritization and rationalization such that the outcome would be one final capital spending plan. With such a strong and direct linkage, the Board would be provided with a basis to judge the rigour with which the resulting capital investment plan has been optimized and rationalized.

[10] Asset Plan (Ex B2, Tab 10, Sch 1, p 13).

The Board finds that Enbridge should continue to work on advancing its asset management plan, specifically in the following two areas:

- Inclusion of all the company's assets; and
- Direct linkage to the budget

Given the significance of the asset management planning process in the context of the Custom IR plan, the Board will require Enbridge to report on these efforts on an annual basis, including some form of an independent third-party assessment of the asset management planning process and resulting plan. The Board concludes that this approach will mitigate the shortcomings and will be the most effective means to ensure that Enbridge develops the necessary asset management plan going forward.

Productivity

Enbridge explained that its capital spending requirements for 2014 to 2018 were identified through a lengthy, rigorous process including several iterations to identify the lowest possible prudent capital budget. Enbridge submitted that its proposed capital budgets are substantially lower than the costs that it actually expects to face and that it will have to find ways to accommodate its actual costs through productivity improvements and initiatives.

Enbridge identified two approaches to productivity with the budgets:

1. "Embedded productivity savings" where the forecast costs are lower than what Enbridge believes will be the actual costs. The gap will be addressed through productivity savings. These "embedded productivity savings" are estimated at $162 million within the 2014 to 2018 capital budget ($127 million related to Enbridge's decision to limit the budgeted cost of customer additions, $16 million challenge associated with maintaining a flat labour cost, and $19 million of inflation-related challenge for 2017 and 2018).

2. In addition to the estimated $162 million of "embedded productivity savings", Enbridge excluded $264 million of "variable costs" from its 2014 to 2018 budget. These "variable costs" are defined as costs that are dependent on outcomes from planned studies and other future activities, where the amount of such costs cannot be forecast with certainty. Enbridge provided a list of identified "variable cost" items for 2014 to 2016 totalling $164 million and then assumed additional uncertainties for each of 2017 and 2018 of $50 million per year, roughly the average of 2014 to 2016, bringing the total to $264 million.

The main issues that the various parties had with Enbridge's approach to productivity improvement were the lack of specific initiatives that the company will employ to achieve the stated budget challenges, the lack of assurance that the initial capital budget was not overstated, and the lack of objective third-party verification of the reasonableness of the proposed capital expenditures.

Enbridge submitted that seeking approval of capital budgets based upon forecasts which have removed significant "variable cost" components and which do not include the costs of expected capital requirements acts as an incentive to generate efficiencies, failing which the company will find itself in a situation of over-spending which will not be addressed until the next rebasing.

Board Findings

The Board finds that, while Enbridge quantified the levels of "embedded productivity savings" included in its budget ($162 million) as well as the "variable costs" excluded from the budget ($264 million), it did not specifically identify the initiatives and programs that it intends to employ in order to achieve these productivity savings. For context purposes, the total of the identified "embedded productivity savings" and "variable costs" ($162 million plus $264 million) represent approximately 9% of the total submitted capital budget for 2014 to 2018.

On the one extreme, these productivity savings can be achieved by completing the proposed program at a lower cost through more efficient execution. On the other extreme, they can be achieved by cutting other work components from the program. Without a clearer identification of productivity initiatives upfront, it is difficult to make a determination as to where the final results fall between these extremes. Obviously, the third possibility is that the work program is completed at a lower cost because the initial estimates were inflated.

Given this lack of clarity, the Board will require Enbridge to report on the status of the work items making up the $162 million embedded productivity savings [11] as well as those items making up the $164 million variable costs for 2014-2016[12] as part of its annual reporting process. The reporting will identify whether and how these work items were accommodated within the approved capital envelope. This approach and the associated level of transparency will assist the Board in monitoring the operation of Enbridge's

[11] Exhibit J1.6 page 3.
[12] Exhibit J1.6 page 6.

Custom IR and will provide Enbridge with an incentive to meet its budgets through productivity improvements.

Proposed Capital-Related Variance Accounts

As indicated earlier, one of the main components of the Custom IR is the demonstration that the applicant is willing and able to assume the considerable risk associated with five-year capital forecasts. Enbridge proposed three variance accounts to track variances between actual and forecast spending:

- The GTA Project Variance Account
- Relocation Mains Variance Account
- Replacement Mains Variance Account

Many parties submitted that these accounts resulted in inappropriate shift in risk from shareholders to ratepayers. Each proposed account is discussed below.

Greater Toronto Area Project Variance Account ("GTAPVA")

The Board has already approved leave to construct the GTA project (EB-2012-0451). Construction is expected to begin in 2014 and the in-service date is forecast for October 2015. Enbridge proposed that an account be created to record any variance between the forecast Allowed Revenue and the eventual actual Allowed Revenue which will be known upon completion of the project. Enbridge maintained that the account was justified given the scale of the project, which is the largest in the company's history with a forecast capital cost of $686.5 million.

Enbridge proposed that the variance for the years 2015 through 2018 be recorded in the account with an offsetting annual entry through revenue, with the cumulative impact at the end of each of 2015 to 2018 to be cleared through a rate rider with other deferral or variance accounts for the subject year.

Some parties supported the account, or a similar mechanism, while others opposed it.

CCC supported the account, but pointed out that if the Union Gas IRM model is used, the account could be more generic. Both BOMA and Energy Probe supported the account, or Y-factor treatment, but under traditional IR plan. Board staff did not oppose the account, but submitted that there should be a cap in order to create a cost control incentive.

Enbridge responded that the account should not be capped and noted that any cost over-runs would still be subject to a prudence review.

BOMA submitted that if a Custom IR is set, then the account should be asymmetric, functioning only to return under-spend to ratepayers. Energy Probe opposed the account, arguing that Enbridge should be prepared to take on forecast risk under a Custom IR. Energy Probe noted that the project is at an advanced stage and concluded that the project did not present a greater risk. Enbridge responded that the GTA project is the most costly single project in the company's history and therefore the risks are greater.

Board Findings

Enbridge notes that Union Gas has a similar account for its major expansion projects. However, Union Gas is under a different rate framework. The Board's expectation under Custom IR is that the company will be prepared and able to bear the risks associated with its capital expenditure forecasts. The risk in this instance is the variance in revenue requirement (due to cost variances or timing differences) between the forecast in-service date and the next rebasing proceeding (expected to be 2019).

The Board finds that Enbridge should bear the risk of cost variances and timing differences until rebasing, and therefore the account will not be established.

The ability to manage risk is an important component of the Custom IR. Enbridge notes that this is the largest single project in the company's history. However, the project has already received leave to construct approval and the in-service date is October 2015; so the project is fairly far advanced. If any cost overrun is found to be prudent at rebasing, the revenue requirement may be adjusted going forward.

Enbridge indicated that the account is also needed to address timing differences. However, the company's testimony in the leave to construct hearing was that the project would proceed because of distribution requirements, whether or not Union Gas and TCPL's related projects proceed. This evidence leads to the conclusion that a delay is unlikely. If the project is delayed, the Board can monitor the situation through the capital reporting, and take action if appropriate.

Relocation Mains Variance Account ("RLMVA") and Replacement Mains Variance Account ("RPMVA")

Enbridge proposed to fix its core capital budget for 2017 and 2018 at the 2016 forecast level. However, Enbridge maintained that the capital costs for relocation mains and replacement mains are unpredictable beyond 2016 and proposed that a variance account be established for each activity.

Board staff opposed these two accounts on the basis that they remove too much risk from the company. Staff quoted from Dr. Kaufmann:

> *So just to step back a second, we know that incentive regulation is supposed to be a substitute for cost of service regulation, and all of these variance accounts are very much focussed on cost recovery. Each one is kind of a miniature cost of service review or plan in itself.*
>
> *When you layer in more and more of these things [variance accounts] on top of an incentive plan, it tends to – at some point, the plan becomes something other than an incentive regulation plan. And I haven't really made an issue of this before, you know, before this point, but I have become aware of that I think that is a problem.*
>
> *So I don't know if that necessarily answers your question about something they can do to protect against the forecast issue per se. But one thing they could do to make this plan more of a – to move it in the direction of an incentive plan is to scale back on some to the Y factoring in variance accounts, particularly for replacement.*[13]

CCC also opposed the accounts, arguing that mains relocations and replacements are normal distribution activities which should be managed within the capital envelope. CCC concluded that the shifting of risk to ratepayers was not justified. Energy Probe also opposed the accounts, arguing that these accounts are like an Incremental Capital Module, which is not permissible under Custom IR. Energy Probe also noted that the accounts are asymmetrical because no under-spend would be returned to customers.

[13] Tr. 3, pp. 143-144.

Board Findings

Enbridge originally proposed to delay fixing the capital budget for the final two years of the Custom IR plan. This was broadly opposed by the parties. Enbridge subsequently modified its proposal to hold the budget flat for the final two years and establish variance accounts for two specific activities. The Board sees this as an improvement in the proposal; one which brings the overall plan closer to the expectations under Custom IR.

The Board agrees with Enbridge that holding capital expenditures flat in 2017 and 2018 will be challenging. However, the Board agrees with parties which have expressed concern about an inappropriate allocation of risk to ratepayers arising from the RLMVA and RPMVA variance account proposal. Enbridge notes that Dr. Kaufmann agrees that the concern about an inappropriate allocation of risk to ratepayers arising from relocation and replacement mains expenditures could qualify as Y-factors under a traditional IR plan. However, as discussed above, one of the key differences between traditional IR plan and a Custom IR plan is the expectation that the company will bear a greater proportion of the forecast risk under the Custom IR plan in exchange for the advance approval of higher capital expenditures for inclusion in rates. The RRFE Report contemplates a robust five-year capital plan along with a demonstration that the distributor is able to manage the forecast risk over the plan term.

Enbridge has further modified its proposal to address the concern that the proposed accounts unduly mitigate the company's risk. In its reply argument, Enbridge proposed that the threshold revenue requirement for the accounts be raised from $1.5 million to $5 million. Enbridge explained that its spending on mains relocations or main replacement would need to be $50 million higher than budgeted to qualify for inclusion in the accounts and any disposition would also be subject to a prudence review. The Board finds that this is a further improvement in allocating capital expenditure risk between the company and ratepayers.

The Board finds that the accounts, as modified through Enbridge's reply argument, are reasonable because the forecast remains flat in total for the final three years of the plan and the risk to be borne by the company remains significant given the limitation of the accounts to two activities and the threshold revenue requirement of $5 million.

