ENBRIDGE GAS INC.

First Tracks Consulting Service In. Answers to
Interrogatories from Environmental Defence (ED)

Exhibit I.5.EGI.ED.1

Reference: EGI Reply Evidence, Page 4

Preamble: The First Tracks report states:

> "I recommend that the OEB address three key questions before moving forward with amortization:
>
> o What level of budget increases are desired?"

Question(s):

(a) Does First Tracks believe the OEB should set the budget first or set the desired levels first?
(b) Does First Tracks believe the OEB could decide at a high-level that significant budget increases are required and that amortization is therefore appropriate without specifying the exact level of budget increase?

Response:

a) The "level" referred to in the quotation is the level of budget increase.

b) Yes. It is my understanding that the OEB has broad authority to authorize or require amortization, regardless of budget levels. That said, it is also my understanding that the OEB will establish a budget level in this proceeding.

Exhibit I.5.EGI.ED.2

Reference: EGI Reply Evidence, Page 10

Preamble: The First Tracks report states:

> With amortization, DSM costs are treated as a regulatory asset instead of an expense. Amortization cost recovery uses an approach consistent with the example provided earlier for pipeline and power plant assets, with one minor difference: with regulatory assets, investment costs are recovered through amortization, rather than the depreciation used for physical assets. Otherwise,

the calculations and cash flows are identical to the example provided earlier for pipelines and power plants.

Question(s):

(a) Does First Tracks agree that it is possible to separate the amortization mechanism from the incentive/return mechanism (e.g., have no equity investment and incentives paid separately)? Please explain.
(b) If the amortization cost of capital were separated from the incentive/return mechanism, does First Tracks agree that it would be appropriate to use the short-term debt rate to amortize these costs? Please explain.
(c) If the amortization cost of capital were separated from the incentive/return mechanism, what does First Tracks believe would be the least expensive source of debt financing? Please consider different debt instruments available to utilities as well as the possibility of accessing capital at rates available to the provincial government.

Response:

(a) My position is that, if the OEB decides to amortize DSM expenditures, the amortization mechanism should be separated from the performance incentive mechanism, but that the performance incentive should be provided in addition to the equity component of the cost of capital required to reimburse shareholders for the capital needed to finance amortization.

With this approach, Enbridge will receive:

- Fair compensation for all Enbridge investors, including debt and equity investors, for the capital they provide to fund the amortization. This is not an incentive payment to Enbridge equity shareholders; it is simply a repayment of the actual costs of capital required to carry the investment over the amortization term.
- A separate performance incentive paid to shareholders over and above the earnings required for amortization. This performance incentive will be structured the same, regardless of whether DSM expenditures are expensed or amortized. This provides Enbridge the incentive to:
  - Prioritize DSM over other investment opportunities if expenditures are amortized, by ensuring that DSM investments earn a premium rate of return compared to other investment opportunities;
  - Prioritize DSM over other non-capital management activities if expenditures are expensed, by providing earnings, where other non-capital activities provide no direct profit driver;
  - Improve program performance, by increasing the incentive payment along with increases in program performance.

If the OEB decides not to amortize DSM expenditures, then Enbridge will continue to receive approximately the same level of earnings from the shareholder incentive that it received over the 2015-2022 plan period. If the OEB does decide to amortize DSM expenditures, then Enbridge will receive earnings—over and above its actual cost to fund the amortization—that are approximately the same as the earnings received over the 2015-2022 plan period. That is, regardless of the cost recovery method, the OEB will provide Enbridge with the same incentive to prioritize DSM over other activities.

(b) No. See response to part (a).

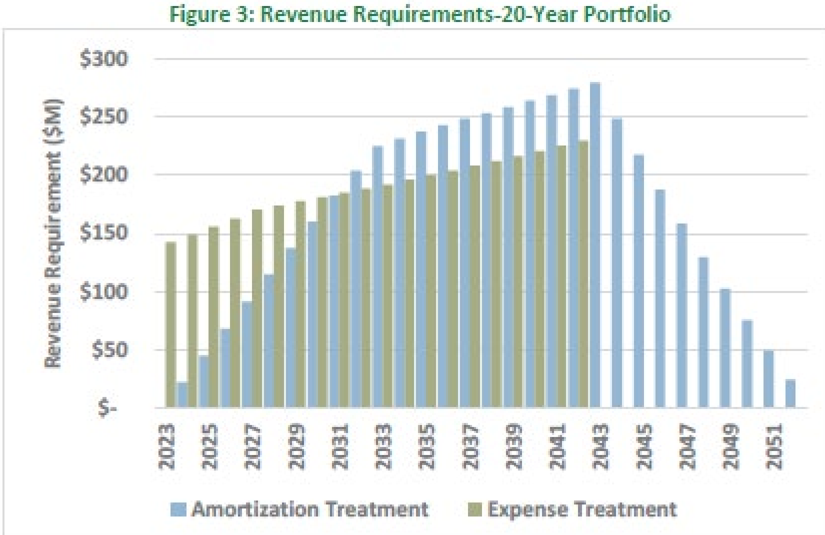
(c) See response to part (a).