Operating and Maintenance Costs

Operating and Maintenance (O&M) costs are the day-to-day costs of running the business. Like capital expenditures, Enbridge's Custom IR plan is built on a 5-year forecast of O&M expenditures. The following table provides the 2013 Board approved and actual, and 2014 to2018 forecast for the main O&M cost categories.

Operating & Maintenance Costs by Category
($ millions)

	2013 Board Approved	2013 Actual	2014	2015	2016	2017	2018
Customer Care/CIS	89.4	83.1	92.6	96.5	100.4	104.4	108.5
DSM	31.6	31.6	32.2	32.8	33.5	34.2	34.9
Pension & OPEB	42.8	44.0	37.2	33.8	30.9	28.5	26.2
RCAM	32.1	32.1	35.3	34.0	33.8	34.8	35.9
Sub-total	**195.9**	**190.8**	**197.3**	**197.1**	**198.6**	**201.9**	**205.5**
Other O&M	**219.2**	**224.7**	**228.0**	**231.5**	**241.0**	**248.5**	**256.3**
TOTAL	**415.1**	**415.5**	**425.3**	**428.5**	**439.5**	**450.5**	**461.8**

The first three rows of the table relate to expenses for Customer Care and Customer Information System (CIS) service charges, Demand Side Management (DSM) expenses and Pension and Other Post-Employment Benefits ("OPEB") expenses. Each of these have been, or will be, set outside of the current case:

- Customer Care/CIS service charges are subject to an approved settlement agreement (EB-2011-0226) which provides a mechanism to determine the costs for each year 2013 to 2018.

- DSM costs are subject to a separate regulatory process. The 2014 DSM budget included in this proceeding was recently approved by the Board in EB-2012-0394. The Board has recently launched a policy consultation related to future DSM expenditures (EB-2014-0134).

- The amounts for Pension and OPEB costs are subject to an agreement stemming from Enbridge's 2013 rate case (EB-2011-0354). Enbridge and the parties to the proceeding agreed that the company should recover only its actual Pension and OPEB costs over the coming IR term. The approved settlement agreement in that proceeding included the creation of a new variance account, the Post-Retirement True-up Variance Account (PTUVA).

Enbridge proposed that as part of the annual rate adjustment process for 2015 to 2018, it would update the values related to each of these areas. No party disputed that these items are beyond the scope of the current proceeding. Together, these expenditures (including Regulatory Cost Allocation Methodology, which is discussed below) represent about 44% of the annual total O&M expenditures.

In the current proceeding, attention focussed on "Other O&M" costs, and to a lesser extent, the Regulatory Cost Allocation Methodology costs and municipal taxes.[14] The Board will address Regulatory Cost Allocation Methodology and municipal taxes first, then Other O&M.

Regulatory Cost Allocation Methodology ("RCAM")

The Regulatory Cost Allocation Methodology ("RCAM") is the corporate cost allocation method used to determine Enbridge's share of corporate costs from Enbridge Inc. The purpose of RCAM is to ensure compliance with the Board's Affiliate Relationships Code and to ensure that the established test to determine appropriate corporation cost allocations is being satisfied. The development of the RCAM has been the subject of review and analysis by several experts and consideration by the Board in the past. The RCAM was in place during the previous IR plan (2008 to 2012) and was most recently addressed in the 2013 rates case (EB-2011-0354). In that proceeding, parties agreed to an amount of $32.1 million as part of the settlement agreement. The overall RCAM methodology involves stakeholder consultations.

[14] RCAM is a separate line item, but municipal tax is a specific component of Other O&M.

Enbridge used the RCAM methodology to forecast a trend for RCAM amounts for the 2014 to 2016 period and that trend indicates a decline due to Enbridge being a decreasing share of Enbridge Inc. The company proposed that the forecast for 2017 and 2018 be set using the same adjustment formula proposed for Other O&M.

Energy Probe submitted that the RCAM costs should be included in setting O&M for the Custom IR plan, with no variance account or true up. Board staff noted that the consultative has not met since 2012 and that the preliminary forecast amounts have increased since the last settlement agreement in EB-2011-0354. Board staff submitted that the 2013 amount should not be seen as being explicitly Board approved because it was part of a larger settlement agreement. Board staff proposed three options for the Board to consider:

- the costs should be subject to consultative review before being embedded in the IR plan;
- the costs should be frozen at the 2013 level ($32.1 million); or
- the costs should be set at the 2008-2012 average ($24.6 million).

Enbridge responded that it intends to reconvene the consultative in late 2014 or early 2015, and at that time the company will share the 2013 and 2014 data. The company noted that the declining forecast for 2014-2016 reflects that Enbridge is a smaller part of Enbridge Inc., while the levels for 2017 and 2018 have been set using the same rate of increase applied to Other O&M, adjusted by other RCAM-specific factors. Enbridge submitted that there is no evidence to suggest that the methodology should be changed, and also noted that any difference between forecast and actual will be captured in the ESM process.

Board Findings

The Board will accept Enbridge’s proposal, including the company’s commitment to reconvene the consultative in 2014 or 2015 to review the 2013 and 2014 data. The Board finds that this adequately addresses Board staff’s concern. Energy Probe argued that RCAM should be considered together with Other O&M. The Board does not agree. RCAM was developed separately and has its own distinct approach. The Board is content to allow the issue to be managed as Enbridge proposes – through the consultative and the ESM process.

Municipal Taxes

Energy Probe argued that the municipal tax forecast for 2017 and 2018 is too high. In Energy Probe's view, there is no evidence to support accelerated growth in this item and proposed that the increase should be limited to 4.8%. This would result in reductions of $200,000 and $400,000 in 2017 and 2018, respectively. Enbridge responded that the increase for 2017 and 2018 was similar to the prior years and included impacts due to the integrity program. Enbridge maintained that tax rate increases are likely to be higher than inflation and noted that net plant is also increasing.

Board Findings

The Board will not adopt Energy Probe's proposal for a specific reduction to municipal taxes. The Board finds that Enbridge's explanation for the municipal tax forecast is reasonable.

Other O&M

Other O&M represents about 55% of the total O&M budget for the 2014 to 2018 period. Enbridge explained that it set the budget using a bottom-up approach to understand the business needs and a top-down approach to embed productivity. The bottom-up approach was a grass roots budget process which was influenced by the expectations of greater needs in areas such as integrity inspections and repair and replacement. From the top-down perspective, a number of constraints were placed on the budget, including holding Full Time Equivalents ("FTEs") constant over the IR period, and limiting the annual total increase to 2.24% (with some exceptions). The 2.24% was based on Concentric's analysis of two external measures of inflation: GDP-IPI-FDD for material and Ontario average hourly wages. To this "target" rate of increase, a number of what Enbridge described as "extraordinary items" were added:

- 2014: $3.3 million added for the full-year effect of hires in 2013, higher hearing costs and higher interest on security deposits.
- 2015: a reduction for lower hearing costs
- 2016: 2.1% increase plus $4.1 million for WAMS
- 2017 and 2018: increase at the average rate of increase for 2014-2016

Enbridge identified three main cost pressures:

- integrity management expenditures;
- customer growth, which is about 1.7% to 1.8% per year; and
- salary and benefits which will likely rise at 3% and 6.1% annually, respectively.

Enbridge submitted that "the totality of the evidence supports the conclusion that the company will be hard pressed to operate within the budgets as requested"[15] and that it will be required to generate additional productivity over the Custom IR term. The company identified a number of specific productivity measures, including the use of GPS and improvements in locates. The company has also budgeted holding FTEs flat, holding bad debt flat, and absorbing other upward cost pressures between $24 million and $43 million per year. Enbridge estimated that its budget for Other O&M includes a total cost savings of $172.4 million over the Custom IR term.

The parties were critical of the O&M forecast, arguing that it was unrealistic, did not contain specific productivity improvements, did not show sufficient efficiency improvements, and was not substantiated by external analysis or rigorous benchmarking.

Board Findings

The Board will make an adjustment to the 5-year Other O&M budget so that it recognizes inflation, incremental cost pressures, and customer growth, but also an adequate level of productivity improvement. This adjustment is necessary to incent Enbridge to greater efficiency and to protect the interests of ratepayers over the term of the Custom IR plan.

Three main issues arose in the submissions from parties:

- The overall approach to budgeting
- Whether sufficient productivity improvements were included in the forecasts
- How the forecast should be adjusted

Overall Approach to Budgeting

SEC argued that the forecasts are not realistic because the company's evidence excludes known costs and known savings. SEC pointed to the known higher costs for items such as outside contractors, bad debt, and benefits and salary increases and the expected cost

[15] Enbridge, Argument in Chief, p. 44.

savings related to, for example, switching from Envision to WAMS, and the rollout of GPS. SEC submitted that the approach is flawed because these factors are not directly reflected in the forecasts. SEC submitted that Enbridge had developed
a hybrid of a 3-year forecast and two years using a formula, which in SEC's view was an indirect and inappropriate approach to traditional IR plan.

The Board does not agree with this overall criticism. A bottom up approach with known or expected specific costs, combined with a top down approach which applies specific cost constraints, can be an appropriate way to develop a reasonable forecast. This is discussed further below. The Board also considers it reasonable to include productivity expectations even if specific programs are not fully identified. This is also discussed further below.

Board staff submitted that Other O&M may include over-forecasting given the inherent incentive in the building blocks approach and that this could be addressed through staff's stretch factor proposal. Board staff submitted that there was no way to verify whether a lower achievable budget could have been presented. CCC submitted that there was no external analysis as to whether the expenditures are reasonable.

The Board agrees that there is an inherent incentive to over-forecast when setting rates for multiple years. The Board's RRFE report contemplates that an applicant will provide independent expert analysis to support its forecasts and/or provide robust benchmarking evidence as to the level of efficiency of the applicant. Enbridge has provided no external analysis of its O&M budgets, and the benchmarking analysis has significant limitations. The Board has taken this into account in its adjustments.

Productivity

Earlier in this decision, the Board has found that the benchmarking evidence does not support a conclusion that Enbridge is particularly efficient. Without this external analysis, the Board must rely on the internal analysis of the budget and the company's own plans for productivity improvements.

A number of parties criticized Enbridge for not identifying specific productivity improvement programs. Board staff argued that there are no specific productivity programs associated with the embedded savings of $172.5 million, and therefore these cost savings may not be sustainable and may not be productivity improvements. In staff's view, the Board should be looking for something more tangible than a “baked in” amount. Board staff also noted that the savings are not large in percentage terms compared to total revenue requirement. CCC, BOMA and SEC also argued that productivity improvements had not been identified sufficiently. Enbridge responded that productivity improvements have been embedded in the forecast and are the difference between the forecast and the expected actuals. Enbridge also pointed to evidence regarding a number of specific productivity programs, including GPS and locates.

The objective is for Enbridge to develop a forecast which is reasonable and defensible. The Board finds that it can be an appropriate approach to develop a forecast which includes self-imposed cost reduction assumptions as a means of ensuring productivity improvements, even if those productivity improvements cannot be precisely identified. The Board would expect a combination of planned programs and unplanned targets given the duration of the Custom IR plan. However, it would also be necessary to ensure that the budget constraints are sufficient to drive an appropriate level of efficiency and that the result is genuine productivity improvements and not merely short-term cost cutting.

One of the specific measures which Enbridge incorporated into its budgets was the requirement that the FTE level be held flat over the IR term. Enbridge maintained that its use of flat FTEs represents “an embedding of productivity” and a stretch factor. However, APPrO argued that holding FTEs flat does not imply the level of productivity which Enbridge is asserting because FTEs increased by about 15% between 2011 (2,070 actual) to 2013 board approved (2,388). The increase between 2011 and the 2014 budget (2,377) was slightly below 15%. APPrO also argued that the vacancy rate would provide flexibility as to the actual level of FTEs and that therefore the budget should be reduced to remove the costs associated with the vacancy rate. Enbridge responded that the 2013 rates include a credit for a 2.5% vacancy rate, and that this credit continues through the forecast period because it is in the base.

The Board agrees that holding FTEs flat is a form of cost containment; however, the Board finds that it is not as significant a constraint as Enbridge claims. First, the increase in FTEs between 2011 and 2014 is close to 15%, which is a significant level of increase over a short period. Second, the rates include a credit equivalent to a 2.5% vacancy rate, but the evidence is that the actual vacancy rate is running at 5%, thereby affording Enbridge with additional flexibility.

Productivity was also analyzed in the context of O&M cost per customer measures. Enbridge noted that total utility O&M per customer is declining in 2016 constant dollars and flat in nominal dollars, and that it is lower than Concentric derived from its approach to a traditional IR plan. The Vulnerable Energy Consumers Coalition ("VECC") argued that the declining cost per customer does not demonstrate efficiency because it is almost exclusively due to customer growth and monopoly economics. The increases in cost per customer for 2014-2018 are lower than in 2013, but in SEC's view that is because of the significant increases in 2012 and 2013.

The Board finds that the cost per customer data is not strong evidence of productivity improvement. The evidence is clear that Enbridge is growing and as a result the Board would expect to see the cost per customer show a declining trend as a result of scale economies. Enbridge witnesses testified that there are limits to scale economies and pointed to customer care as an area that would not decline on a per customer basis as customers are added. However, the customer care costs are subject to a separate budget setting mechanism.

The Board concludes that while Enbridge's approach is reasonable, the evidence is not sufficient to reach a conclusion that an appropriate level of productivity has been incorporated into the forecast. A number of parties made specific recommendations as to how the Other O&M forecast should be adjusted to incorporate a sufficient level of productivity. These are discussed in the next section.

Adjustments to the Forecast

Board staff proposed that a productivity factor be imposed on Enbridge in the form of a reduction to the total revenue requirement of $20 million per year. Staff pointed to a number of factors in support of its proposal:

- the recent levels of over-earning
- statements in the Strategic Plan
- the "stretch objective" included in Enbridge's memo to its Board of Directors regarding this application.

This productivity factor, totalling $100 million over the five years, would be a direct consumer benefit. Staff also submitted there should be a further stretch factor beginning in 2015, modelled on the approach for electricity distributors, which would amount to about $6.3 million to $7.8 million per year (or about $28.6 million over the IR term).

APPrO submitted that Other O&M should be adjusted for ongoing vacancies.

Energy Probe submitted that a number of adjustments should be made to the combined Other O&M and RCAM budget:

1. At a minimum, the Board should apply the Enbridge inflator of 2.24% to 2013 Board approved levels to set O&M for 2014 and, therefore, the base for subsequent years. This would result in a $35.8 million reduction over the IR term.
2. The Board should replace the escalation factor of 2.22% for 2015 with the Board determined inflation level of 1.7%. This change would increase the total O&M reduction described in #1 to $42.6 million.
3. The Board should reduce the subsequent years' inflation to 2%, which in Energy Probe's view is reasonable in light of 2008-2013 trend and most forecasts. This change would further increase the total reduction to $49.1 million.

CME argued that rates should be set using a traditional IR approach and that inflation should be set using GDP-IPI at 1.7% and that a combined productivity and stretch factor should be 60% of inflation, as it is for Union Gas.

Enbridge opposed the proposed reductions and argued that with the exception of the impact of WAMS, the increase in Other O&M is less than a combination of inflation (about 2%) and customer growth (about 1.7-1.8%). Enbridge noted that WAMS causes an incremental $4.1 million increase beginning in 2016, but over time replaces the costs of Envision. Enbridge also noted that its budgeting was done before the 2013 actuals were known. Enbridge argued that the Board should use 2013 actuals, which were higher than the level in the 2013 settlement agreement, as the starting point for any analysis as this is "the only and best evidence of the actual costs to undertake the operations".[16]

The Board finds that Other O&M should be set on the basis of yearly increases of 1% beginning with the 2014 proposal level. Some parties argued that the 2014 level should be reduced, but the Board will not do so. The 2014 level is 3.9% higher than the 2013 approved level, and 1.5% higher than the 2013 actual. The Board finds that this level of increase is reasonable in light of the cost pressures facing the company. More

[16] Enbridge, Argument in Chief, p. 46.

importantly, the Board concludes that accepting the 2014 level as proposed, combined with robust expectations for productivity improvements over the term of the IR plan represents an appropriate balance between the company and ratepayers.

The Board understands that there will be incremental expenses over the period related to WAMS and the integrity management program. However, over any given period there will be incremental cost pressures. It is the Board's expectation that the company will manage all expenditures and prioritize its work accordingly.

Proposed increases in Other O&M greater than inflation might be reasonable if there was robust benchmarking analysis to demonstrate that the company had achieved a significant level of efficiency and if there was external expert analysis of the budgets themselves. Neither was provided in this case. Enbridge has incorporated productivity into the budget in the form of constraints imposed and implied savings included. However, the Board finds that the level is not sufficient in light of the various concerns with the overall analysis identified above.

Enbridge implies that any increase which is less than inflation plus customer growth demonstrates efficiency and productivity improvements. Unless there is evidence that Enbridge has reached a point at which it cannot achieve any further economies of scale, the Board would expect that a period of customer growth would provide many opportunities for further productivity improvements.

In setting the Other O&M, the Board finds that it is appropriate to recognize the impacts of forecast inflation, incremental cost pressures from WAMS and integrity programs, the impact of embedded and incremental productivity improvements, Enbridge's history of earning in excess of its allowed ROE, and the company's communication to its Board of Directors that it expects to earn above the allowed return. Based on current and forecast inflation, the program costs included in the evidence, the rate of customer growth and expectations for productivity improvements, the Board concludes that Other O&M should be kept to a level which increases at 1% per year, beginning with the 2014 budget. This will result in a cumulative reduction of about $42.3 million, primarily coming in the later years of the plan. The Board notes that this category of O&M represents only about 55% of total O&M and that the remaining expenditures are subject to other adjustment mechanisms which have been agreed amongst the parties or set by the Board in other proceedings.

Other O&M Costs
Proposed and Approved
($ millions)

	2014	2015	2016	2017	2018
Other O&M Proposed	228.0	231.5	241.0	248.5	256.3
Other O&M Approved 1%	228.0	230.3	232.6	234.9	237.3

Cost of Capital

Enbridge proposed to maintain its current capital structure at 64% debt and 36% equity throughout the plan and presented a forecast of the cost of capital for each year of the Custom IR term and included it as a cost within the Allowed Revenues. The company cited the *Report of the Board on the Cost of Capital for Ontario's Regulated Utilities* (EB-2009-0084 "Cost of Capital Report") to argue that from a ratemaking perspective, the cost of capital is a cost to the utility just like operating and maintenance expense or capital spending.

For the cost of debt, the company provided a forecast of debt issuances for 2014 through 2018, including forecast cost rates and debt issuance costs. The mix of long term debt, short term debt, and preferred shares varies by a small amount each year because of the pacing of capital spending and cash flow requirements. For return on equity, Enbridge used interest rate projections from June 2013 to forecast the return on equity for the next five years, as follows:

Return on Equity
2013 Board approved and 2014-2018 Forecast

Year	2013 (approved)	2014	2105	2016	2017	2018
Return on Equity	8.93%	9.27%	9.72%	10.12%	10.17%	10.27%

The estimated revenue requirement increase associated with the return on equity forecast increase, over the Custom IR plan term, is $130 million. However, Enbridge forecast that its cost of debt will decline by $51 million over the Custom IR term, which has an offsetting impact on the revenue requirement. The net effect is an increase in the revenue requirement of $79 million over what it would be if the return on equity and cost of debt were fixed at 2013 levels for the duration of the Custom IR.

Parties were generally opposed to Enbridge's proposal. They argued that the approach was inconsistent with Board policy and proposed that the return on equity and cost of debt should be fixed at the 2013 levels for the duration of the Custom IR.

Board Findings

The Board accepts Enbridge's proposal to set the capital structure at 64% debt and 36% equity. This aspect was not contentious.

Enbridge argued that return on equity and cost of debt should be determined in a consistent way. The Board agrees with this position. Most arguments focussed on the return on equity, so the Board will consider that component first.

Energy Probe and BOMA argued that Enbridge's proposal to forecast return on equity for five years based on first quarter 2013 data is inconsistent with Board policy. The Board agrees. Although the Board's RRFE Report does not establish a policy for how the cost of capital should be determined under Custom IR, the cost of capital is a genuine cost to the company and theoretically a Custom IR could incorporate a forecast of the return on equity for each year of the Custom IR term. However, Enbridge's approach to developing the forecast return on equity stretches the Board cost of capital policy beyond what was contemplated by the Board. In its Cost of Capital Report the Board confirmed that it would continue to use a formula-based equity risk premium approach to set the return on equity for distributors that had filed a cost of service application – a single year application. At the time that policy was set, the Board had not contemplated applications for a five year revenue requirement.

The Board could consider applying its cost of capital policy to setting the return on equity for a longer term, but there would need to be a sufficient evidentiary basis. SEC and APPrO submitted that there was insufficient evidence to support the return on equity forecast because interest rates are inherently difficult to forecast and typically require expert evidence, and this was not provided. Board staff submitted that interest rate projections are notoriously inaccurate especially when extending to five years. The Board agrees with these arguments. Using interest rate forecasts made in the first half of 2013 to project estimates for five years is not sufficient evidence to set the return on equity for five years. The Board finds that expert testimony and appropriate discovery would be required to substantiate the forecast element of the formula-based equity risk premium and to assess fully the alternatives and consequences.