Exhibit I.5.EGI.ED.3

Reference: EGI Reply Evidence, Page 12

Preamble: The First Tracks report includes the following figure:

Figure 3: Revenue Requirements-20-Year Portfolio



Question(s):

(a) Please reproduce Figure 3 with the cost of capital for amortization being at the deemed short-term debt rate.[1]

[1] https://www.oeb.ca/regulatory-rules-and-documents/rules-codes-and-requirements/cost-capital-parameter-updates

(b) Please reproduce Figure 3 with the cost of capital for amortization being 1.9%.[2]
(c) What discount rate is used in Figure 3?
(d) Please confirm that the appropriate discount rate is not necessarily equal to the cost of capital.

Response:

(a) I have not performed the calculations described. I provided a copy of the spreadsheet tool used to develop Figure 3 in response to Exhibit I.7.OEB Staff.2, as well as similar tools that incorporate tax calculations. Environmental Defence may perform this scenario on its own through the use of these tools.

(b) See response to part (a).

(c) There is no discount rate used in Figure 3. All values presented are in nominal dollars.

(d) Not confirmed. For the purpose of my report, which shows the dynamics of utility revenue requirements and cash flows—especially how amortization calculations create utility revenue requirement collections that offset initial utility investments in present value terms—the appropriate discount rate is equal to the utility's cost of capital.

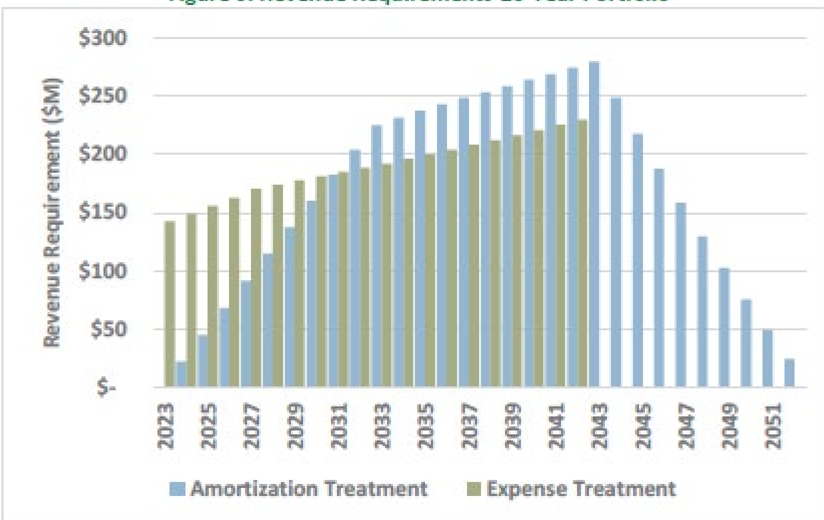
Exhibit I.5.EGI.ED.4

Reference: EGI Reply Evidence, Page 12

Preamble: The First Tracks report includes the following figure:

[2] https://www.oeb.ca/regulatory-rules-and-documents/rules-codes-and-requirements/cost-capital-parameter-updates

Figure 3: Revenue Requirements-20-Year Portfolio



Question(s):

(a) Please reproduce Figure 3 with the cost of capital for amortization being at 1.9% and the discount rate being 6.08%.[3]
(b) Please confirm that the following document at page 158 describes the Ontario government's average cost of borrowing as being 1.9%: Government of Ontario, *2021 Ontario Economic Outlook and Fiscal Review*, https://budget.ontario.ca/2021/fallstatement/pdf/2021-fall-statement-en.pdf.
(c) Please confirm that the discount rate used by Enbridge for its DSM plan is 6.08%.

Response:

(a) See response to Exhibit I.5.EGI.ED.3 Part a.

(b) Confirmed.

(c) Enbridge Gas Response:

Confirmed. This was also previously confirmed in interrogatory response at Exhibit I.13.EGI.EP.21 Part c.