Finding that there is insufficient evidence to approve a five year forecast for return on equity, the Board has two options: fix the return on equity now for the duration of the Custom IR or update the return on equity each year during the annual rate adjustment proceeding.

Many parties submitted that the return on equity should be fixed now for the duration of the Custom IR, arguing that under traditional IR, the return on equity is set in base rates and remains in place throughout the IR term. In the view of some parties, the base year should be the 2013 cost of service proceeding. CME argued that fixing the cost of capital at the base year levels for the full term of the IR Plan is one of the added risks assumed by the utility as part of an IR structure. BOMA pointed out that fixing the cost components at the base year levels was the practice in the prior Enbridge IR Plan (as well as Union Gas' two recent IR plans) and that there is no justification to change the approach.

Enbridge responded that these arguments were flawed in two respects. First, Enbridge noted that no party contended that interest rates and credit spreads (which drive the determination of return on equity under the Board's formula), will be constant over the IR term. Second, the company submitted that the suggestion that the return on equity is fixed under traditional IR is misleading because under traditional IR the return on equity is part of the overall revenue requirement that is subject to annual formulaic increases through the escalation factor. The Board accepts Enbridge's characterization that the return on equity under traditional IR has an implied escalation factor. In comparison, fixing the return on equity under a Custom IR would truly fix the return on equity over the full term. Whether this would be to the benefit of the company or ratepayers would depend on how rising or falling equity and debt rates contributed to the net position.

The other option would be to set the return on equity each year as part of the annual rate adjustment process. Enbridge included this proposal in its reply argument. The company noted that before making its application it had considered whether the return on equity should be re-set each year. However, it had decided against that approach and advanced a forecast approach in its application in order to minimize the number of annual adjustments. Having considered stakeholder submissions, Enbridge proposed that the return on equity (and the cost of debt) be set for each year during the annual rate adjustment proceeding using the Board's established methodology. Under this revised approach the cost of capital for 2014 would be set on a final basis in this proceeding. The cost of capital for 2015 to 2018 would be set on a placeholder basis in this proceeding, and then be set on a final basis in the relevant annual rate adjustment proceeding. Enbridge proposed that the return on equity (and cost of debt) would be determined using the most up-to-date data available at the time of each application. If timing permitted, Enbridge proposed to use the Board-approved return on equity, which is currently prepared in October and published in November each year.

If the Board were to update the return on equity each year using the Board approved parameters the process would be fairly straightforward, but the company would be shielded from any forecast risk. When compared to fixing the cost of capital now, the company might be better or worse off. Having considered the two options and the circumstances of this application, the Board concludes that the preferred approach is to update the return on equity each year during the annual rate adjustment proceeding using the Board approved parameters. The Board publishes these figures in November which should provide Enbridge with adequate time to incorporate them into the final rates.

Having already determined that the return on equity and cost of debt should be determined on a consistent basis, the Board concludes that the cost of debt should also be set each year through the annual rate adjustment proceeding. The Board accepts that setting the cost of debt may be somewhat more contentious than setting the return on equity since it will not be formulaic; however, there is evidence in this proceeding which provides an indication of the expected timing for future debt issues and, as a result, the issue may be amenable to negotiation among the parties.

Site Restoration Costs ("SRC")

Site restoration costs ("SRC") are also referred to as net salvage. Net salvage values can be positive or negative. When assets are retired and replaced, if the proceeds of disposal do not cover the costs of removal then the net salvage is negative. The Board has approved the recovery of SRC as part of Enbridge's composite depreciation rates since at least 1959, either directly or through the acceptance of settlement agreements.

For regulatory purposes, SRC forms part of accumulated depreciation. Rate base and the return on rate base are lower as a consequence. Enbridge recovers SRC annually through depreciation expense included in its revenue requirement. Enbridge's audited financial statements have been prepared in accordance with US Generally Accepted Accounting Principles ("US GAAP"). For purposes of financial statement disclosure, Enbridge reports SRC as a long-term liability as a result of rate regulation. As of December 31, 2013, SRC is $903.9 million.

Enbridge retained Gannett Fleming to complete a number of comprehensive depreciation studies for Enbridge. Its most recent 2011 study was based on a review of assets in service through December 31, 2010, and at that time, Enbridge's SRC was calculated to be more than $700 million. Gannett Fleming carried out a two-phase review of net salvage calculations and recommended that Enbridge stop using the traditional method for SRC and instead adopt the Constant Dollar Net Salvage ("CDNS") method. The primary difference between the traditional method and the CDNS method is the treatment of inflation and expected lives. Enbridge described it as follows:

> *Under the CDNS approach, historic transactions are revalued to a current cost to allow for a current cost percentage of net salvage with the impacts of historic inflation removed; the current cost estimate is then inflated using appropriate estimates for future inflation.*[17]

Historic inflation rates were substantially higher than current and expected inflation rates. By adopting the CDNS method beginning in 2014, the result is that substantially more SRC has been collected in the past than is now considered necessary. In addition, under CDNS, lower depreciation rates are required on a going-forward basis. These two impacts would reduce costs to ratepayers. While CDNS has not been widely adopted in

[17] Enbridge, Argument in Chief, p. 59.

Canada, Mr. Kennedy, the expert witness from Gannett Fleming explained that often its adoption results in higher rates but that Enbridge was unique amongst Canadian utilities in terms of the timing of its growth and retirements. Mr. Kennedy was confident that the circumstances which led to a reduction in SRC under CDNS for Enbridge would not change over the next five years.

Enbridge submitted that the CDNS approach is a conceptually preferable methodology which results in both a substantial refund to ratepayers and reduced rates over the term of the Custom IR. Enbridge proposed to return the excess SRC to ratepayers using a rate rider over the Custom IR period, and the amount was calculated to be $259.8 million. This rate rider would not directly affect rates and would not be included in revenue requirement, but would have the impact of lowering ratepayer bills from what they would otherwise be.

The return of $259.8 million to ratepayers does indirectly affect revenue requirement (and therefore rates) in three ways. First, as amounts are refunded to ratepayers, accumulated depreciation is reduced, net rate base increases and Enbridge's cost of capital is applied to a higher rate base. Second, the return of amounts to ratepayers gives rise to a tax deduction which lowers taxes payable. Third, lower depreciation rates going forward reduce the revenue requirement. These three effects result in a cumulative revenue requirement reduction of $241.4 million during the Custom IR plan.

There was little support for Enbridge's proposal. Board staff argued that there should be no refund; some intervenors argued that the refund should be greater than $259.8 million, while others, led by SEC, argued that the full $900 million should be returned. Many parties argued that the amount collected through rates going forward should be reduced to the amount forecast to be spent on SRC. A number of parties also recommended a generic proceeding on the issue.

Board Findings

The Board will accept Enbridge's proposal to adopt the CDNS method for site recovery costs, including the amounts to be collected during the Custom IR period. However, the Board will make some adjustments to the refund amount which will also impact rates through the three effects described above. The Board will consider further whether a generic proceeding is warranted, but will require Enbridge to undertake additional work regarding the discount rate to be used and whether a segregated fund should be established.

The arguments raised four main issues, which the Board will address in turn:

1. Should the CDNS method be adopted?
2. If the CDNS method is adopted, should there be any adjustments to Enbridge's proposal?
3. What amount should be collected for SRC going forward?
4. Should the Board conduct a generic proceeding or review?

Should the CDNS method be adopted?

SEC agreed with Enbridge that the CDNS method is better than the traditional method, but argued that the Board should reject both methods. SEC submitted that Enbridge should not recover SRC from ratepayers as part of depreciation expense within revenue requirement; instead the company should recover SRC as an annual expense using amounts to be spent in the test period. In SEC's view, this would be consistent with US GAAP. As a result, SEC also submitted that the Board should order the return of the total accumulated SRC to ratepayers (approximately $903.9 million) over ten years. SEC provided a detailed explanation of how the refund should be implemented taking into account rate base and income tax effects, and the objective of preventing a significant rate increase when the refund period ends.

IGUA, the Federation of Rental Property Owners ("FRPO"), and CCC supported SEC's position. CME largely supported SEC's position, but argued that $500 million should be refunded to ratepayers during the IR term, and a generic proceeding should be used to determine what should be done with the remaining balance. CME also submitted there was conceptually little difference between SRC and deferred taxes. Energy Probe agreed with CME and submitted that the Board should follow a similar approach to that used by Union Gas for the refund of accumulated deferred tax balances in the late 1990's. VECC supported SEC's argument and recommended drawing down the SRC to a more appropriate balance by providing ratepayers with a phased, front-end loaded offset to revenue requirement.

Enbridge responded that its proposal had the support of Mr. Kennedy and that no other witnesses testified on the issue. Enbridge urged the Board to assess the proposals made by others by considering the extent to which they have appropriate evidentiary grounding. Specifically, Enbridge argued that the Board should consider whether the various proposals should have been the subject of evidence called specifically to support them, whether they should have been tested during the evidentiary phase of the hearing and, in some instances, whether they should at least have been put to the witnesses.

SEC maintained that its proposal was fully consistent with US GAAP, and that its proposal was essentially the default approach under US GAAP, and argued the following:

> *Now that US GAAP has been adopted and approved, the question should be whether there is a good regulatory reason for the Board to overrule the normal accounting rule for removal and site restoration costs, and instead impose its own rule (for example, net negative salvage).*[18]

The Board finds that this is not the appropriate question. The Board is not “overruling” US GAAP; the Board is considering whether to approve the continuation of a long-standing regulatory approach to dealing with site restoration costs with a change in the methodology to adopt CDNS. In that context, the appropriate consideration is whether there are significant flaws in the current overall approach and whether there is sufficient evidence to adopt an alternative approach to SRC.

The Board finds that, in principle, it is reasonable for current ratepayers to pay toward the cost of eventually retiring the assets which they are currently using. The timing and the extent of these future costs are inherently uncertain, hence the reliance on specialized studies by depreciation experts, and periodic reviews and updates. This overall approach has been approved by the Board, and in many instances agreed to by the parties through settlements, for a long period of time. Enbridge is proposing to modify the overall approach to use CDNS, but SEC is proposing a very significant change to the overall approach. Given the long-standing approval of the overall approach, the Board would need compelling reasons to make a significant change and robust evidence as to all the associated impacts. The Board has neither in this case. There are three reasons for this conclusion.

First, the objections to Enbridge’s overall approach are largely grounded in the view that the amount being recovered will never be used to cover actual costs because asset lives are getting longer and Enbridge continues to grow. A number of parties have likened the

[18] SEC, Argument, p. 76.

issue to deferred taxes. SEC argued that collections will continue to exceed outlays for the foreseeable future and therefore the situation is like deferred taxes for which there is little likelihood of eventual payment as long as the company continues to grow. However, there was little evidence or analysis to support this analogy or examine how the two issues might differ. For example, if Enbridge's growth slows or stops, the return of the total SRC now would appear to shift a considerable SRC burden to future ratepayers at a time when those ratepayers might also be burdened by the other potential rate impacts of a slow-growth or no-growth utility.

Second, SEC argued that the National Energy Board has already decided that similar costs should be dealt with on a current cost basis. However, there was no evidence on this point, and in its reply, Enbridge disputed SEC's interpretation of the National Energy Board's approach.

Third, SEC further argued that there is no segregated fund to protect ratepayers. But that is not a reason to return the funds now to ratepayers – that is an argument to examine whether some additional ratepayer protection is warranted, perhaps in the form of a segregated fund. This issue is addressed later in this section.

The Board concludes that there is no compelling reason to reject the overall approach to SRC. Having determined that it is appropriate to maintain the current practice of collecting money from current ratepayers to fund the future retirement and restoration costs, the Board must consider whether it is appropriate to change from the traditional method to the CDNS method. Other than Board staff, no party argued for the retention of the traditional approach.

Board staff argued that there is uncertainty about asset lives and asset replacements and therefore the SRC should be retained in full. Board staff submitted that Enbridge had provided sufficient evidence that the company will require several billion dollars in the future to remove and replace assets at the end of their useful lives and noted Mr. Kennedy's view that the amount would exceed $3 billion. Board staff was not opposed to the adoption of the CDNS method, but submitted that it should not be implemented until a new asset plan has been completed.

While Enbridge's future site restoration costs may be significant, there is no compelling evidence that those requirements will be of the magnitude and timing that would warrant setting aside Gannett Fleming's analysis of the appropriate SRC level. The evidence was in fact more weighted toward the conclusion that as Enbridge continues to grow, the recoveries for SRC will exceed the outlays. The Board concludes that the CDNS should be adopted.

If the CDNS approach is adopted, should there be any adjustments to Enbridge's proposal regarding the determination of the refund?

Enbridge proposed to refund $259.8 million in excess SRC over the Custom IR term. Three areas were raised in submissions: foregone interest, the discount rate, and the point in time to be used for the calculation. The Board will address each in turn.

BOMA supported Enbridge's proposal but argued that an additional amount should be deducted from the revenue requirement each year for foregone interest. In BOMA's view, Enbridge has received an interest free loan from ratepayers in the form of the SRC funds and this "foregone interest" should be returned. BOMA is incorrect. The evidence is clear that interest was not paid on the SRC balance because the amount operated as a reduction to rate base and hence the return on rate base (paid by ratepayers) was lower than it otherwise would have been.

Gannett Fleming performed its analysis using a discount rate of 2.38%, the then current rate for long Canada bonds (October 2012). This is comparable to the rate mandated under Canadian GAAP for Asset Retirement Obligations ("ARO"). SEC argued that if the proposal is accepted, the discount rate should be adjusted for three reasons:

1. Under US GAAP, the discount rate for ARO is the credit-adjusted risk free rate, which in SEC's view is the weighted average debt rate for Enbridge.
2. The rate is to be a proxy for the expected investment returns on the reserve, and 2.38% is unreasonably low.
3. Pension funds have a similar structure and Enbridge used a discount rate of 4.3% which was recommended by its advisors as of December 2012.

CME agreed that a higher discount rate should be used and submitted that the refund amount over the period 2014 to 2018 should be at least $500 million, which is essentially the level of refund by 2018 under SEC's proposal.

Enbridge responded that there is no evidence to support any discount rate other than the one used by Gannett Fleming. The Board does not agree. SEC has identified a number of facts which strongly suggest that an appropriate discount rate would be higher than

2.38%, and in particular the fact that 4.3% is being used for the pension funds. In addition, Mr. Kennedy supported his use of 2.38% as being comparable to what he has used in other analyses, but he acknowledged *"I'll admit to not thinking about trying to normalize that discount rate with other net present value calculations the company had made in other areas."*[19] The Board finds that this is a significant consideration.

The evidence is that if the discount rate were increased to 4.95%, which SEC identified as Enbridge's weighted cost of debt, the excess SRC would increase by an estimated $243 million and the annual SRC provision over the Custom IR term would decline by an estimated $174 million. The Board concludes that the discount rate should be examined in more detail at the next rebasing, however, for the 2014 to 2018 period, the refund will be increased by $120 million and the SRC provision will be reduced by $85 million. This represents half of the estimated impact of using a discount rate of 4.95% and the Board finds that to be a reasonable proxy for a more appropriate discount rate based on the evidence in this proceeding.

The excess SRC has been calculated as of December 31, 2010, but SEC argued that if Enbridge's proposal is accepted, at a minimum the amount should be updated to December 31, 2013. SEC argued that the evidence suggests that excess SRC was higher at the end of 2013 than at the end of 2010 by about $100 million, Mr. Kennedy acknowledged that there would likely be additional excess SRC, but did not recommend that the refund amount be re-calculated or re-estimated. Mr. Kennedy testified that it would be a complex undertaking to do an accurate re-evaluation as of the end of 2013 and he also explained that lags were not uncommon given the time required to produce the necessary studies and the periodic nature of major depreciation studies. The expectation is that another major study would be done in 2017 or 2018.

The Board accepts that studies of this nature will create some amount of lag which will be corrected with the subsequent study. The Board will not order an additional refund of excess SRC. Although the lag will be substantial by the time the next depreciation study is completed, the Board has already increased the refund to address the discount rate issue. The Board wishes to be cautious, pending the resolution of the discount rate issue, to ensure that the refund does not end up being too high.

Enbridge proposed to refund $259.8 million; the Board will require a refund of $379.8 million. The adjustment will have consequential impacts on the rate base and income tax

[19] Tr. 9, p. 126.

calculations. Enbridge will be required to calculate these impacts as part of the rate order process.

What amount should be collected for SRC going forward?

Enbridge proposed to recover $247.3 million for SRC over the IR period. The company forecast that it would spend $76.4 million on restoration projects in that period. Board staff, CME and SEC argued the amounts collected should be limited to the forecast expenditure.

The Board has decided that it will continue to approve Enbridge's overall approach to SRC with the modification to use CDNS. Part of that approach is that the annual collections for SRC may exceed the actual expenditures. As discussed above, the Board finds no compelling reason to depart from this approach at this time. The Board has addressed the issue of the discount rate above and has directed that the SRC collected over the IR period be reduced by $85 million. This will reduce the amount collected from the proposed level of $247.3 million to $162.3 million.

SEC pointed to the National Energy Board and claimed that it approved the recovery of retirement costs as a current expense. Enbridge disagreed with this interpretation. There is limited evidence in this proceeding about the National Energy Board's approach to this issue, and there is no analysis of whether the approach would be applicable to Enbridge.

Should the Board conduct a generic proceeding or review?

Board staff recommended that the Board require Enbridge to produce a report addressing the implications of creating an irrevocable trust for the SRC amounts. Staff suggested that the report could be filed and form a part of the 2014 ESM application expected to be filed in the spring of 2015.

CME and SEC recommended that the Board conduct a generic review of SRC and that the review should be informed by the National Energy Board proceeding on abandonment costs and the National Energy Board principles related to abandonment costs and removal costs. SEC submitted that the generic review should include gas and electricity distributors and electricity transmitters and should address issues related to how funds should be collected and whether they should be segregated. In SEC's view, the generic review could be done in parallel with the SEC proposal to refund the entire balance over

10 years, as the amounts to be returned by the end of 2018 would still allow for adjustments going forward. FRPO, CCC, and IGUA supported a generic review.

Enbridge responded that there is no evidence of a live issue with respect to SRC involving any other utility regulated by the Board. Enbridge also expressed doubt that Union Gas will be addressing an SRC issue in the near future or at all, given that Union Gas is in the first year of a five-year IR plan and no SRC issue is evident within that plan.

The evidence in this case shows that the approach to SRC is case specific in terms of the age of the utility's assets, the replacement schedule, expected growth, and SRC accumulated to date. A generic review might be used to assess the current situation and set principles, but it is not clear that the issue warrants such a review at this time. The Board will consider the recommendations by parties as it conducts its business planning over the next period. However, the Board will direct Enbridge to examine the issue of whether a segregated fund should be established as a means of protecting ratepayers. Enbridge shall present this evidence as part of the first application following this Custom IR.

Deferral and Variance Accounts

Enbridge has a number of deferral and variance accounts in place. For some, it has proposed to retain the accounts unchanged; for a few accounts Enbridge has proposed changes. Enbridge also proposed several new accounts. Each category is addressed below.

Existing Accounts – no changes proposed

Enbridge proposed to maintain a number of previously approved accounts. Each would be in place for the full IR term, with the exception of the Design Day Criteria Transportation Deferral Account, which would be in place for 2014 only:

- Design Day Criteria Transportation Deferral Account ("DDCTDA") (2014 only)
- Purchased Gas Variance Account ("PGVA")
- Unaccounted for Gas Variance Account ("UAFVA")
- Storage and Transportation Deferral Account ("S&TDA")
- Deferred Rebate Account ("DRA")
- Customer Care CIS Rate Smoothing Deferral Account ("CCCISRSDA")
- Average Use True Up Variance Account ("AUTUVA")
- Manufactured Gas Plant Deferral Account ("MGPDA")
- Ontario Hearing Costs Variance Account ("OHCVA")
- Electric Program Earnings Sharing Deferral Account ("EPESDA")
- Ex-Franchise Third-party Billing Services Deferral Account ("EFTPBSDA")
- Post-Retirement True-Up Variance Account ("PTUVA")
- Lost Revenue Adjustment Mechanism Variance Account ("LRAM")
- Demand Side Management Incentive Deferral Account ("DSMIDA")
- Transition Impact of Accounting Changes Deferral Account ("TIACDA")
- Open Bill Revenue Variance Account ("OBRVA")

Parties only made submissions on two of the accounts: the OHCVA and the DDCTDA.

Board staff, CCC, SEC and EP all submitted that the OHCVA should be discontinued. They argued that hearing costs are part of a normal business activity and that no other Ontario utility has a similar account. Enbridge argued that the account is necessary because the expenses are unpredictable and out of company control. The company noted that the account has been in place for 15 years, often under the framework of a settlement agreement.