[3] https://www.oeb.ca/regulatory-rules-and-documents/rules-codes-and-requirements/cost-capital-parameter-updates

Exhibit I.5.EGI.ED.5

Reference: EGI Reply Evidence, Page 14

Preamble: The First Tracks report states:

> Over the full cost recovery period, the present value of revenue requirements is identical for both amortization and expense treatment (when using the utility's cost of capital as the discount rate). Under both treatments, the present value of revenue requirements exactly equals the present value of DSM expenditures. In other words, the discounted cash flow for both treatments equal zero; because revenue exactly equal costs with expense treatment, and because the utility earns exactly it's authorized cost of capital with amortization treatment.

Question(s):

(a) Please confirm that the present value of amortization treatment versus expense treatment is positive (i.e., net savings) if the cost of borrowing for amortization is less than the discount rate, and vice versa. Please explain.
(b) Please confirm that this is just as true if the spending were on infrastructure as in the case of DSM. Please explain.

Response:

(a) Confirmed. As I stated on page 32 of my report: "As a mathematical exercise, I don't disagree with Optimal's conclusion that customers with discount rates higher than the cost of capital applied in the amortization calculations will accrue savings in present value terms. However, I disagree with the broader policy conclusion that the use of customer discount rates represents a reasonable framework for evaluating DSM in Ontario."

(b) Confirmed.

Exhibit I.5.EGI.ED.6

Reference: EGI Reply Evidence, Page 5

Preamble: The First Tracks report states:

> "If the OEB does approve substantial DSM budget increases, I recommend that the OEB:
>
> o Phase in increases over several years; other jurisdictions have phased in large budget increases over three to four years."

Question(s):

(a) The First Tracks report refers to ramp-up periods in other jurisdictions. Please provide some examples of ramping up that has occurred in other jurisdictions in terms of percent increases per year (by m3 and budget if possible).
(b) The First Tracks report refers to ramp-up periods in other jurisdictions. Please describe one to three jurisdictions that have successfully ramped up the fastest.

Response:

(a) Please see response to Exhibit I.7.EGI.STAFF.3

(b) Please see response to Exhibit I.7.EGI.STAFF.3

Exhibit I.5.EGI.ED.7

Reference: EGI Reply Evidence, Page 23

Preamble: The First Tracks report states:

> By phasing in budget increases, the OEB will allow Enbridge and its implementation partners—the trade allies and implementation contractors responsible for deploying the higher budgets—a chance to ramp up the required infrastructure. At $142 million, Enbridge already deploys one of the largest gas DSM portfolios in North America, and so substantial budget increases will likely require structural market changes to accommodate more funding.

Question(s):

(a) Please substantiate the above statements by comparing Enbridge to the 10 largest DSM portfolios in North America measured proportional to the size of the market (e.g., ratio of DSM budget to total gas consumption).

Response:

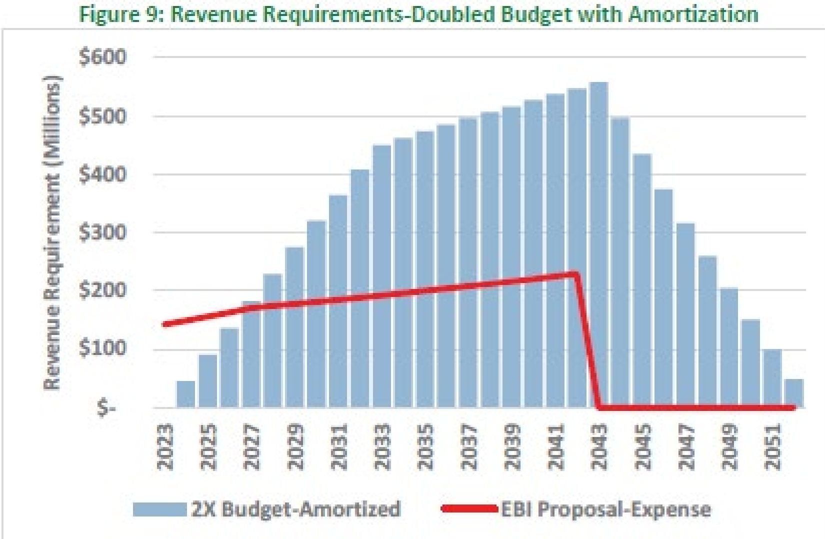
(a) My statement referred to the absolute level of funding, not the relative level compared to revenues or total gas consumption. While I have not performed a comprehensive assessment of natural gas budgets in North America (and it can be difficult to segregate natural gas budgets for utilities providing combined electric and gas programs), I believe that Enbridge's budget is larger than all North American portfolios with the exceptions of Pacific Gas & Electric in California and the Massachusetts utilities.