FRPO submitted that the DDCTDA should be retained beyond 2014 and kept separate from the new UDCDA to ensure transparency. In FRPO's view, it is not appropriate to merge accounting of a number of factors given the current uncertainty about infrastructure development and possible National Energy Board decisions. Enbridge responded that the account does not need to be maintained, arguing that it would not be possible to distinguish the amounts due to historic changes in design day and those related to procuring long haul Firm Transportation ("FT") rather than short haul.

Board Findings

The Board will discontinue the OHCVA. The Board finds no evidence of an ongoing need for a cost pass-through for what is a standard activity for a regulated utility.

The Board concludes that the DDCTDA should be discontinued after 2014, as proposed by Enbridge. The Board agrees with the company that it will be impractical to attempt to distinguish the balances in the way proposed by FRPO. The Board notes the extensive gas supply reporting agreed to by the company and finds that this information will provide sufficient transparency in this area.

All the other accounts in the list above are approved for continuation.

Existing Accounts – changes proposed

Enbridge proposed to make modifications to a number of previously approved accounts:

- Gas Distribution Access Rule Impact Deferral Account ("GDARIDA")
- Demand-Side Management Variance Accounts ("DSMVA")
- Transactional Services Deferral Account ("TSDA")

Gas Distribution Access Rule Impact Deferral Account ("GDARIDA")

The GDARIDA is used to record all incremental unbudgeted capital and operating costs associated with the development, implementation, and operation of the Gas Distribution Access Rule ("GDAR") and any amendments to the rule. The GDARIDA was previously approved as, and known as, the Gas Distribution Access Rule Cost Deferral Account, (“GDARCDA”). The company is proposing an alteration to the scope of the account to include all financial impacts which could arise as a result of changes in GDAR. No party objected to this proposal.

Demand-Side Management Variance Accounts (“DSMVA”)

Enbridge has three DSM deferral and variance accounts for 2014. The company proposed to establish that same group of accounts for 2015 through 2018, but indicated that it has not received any direction from the Board. Additionally, Enbridge proposed that any further variances in DSM spending and results, beyond those included within the 2014-2018 forecasts, which occur as a result of Board decisions in any other proceeding be included within each of the 2014-2018 DSM variance accounts. Enbridge explained that it has included the approved or projected level of DSM spending in each of its 2014-2018 forecasts of costs. No party objected to this proposal.

Transactional Services Deferral Account (“TSDA”)

The proposal for the 2014-2018 TSDA is to record the incremental net revenue from transportation and storage related Transactional Services, to be shared 90/10 between Enbridge’s ratepayers and shareholders. While Enbridge proposed to continue to include a forecast of $12 million in Transactional Services revenue as an offset to rates, the company proposed to remove the $8 million guarantee (a maximum $4 million credit to the company). The result would be that up to the full $12 million could be returned to Enbridge. Enbridge justified this proposal on the basis of recent changes in TCPL tolls and the resulting uncertainty about future prices and potential related impacts.

A number of parties objected to this proposal. Board staff argued that the base amount should be increased to $24 million from $12 million, based on performance in 2012 and 2013, and that the maximum credit should be increased from $4 million to $8 million. The net effect would be a $16 million guarantee to ratepayers. FRPO considered staff’s position, but acknowledged that the company will be managing significant exposure to unabsorbed demand charges and submitted that increasing the amount and the guarantee would not be justified. FRPO concluded that no change should be made to the account. BOMA and CCC also argued that the guarantee should remain unchanged. Enbridge responded that the current approach is not appropriate because of current and expected changes in TCPL’s tolls and services, as well as the company’s own service changes.

Enbridge noted that the FT-RAM program (which has been a large proportion of Transactional Services revenues) has been discontinued, the amount of capacity available for release is high, there will be reduced reliance on long-haul because of the GTA project, and the revenue from storage continues to decline. Enbridge concluded that the opportunities to earn Transactional Services will be reduced, so it would be appropriate to remove the $8 million guarantee.

Board Findings

The proposed changes to DSMVA and GDARIVA were unopposed and will be accepted by the Board. The Board notes that further direction regarding DSM accounts may arise from the current DSM consultation.

The Board approves the proposed change to the TSDA. The Board accepts the company's evidence that a number of significant changes have taken place in the market and these changes are likely to reduce the opportunities for Transactional Services and therefore the associated revenues. Once there is more experience under the new market conditions, the Board will consider whether a ratepayer guarantee should be reinstated.

Proposed New Accounts

Enbridge proposed eight new accounts:

- Earnings Sharing Mechanism Deferral Account ("ESMDA") (2014-2018)
- Unabsorbed Demand Cost Deferral Account ("UDCDA") (2014 only)
- Customer Care Services Procurement Deferral Account ("CCSPDA") (2014-2016)
- Greenhouse Gas Emissions Impact Deferral Account ("GGEIDA") (2014-2018)
- Constant Dollar Net Salvage Adjustment Deferral Account ("CDNSADA") (2014-2018)
- Greater Toronto Area Project Variance Account ("GTAPVA") (2014-2018)
- Relocation Mains Variance Account ("RLMVA") (2017-2018)
- Replacement Mains Variance Account ("RPMVA") (2017-2018)

Earnings Sharing Mechanism Deferral Account ("ESMDA")

The purpose of the ESMDA is to record the ratepayer share of annual utility earnings that result from the earnings sharing mechanism throughout the term of the Custom IR.

This issue has been addressed earlier in this decision, and the account will be structured accordingly. Simple interest will be calculated on the opening monthly balance of the account using the Board approved EB-2006-0117 interest rate methodology.

Unabsorbed Demand Cost Deferral Account ("UDCDA") (2014 only)

Enbridge intends to contract for incremental one-year long-haul FT capacity on TCPL to meet its Peak Day requirements in 2014. If the company is unable to use 100% of its capacity, then the associated Unabsorbed Demand Costs "UDC" will be debited in the UDCDA (excluding the amounts that will be captured in the DDCTDA). Enbridge's forecast of UDC costs for 2014 is $62.8 million (excluding amounts that may be recorded in the 2014 DDCTDA), and that is the maximum amount that may be recorded in the 2014 UDCDA. Enbridge committed to using its best efforts to mitigate the UDC and will provide the balance in the UDCDA and DDCTDA through the QRAM process. Simple interest will be calculated on the opening monthly balance of the account using the Board approved EB-2006-0117 interest rate methodology.

Board Findings

No party objected to this account, and the Board will approve it.

Customer Care Services Procurement Deferral Account ("CCSPDA")

Enbridge proposed that the CCSPDA be in place for 2014, 2015 and 2016 to capture the costs associated with the benchmarking, tendering and potential transition of customer care services to a new service provider(s). Enbridge would then bring forward the costs recorded in this account for recovery in rates in 2017. Simple interest is to be calculated using the Board approved EB-2006-0117 interest rate methodology.

Energy Probe supported the account, but submitted that there should be a cap of $5 million to provide an incentive to Enbridge to manage its costs. BOMA supported Energy Probe's position. Enbridge responded by accepting the $5 million limitation proposed by Energy Probe.

Board Findings

The Board will approve the account, with the $5 million limit.

Greenhouse Gas Emissions Impact Deferral Account ("GGEIDA")

The GGEIDA would be used to record the impacts of provincial and federal regulations related to greenhouse gas emission requirements along with the impacts resulting from the sale of, or other dealings in, earned carbon dioxide offset credits. This new account would replace the more limited Carbon Dioxide Offset Credits Deferral Account ("CDOCDA"). Simple interest is to be calculated on the opening monthly balance using the Board approved EB-2006-0117 interest rate methodology.

Board Findings

No party objected to this account, and the Board will approve it.

Constant Dollar Net Salvage Adjustment Deferral Account ("CDNSADA")

The CDNSADA is part of the company's proposal related to site restoration costs (the SRC issue). The SRC issue has been addressed earlier in this decision, and the CDNSADA account will be structured accordingly. Because the balance in the account will offset rate base, Enbridge proposed that no interest be calculated for this account. The Board accepts this approach.

Greater Toronto Area Project Variance Account ("GTAPVA")

This account request has already been addressed in the capital expenditure section.

Relocation Mains Variance Account ("RLMVA") and Replacement Mains Variance Account ("RPMVA")

These account requests have already been addressed in the capital expenditure section.

Cost Allocation and Rate Design

Introduction

Enbridge is not proposing any changes to its Board approved cost allocation methodology for 2014. The company is proposing some modifications to Rate 100 and Rate 110, and to the Rate Handbook.

This decision addresses the following issues:
- Allocation of costs to Rate 125
- Allocation of costs to non-utility storage
- Changes to Rate 100 and Rate 110
- Rate 332
- Rate Handbook changes

Allocation of Costs to Rate 125

APPrO submitted that costs are being over-allocated to Rate 125. APPrO identified two specific concerns:
1. the allocation of extra-high pressure (XHP) pipeline assets to Rate 125 when those pipes are not used to serve Rate 125 customer and are not capable of serving those customers; and,
2. the impact of the economic feasibility analysis conducted for new Rate 125 customers (to determine the initial contribution) combined with the cost allocation process for major new reinforcement projects (to determine ongoing charges).

APPrO sponsored expert evidence by Mr. Todd and Mr. Roger of Elenchus. The Board will address each of the concerns separately.

Allocation of XHP assets

Rate 125 is currently allocated a portion of the costs of all XHP pipeline assets. These pipelines vary in size from 1.5” to 36”. APPrO submitted that Rate 125 customers should only be allocated costs for pipelines actually used to serve Rate 125 customers, specifically only pipes which are 12” and larger. APPrO argued that its proposal is not contrary to the principle of postage stamp rates because the issue is not related to making distinctions based on the vintage of the assets, which is a key concept of postage stamp rates. In APPrO's view, the issue is between higher and lower capacity assets (i.e. pipe diameter). APPrO pointed out that Enbridge already distinguishes between higher capacity (TP) and lower capacity (HP and LP) pipelines and argued that a further distinction of TP assets which better reflected cost causality would be appropriate. APPrO also submitted that it was appropriate to make incremental changes to the cost allocation process where justified, and that it was not necessary to undertake a complete cost allocation study before making an incremental change.