Exhibit I.5.EGI.ED.8

Reference: EGI Reply Evidence, Page 24

Preamble: The First Tracks report states:

Figure 9: Revenue Requirements-Doubled Budget with Amortization



> If the OEB wishes to continue meeting its historic guidance on rate impacts, budget increases would need to be far lower than this 2X adjustment. Figure 10 shows more modest increases of 20%, with amortization calculated at Enbridge's WACC and various amortization terms. These scenarios track closer to the OEB's historic rate guidance, with higher savings in the short term and lower increases in the long term.

Question(s):

(a) Please confirm the percent by which Enbridge could increase the budget it has proposed while remaining within the $2 residential rate impact cap that previously applied in Ontario.
(b) Please reproduce Figure 9 but with the monthly average residential rate impact as the vertical axis instead of the revenue requirement. Please provide all calculations.
(c) Please reproduce Figure 9 with a discount rate of 4% and cost of borrowing for amortization of 2%. Please provide all calculations.

Response:

(a) As shown in figures 9 and 10 of my report, and in the discussion on pages 24-25 of the report, the budget increases that could be accommodated within the OEB's historic rate guidance—in the short term—will vary depending upon the amortization term and cost of capital used to calculate amortized revenue requirements. In the long term, revenue requirements from amortized DSM expenditures will exceed the OEB's historic rate guidance.

(b) I have not performed that calculation.

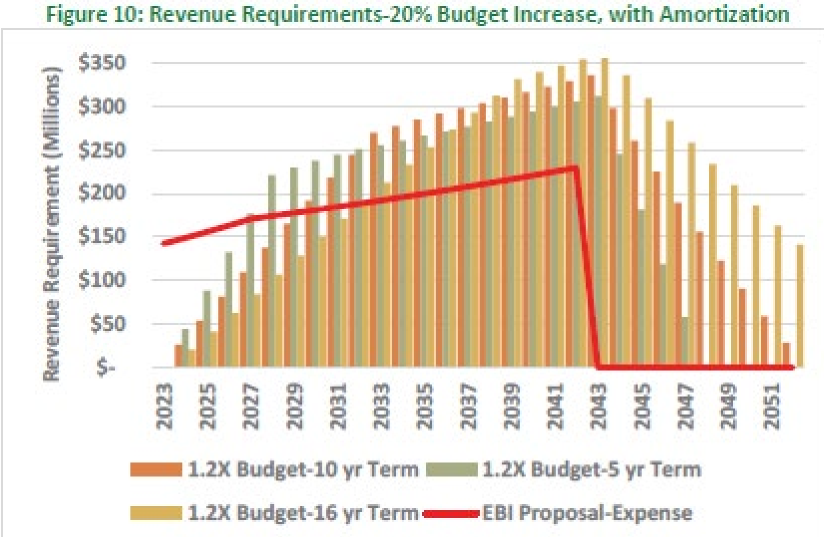
(c) See response at Exhibit I.5.EGI.ED.3 Part a.

<u>Exhibit I.5.EGI.ED.9</u>

<u>Reference:</u> EGI Reply Evidence, Page 25

<u>Preamble:</u> The First Tracks report states:

Figure 10: Revenue Requirements-20% Budget Increase, with Amortization



<u>Question(s):</u>

(a) Please reproduce Figure 10 but with the monthly average residential rate impact as the vertical axis instead of the revenue requirement. Please provide all calculations.
(b) Please reproduce Figure 10 with a discount rate of 4% and cost of borrowing for amortization of 2%. Please provide all calculations.

<u>Response:</u>

(a) I have not performed that calculation.

(b) See response at Exhibit I.5.EGI.ED.3 Part a.

Exhibit I.5.EGI.ED.10

Reference: EGI Reply Evidence, Page 30

Preamble: The First Tracks report states:

> I don't see how Enbridge could raise a billion dollars by promising investors only 4% returns.27 Those investors would instead shift their funds to other gas utilities earning their full authorized costs of capital. If Optimal believes that Enbridge could somehow finance its DSM funding solely through bond investors, I don't understand how this could work in Ontario. It is my understanding that the OEB directs Enbridge to maintain a capital structure including 36% equity. If Optimal thinks Enbridge could somehow dedicate a bond raise to support the DSM portfolio, this would have the impact of skewing the capital structure, and it would force Enbridge to increase equity to maintain the OEB's guidance on capital structure.