Enbridge responded that it would be inappropriate to make one change in isolation of a broader examination of cost allocation. Energy Probe took the same position. Enbridge argued that looking at isolated cost elements (such as pipeline assets) is contrary to postage stamp rates:

> *Therefore, should the current Board approved postage stamp cost allocation methodology be changed (i.e. to make it more detailed), it could not be done appropriately (reflecting postage stamp principles) based on an isolated parameter such as the pipe size. Other elements comprising the total cost of the XHP (TP) system and the allocation of these to the customer classes would need to be taken into account as well in order to maintain cost causality. The approach proposed by APPrO does not accomplish this.*[20]

Enbridge noted that different options would have different consequences, including possibly increasing the level of costs allocated to Rate 125 (for example, allocating costs based on peak hourly demand rather than peak daily demand). Enbridge submitted that even if the Board adopts APPrO's proposal, then Rate 125 customers should at least be allocated the costs of pipes that can serve Rate 125 customers. Enbridge pointed out that this would be consistent with Elenchus' approach and would result in pipes 6" and larger being allocated to Rate 125. Enbridge also argued that if this change were made, then the allocation factor would need to be changed.

APPrO maintained that no change to the associated allocation factor would be necessary. APPrO argued that because gas generally flows through larger diameter XHP system before the smaller diameter XHP, if the XHP system is divided into two categories (over

[20] Enbridge, Reply Argument, p. 136.

and under 12"), there is still no change in the customers which are using the larger section of the system:

> *It is still the same customers (all of them) with the same cost responsibility as determined by the peak day allocator. The allocator is still valid, based on cost causality, to allocate category one XHP, since the allocator reflects how the XHP category is used. If not all customers use XHP category one, then the allocator would have to be different, but that clearly is not the case.*[21]

The company responded:

> *…cost causality would not be maintained if certain pipeline diameters and associated costs are removed from the cost of the XHP system, without making a corresponding adjustment to the Delivery Demand TP allocator to account for the demand that is met through those pipelines.*[22]

Enbridge did not present evidence as to how the allocators should change, but instead argued that any changes to the cost allocation should be done only on a holistic basis which would include an examination of other cost elements as well as the allocation factors.

Board Findings

There are two main issues at play: 1) to what level of detail should assets be divided to ensure a fair allocation within the overall framework of appropriate cost allocation; and 2) is it appropriate to make incremental changes in the absence of a complete review of the cost allocation.

With respect to the division of assets, the Board finds that it is generally inappropriate to allocate the costs of assets to a class of customers if those assets are incapable of serving that class of customers. The evidence is clear that high pressure pipelines less than 6" in diameter cannot be used to serve Rate 125 customers. On that basis, pipelines under 6" should not be allocated to Rate 125. APPrO pointed out that no Rate 125 customers are served using pipes less than 12" and that Enbridge's evidence is that it

[21] APPrO, Argument, p. 26.
[22] Enbridge, Reply Argument, p. 140.

would be unlikely to attach a new Rate 125 customer to an existing 6” or 8” line. However, Rate 125 covers a wide range of load sizes. The addition of a smaller Rate 125 customer using a 6” or 8” pipeline would have the effect of introducing instability into the cost allocation process if the allocation were based on what is used to serve, as opposed to what is capable of serving. The Board finds, therefore, at a minimum, Rate 125 should be allocated the costs of pipelines which are physically capable of serving the load; in other words, 6” and greater. This is consistent with Elenchus’ recommendation.

There has not been a systematic review of all cost categories related to Rate 125. It may be that such an analysis would result in additional costs allocated to Rate 125. This is one of the concerns with making incremental changes in the absence of a full cost allocation study. However, the Board finds that ratepayers should be able to make a case for an incremental change without bearing the responsibility for conducting a complete cost allocation analysis. It was open to Enbridge to provide responding evidence outlining other specific modifications which should be considered. It did not do so. For example, Enbridge asserted that the allocation factor should be changed if the XHP assets were sub-divided, but it did not provide evidence as to why or how the allocation factor should be changed. In addition, the Board is prepared to make this incremental change because it will have a negligible impact on the rates of other classes, and therefore other ratepayers are not materially adversely impacted.

Economic Feasibility Analysis and Ongoing Rates

APPrO submitted that Rate 125 customers are paying twice for excess capacity in the system: at the time of the initial economic feasibility analysis through contribution charges and again through ongoing charges for additional capacity which is designed to meet 20-year growth for general service customers. APPrO was unable to estimate the impact of this issue because Enbridge declined to provide a working copy of the cost allocation model. APPrO proposed that the issue should be addressed at the next application and that the Board should direct Enbridge to study the issue with stakeholders and make a proposal. Enbridge responded that there is very little excess capacity and it only exists for a short period. In Enbridge’s view, there is no meaningful issue to be addressed.

Board Findings

The Board will not adopt APPrO’s proposal. The economic feasibility analysis and capital cost recovery is done in order to offer a Rate 125 customer a billing contract demand which results in a bypass competitive rate. Once a customer is connected, it becomes part of the larger system and should share in the cost responsibility for that system. The Board accepts Enbridge's evidence that the excess capacity associated with reinforcement projects is limited in size and duration and concludes that there is no compelling basis on which to require further analysis of this issue at this time. It is open to APPrO to pursue this issue when a full cost allocation is presented.

Allocation of Costs to Non-Utility Storage

FRPO raised concerns about two related storage cost allocation issues: base pressure gas and lost and unaccounted for gas. FRPO argued that the question of whether base pressure gas should be allocated to non-utility storage on a fully allocated cost basis or on an incremental cost basis would need to be resolved at a future proceeding. FRPO further submitted that it was not clear whether any cost for lost and unaccounted for gas had been allocated to non-utility storage, but that some level of cost should be. FRPO proposed that 12.4% of total lost and unaccounted for gas should be allocated to non-utility storage (at the QRAM price), noting that this would provide an incentive to Enbridge to complete the necessary study. BOMA supported FRPO's position.

Enbridge responded that no incremental costs have been allocated to utility customers as a result of unregulated storage. Enbridge noted that it is doing an engineering study to see if lost and unaccounted for gas has changed and if it is higher, then the shareholder will bear that cost if it is the direct result of unregulated storage. Enbridge maintained that any change in lost and unaccounted for gas will be allocated on cost causation principles.

Board Findings

Based on the evidence in this proceeding and Enbridge's submissions, it appears that costs for base pressure gas and lost and unaccounted for gas are being allocated to non-utility storage operations on an incremental cost basis. It is not clear to the Board that an incremental cost basis is appropriate. Generally, costs should be allocated to non-utility operations on a fully allocated cost basis to ensure there is no cross-subsidy to the competitive business from the regulated business. Union Gas uses a volumetric approach to allocate costs between utility and non-utility storage.

The Board will not order a specific allocation at this time, however, the Board directs Enbridge to prepare the necessary evidence and proposal in time for the 2015 or 2016 rate application. Regardless of the company's proposal, the evidence must contain the information necessary to make an allocation of base pressure gas and lost and unaccounted for gas to non-utility storage on a fully allocated cost basis and on a volumetric basis. Suitable estimations or approximations will be acceptable.

Changes to Rate 100 and Rate 110

Enbridge proposed to change Rate 100 (Firm Contract Service) to provide an additional service option for customers that have low load factor operations. Enbridge explained that, currently, a number of larger customers are not using Rate 100 service and instead are taking service under Rate 6. There are about 33 general service and two potential customers that would be candidates to choose the revised Rate 100 service.

Enbridge also proposed to lower the minimum load factor for service provided under Rate 110 (Large Volume Load Factor Service) from 50% to 40%. The lower load factor requirement would facilitate continuity of service for Rate 110 customers who undertake energy conservation and energy efficiency initiatives (because their load factor has declined as result of the energy conservation and efficiency initiatives). It would also provide an option for general service customers with load factors greater than 40% to take service under Rate 110.

Board Findings

IGUA and BOMA supported the changes. The Board accepts Enbridge's evidence that the changes will improve the service offerings under these rates and therefore accepts the proposed changes.

Rate 332: Parkway to Albion (GTA related)

Rate 332 (Parkway to Albion Transportation Service) relates to Segment A of the GTA Project and would be applicable to the proposed transportation service agreement with Rate 332 shippers for transportation service on Segment A. The Rate 332 monthly charge is designed to recover the shipper's portion of the Segment A costs. In the GTA leave to construct proceeding, Enbridge proposed that the derivation of the annual revenue requirement and determination of Rate 332 monthly charge be considered on a stand-alone basis. The revenue requirement for Segment A would be based on a cost-of-service methodology and include costs for administration, operation, maintenance, depreciation, cost of debt, return on equity, and municipal and income taxes. In accordance with the Board's GTA Decision and Order (EB-2012-0451), which approved the methodology, 60% of the annual revenue requirement for Segment A will be recovered from shippers through a contract demand charge for contracted capacity. The actual Rate 332 is being set in this proceeding.

Board Findings

The Board accepts Enbridge's proposal.

BOMA argued that this issue should be moved to the 2013 ESM or 2015 rate proceeding. BOMA noted that the incremental capital cost associated with this service has increased and argued that there was a lack of detailed evidence and examination of the rate in this case, including how the shipper's share of costs is to be determined or whether a range rate will be used as originally proposed. Enbridge responded that BOMA was incorrect. What BOMA referred to as a range rate in fact is a range of potential rates which the company provided as information for shippers. In Enbridge's view, the evidence is clear that Rate 332 will be allocated 60% of the fully allocated revenue requirement for Segment A of the GTA project and this will be recovered using a demand charge.

The Board agrees that BOMA's assessment is incorrect. The derivation of the rate was initially presented in the leave to construct proceeding, and the evidence in the current proceeding is consistent with the previous evidence. In addition, the evidence is clear that Rate 332 will bear 60% of the fully allocated costs of Segment A.

APPrO had no comments on Rate 332, but recommended that Enbridge proactively develop daily interruptible service. Enbridge responded that no changes would be needed to be able to offer Transactional Services and if the opportunity to offer further services arises then the company will bring forward a proposal during the IR period. The Board is satisfied with Enbridge's response to APPrO's suggestion.

Rate Handbook Changes – change to Terms & Conditions for Large Customers

Enbridge proposed an additional provision to its Terms and Conditions of service in its Rate Handbook which would require Enbridge and its largest customers to meet once annually to review the customer's expected consumption and to confirm the emergency contact information that Enbridge has on file for the customer.

APPrO noted the commercially sensitive nature of the information being requested and submitted that it was not clear how Enbridge would use the information. APPrO submitted that the provision should not apply to contract customers because the provision of information should be negotiated between the parties and put into the contract. Enbridge responded that the information is needed from a safety and reliability perspective whether or not the customer is buying gas from the company because of the size of the customers and the potential impact on system. The company noted that annual contract customers are already complying with the proposed provisions, and for customers with longer term contracts (Rate 125) the intent of the provision is fulfilled through the "annual consumption forecast". Enbridge concluded that the proposal effectively only impacts General Service customers.

Board Findings

The Board concludes that there is no adverse impact on customers arising from the proposal. The Board finds that Enbridge has justified the need for the information and has provided adequate assurance that commercially sensitive information will be treated appropriately. The Board notes that in all material respects large contract customers are already operating under the proposed provisions.