Question(s):

(a) Is there any reason why arrangements could not be made with the Government of Ontario to obtain access to inexpensive government debt to finance the cost of DSM? In other words, is there any reason why the Government of Ontario could not borrow at the 10-year government bond rate and lend those funds to Enbridge for DSM purposes at or close to its own cost of borrowing?

Response:

I am not an expert regarding whether the Government of Ontario could or would pass the legislation required to fund Enbridge DSM activities with government debt, or how those transactions would be structured. However, I do not believe this question is relevant to the OEB's decision in this proceeding, because there is no proposal from the Government of Ontario that would actually accomplish this. In this proceeding the OEB must set budgets, cost recovery policies, and other determinations regarding Enbridge's proposed DSM Plan based on the evidentiary record.

Exhibit I.5.EGI.ED.11

Reference: EGI Reply Evidence, Page 49 & 57

Preamble: The First Tracks report states on page 49:

> I agree with EFG that, if the OEB does substantially increase portfolio budgets and savings goals—either in the current case, at the Mid-Point Assessment, or in the next plan cycle—that maximum incentive payments should also increase. In

> my view, Enbridge's profit incentive should be commensurate with the financial and management resources required to successfully execute the approved portfolio.

The First Tracks report states on page 57:

> 3.5.1.2. Maximum Performance Incentive Payments
>
> Increase performance incentive pool if budgets or savings goals increase substantially, as recommended by Optimal and EFG.

Question(s):

(a) If the maximum incentive pool is to grow, should it be pegged to: (a) first year m3 savings, (b) forecast lifetime m3 savings, (c) budget, or (d) net TRC benefits? Please discuss the pros and cons of each (perhaps in a table).
(b) Does First Tracks agree that pegging the incentive pool to the DSM budget would provide less incentive to propose a plan with better outcomes in comparison to pegging the pool to the m3 savings or net TRC benefits?
(c) Please express the current incentive pool for 2023 as (i) a ratio of the maximum incentive pool ($) to the forecast lifetime m3 saving (m3) and (ii) a ratio of the maximum incentive pool ($) to the net TRC benefits.
(d) Does First Tracks agree that it would be ideal to peg the incentive pool to the plan outcomes (i.e., m3 savings to $ TRC net benefits) *before* Enbridge finalizes its DSM plan so that the peg will incentivize Enbridge to prepare a plan that results in the better outcomes?
(e) If the OEB were to peg the incentive pool to the m3 of lifetime savings, what would an appropriate ratio be between the incentive pool and the m3 of lifetime savings? Please provide a recommended figure and a range or reasonableness.
(f) If the OEB were to peg the incentive pool to the net TRC benefits ($), what would an appropriate ratio be between the incentive pool and the net TRC benefits? Please provide a recommended figure and a range or reasonableness.

Response:

(a) The appropriate scaler for the incentive pool would depend on the OEB's final determination regarding the performance incentive mechanism. If the OEB accepts my compromise proposal, then annual savings, which is the key driver for the large majority of incentive payments, would be an appropriate scaler.

(b) Yes

(c) Enbridge Response:

i)

Proposed incentive pool:	**$19,890,000** Note: in 2023, only annual components of the shareholder incentive will be available to Enbridge Gas, the long-term components of the shareholder incentive will only be available in 2024 and 2027 (Updated Application Exhibit D, Tab 1, Schedule 2, Page 3 of 16)
Forecast lifetime m3:	**1,749,703,196 cumulative cubic metres** (Exhibit I.5.EGI.GEC.5)
Ratio:	$19,890,000 : 1,749,703,196 ccm

ii)

Proposed incentive pool:	**$19,890,000** Note: in 2023, only annual components of the shareholder incentive will be available to Enbridge Gas, the long-term components of the shareholder incentive will only be available in 2024 and 2027 (Updated Application Exhibit D, Tab 1, Schedule 2, Page 3 of 16)
Forecast net TRC benefit:	**$372,260,124** Forecasted 2023 Net Benefits ($) Result (Updated Application, Exhibit D, Tab 1, Schedule 2, Page 13 of 16)
Ratio:	$19,890,000 : $372,260,124

(d) I believe that this approach might work in future proceedings, where the OEB provides policy guidance in advance regarding the size of the incentive pool relative to the appropriate key metrics. I don’t understand how this approach can work in this proceeding, where Enbridge has already proposed a plan.

(e) I have not performed this analysis.

(f) I have not performed this analysis.