Reporting

This section summarizes the various reporting requirements which were either proposed by Enbridge, or agreed to by Enbridge as a result of requests from intervenors:

- Enbridge's plan includes a proposed performance measurement framework which consists of an Annual Productivity Report to be filed as part of the ESM application, and a Performance Metrics Benchmarking Report to be filed at the end of the Custom IR term.

- Enbridge agreed to provide the same information as Union Gas agreed to provide in section 12.1 of the Union Gas settlement. Enbridge indicated that it will provide the information as part of its ESM proceedings, or at the end of the Custom IR term. Enbridge indicated that it would not provide the items from the Union Gas list which are not relevant to Enbridge, such as audited statements for utility operations which have not been prepared for Enbridge.

- Enbridge agreed to annually provide intervenors with its Reporting and Record Keeping Requirements "RRR" filings that are relevant to the regulated utility such as SQR's and affiliate transaction reporting. Union Gas has also agreed to provide its annual RRR filing to intervenors,

- Enbridge agreed to hold annual stakeholder meetings during the Custom IR term, similar to what Union Gas agreed to in its Settlement Agreement. Enbridge proposed an annual funded stakeholder meeting, including funding for reasonable preparation for the meeting and follow up comments from the meeting, after the public release of year-end financial results but prior to Enbridge's filing its annual non-commodity deferral accounts disposition application (March/April timeframe).

  At the annual stakeholder meeting, Enbridge proposes to:

  1. review previous year's financial results (i.e. earnings, capital spending) and other key operating parameters (i.e. SQR performance) for the most recently completed year;
  2. present and explain market conditions and expected changes/trends and the impact these may have on the regulated operations;
  3. present and review the current gas supply plan memorandum; and

4. present results of any customer surveys undertaken during the year.

Enbridge proposes to file all information resulting from this annual meeting with the Board and ensure it is available to any party not able to attend.

- For Gas Supply reporting, Enbridge agreed within the October 2013 Settlement Agreement related to Enbridge's 2014 Gas Supply Plan to provide monthly reporting related to the use of new FT services acquired from TCPL and associated UDC. Subsequently, in response to discussions with FRPO, Enbridge agreed to provide further items within the monthly reporting. Then, during the examination of the gas supply panel at the hearing, Enbridge agreed to provide one additional item (monthly storage targets).

  In is submission, FRPO requested further monthly reporting be added to the items noted above. Specifically, FRPO requested that Enbridge provide monthly reporting on the amount of FT capacity that is assigned to third parties through a UDC-related "outright release" (as differentiated from a capacity release exchange transaction), and the revenue generated from such transactions.
  Enbridge responded that it is prepared to provide this additional gas supply reporting, and began doing so within its latest monthly report, which was filed with the Board on April 30, 2014.

  FRPO also requested that Enbridge prepare an annual Gas Supply Plan memorandum consistent with what is being prepared and provided by Union Gas. The Gas Supply Plan memorandum would include the following:

  1. a summary of the current natural gas market situation;
  2. the results of the design day demand forecast with a discussion of the underpinning assumptions;
  3. an overview of the current gas supply portfolio;
  4. the identification of near term portfolio decisions and a description of how the Enbridge strategy for the specific portfolio decision conforms to the gas supply planning principles; and
  5. a summary of major upstream pipeline regulatory filings and/or recent regulatory orders (e.g. RH-003-2011); physical infrastructure projects that will likely impact Enbridge; and the implications associated with gas supply basins.

Enbridge responded that it is prepared to prepare the requested Gas Supply Plan memorandum on an annual basis. The contents of the memorandum would be consistent with what is set out within the April 2014 Union Gas Supply Plan memorandum that was presented at the Union Gas Stakeholder Meeting. Enbridge proposed to include the Gas Supply Plan memorandum as part of the materials to be provided to stakeholders for the annual stakeholder meeting.

- For capital expenditures, Enbridge agreed to provide whatever annual reporting on actual amounts spent that is required by the Board. Enbridge acknowledged that this may go beyond the reporting that is already included within ESM applications, to identify differences between annual spending and the amounts that were approved and included in Allowed Revenues. This reporting would allow the Board, according to Enbridge, to assess whether the company's actual spending is consistent with the approved Custom IR plan.

Board Findings

The Board accepts Enbridge's reporting commitments which are outlined above. In addition, as stated in the Board Findings sections associated with Capital Expenditures, the Board will require Enbridge to report, on an annual basis, on the following aspects:

- Progress of GTA and WAMS projects, including actual cost and schedule versus forecast
- Status and expenditures for the system integrity program
- Progress in efforts to improve the asset management plan
- Status of work programs comprising the productivity savings
- Progress on the benchmarking study (capital and O&M), including stakeholder consultation and independent, third-party involvement.

The Board directs Enbridge to compile a comprehensive list of all its reporting commitments for inclusion in the Draft Rate Order.

Implementation

On November 28, 2013, the Board declared Enbridge's existing rates to be interim effective January 1, 2014, pending the final resolution of the matters in this proceeding. No orders have superseded the November 28, 2013 Interim Rate Order and therefore the rates remain interim.

2014 Rates

The Board must determine when the new 2014 rates should be implemented and the effective date of the new 2014 rates. Enbridge proposed that the new 2014 rates be made effective January 1, 2014 and be implemented in conjunction with the October 1, 2014 QRAM. Under Enbridge's proposal, there would be two rate riders:

- Rider D would credit ratepayers with the 2014 portion of any SRC reserve that is to be refunded. Rider D would apply to a customer's monthly consumption and would appear as a separate line item on the monthly bill.
- Rider E would credit ratepayers with the difference in revenue between interim and final 2014 rates for the period from January 1, 2014 to the date when final rates are implemented.

If Enbridge's application had been approved as proposed, an average residential ratepayer would have seen a rate decrease of 1.7% or $9 in 2014 along with an additional credit of $27 for the SRC refund, followed by rate increases ranging from 2.1% to 4.6% in later years of the Custom IR. As a result of this decision, the Board expects that the reduction in 2014 will be the same or slightly larger and that the rate increases in 2015 and beyond will be somewhat lower than proposed by Enbridge. Enbridge will be required to calculate the new impact levels and present them as part of the Draft Rate Order process.

No party opposed setting an effective date of January 1, 2014, because it is widely expected that the new rates will be lower than the interim rates, which will result in a ratepayer credit in 2014.

Energy Probe submitted that the 2014 rates should be implemented in the first month after they are approved, rather than waiting for a QRAM application. Other parties noted the recent gas commodity price increases and submitted that 2014 rates should not be delayed, so as to pass on the lower rates as soon as possible. Enbridge responded that aligning implementation with the October 1, 2014 QRAM would reduce confusion which might otherwise arise from having a rate change billing outside of the established quarterly rate change mechanism. However, Enbridge noted that if the October 1 date could not be met, then implementation should be done before the January 1, 2015 QRAM, on either November 1 or December 1.

Board Findings

The Board finds that the new 2014 rates should be made effective January 1, 2014 and will be implemented with the October 1, 2014 QRAM. Normally, the Board would be reluctant to implement rates with an effective date so far back. However, the timing is due in part to the nature and timing of the application, and the new rates will be lower than the current interim rates. Therefore, the Board finds that it is appropriate in these circumstances to set an effective date of January 1, 2104.

The Board expects that the rate order process can be completed to allow for implementation along with the October 1 QRAM. CME proposed that a technical conference be held following the release of the decision to enable interested parties to address any matters pertaining to implementation. The Board will provide for a technical conference to be held shortly after the Draft Rate Order is submitted in order for Enbridge to explain how it has derived the new 2014 rates from the Board decision.

2015-2018 Rates

The Custom IR proposal provides for an annual rate adjustment process. Enbridge requested that the Board set “Allowed Revenues” for each year from 2015 through 2018 as part of the current approval process. Revenue requirements for 2014 are established separately as a final amount and do not require an “Allowed Revenue” step. The Allowed Revenue amounts would serve as a placeholder for rates, and would be updated annually with more current forecasts of specific elements (described below) prior to the start of each year of the plan.

Board Findings

The Board will accept Enbridge’s proposal for setting rates in 2015, 2016, 2017 and 2018. While most elements of Allowed Revenue have been determined in this proceeding, certain specific elements will have a placeholder amount set at this time and then be updated in advance of the start of each rate year. The elements to be updated include:

- Volumes (including customer additions and a probability weighted large volume customer forecast).
- Gas-cost related items
- Customer care/CIS costs, in accordance with the Board-approved EB-2011-0226 Settlement Agreement
- DSM
- Pension and OPEB costs
- Return on equity (set using the Board's policy)
- Cost of debt

Enbridge is directed to include a complete list of the elements which will be updated annually as a result of its proposal and this decision. The list shall be included as part of the Draft Rate Order.

Draft Rate Order

The Board directs Enbridge to file a Draft Rate Order and a Draft Accounting Order which together will comprehensively reflect the Board's findings in this decision and allow the decision to be implemented as soon as possible. The Board expects that the Draft Rate Order and Draft Accounting Order will contain sufficient detail and supporting documentation to allow the Board and parties to verify that the Board's findings are properly addressed. The Draft Accounting Order will address the Deferral and Variance Accounts. The Board will provide for a technical conference and will also allow interested parties to file submissions on the Draft Rate Order and Draft Accounting Order. Enbridge will have an opportunity to reply. The Board's expectation is that its Final Rate Order and Accounting Order will be available for an October 1, 2014 implementation timeframe.

The process for the filing of claims for cost awards will be set out after the Draft Rate Order process is complete.

THE BOARD ORDERS THAT:

1. Enbridge shall file with the Board and serve on the other parties a Draft Rate Order and Draft Accounting Order by **Thursday July 31, 2014**.

2. A Technical Conference involving Board staff, intervenors and Enbridge will be convened on **Wednesday August 6, 2014 at 9:30 a.m.** The Technical Conference

will be held in the Board's hearing room at 2300 Yonge Street, 25th Floor, Toronto. The Technical Conference will pertain to the Draft Rate Order and Draft Accounting Order.

3. Parties wishing to make submissions on the Draft Rate Order or Draft Accounting Order shall file such submissions with the Board and serve a copy on all parties by **Thursday August 14, 2014**.

4. Enbridge may file a reply by **Tuesday August 19, 2014**.

DATED at Toronto July 17, 2014

ONTARIO ENERGY BOARD

Original Signed By

____
Paula Conboy
Presiding Member

Original Signed By

____
Cynthia Chaplin
Member

Original Signed By

____
Emad Elsayed
Member