2016 EARNINGS SHARING AMOUNT AND DETERMINATION PROCESS

1. The 2016 Earnings Sharing amount included within Enbridge Gas Distribution Inc.'s ("Enbridge", or "the Company") Fiscal 2016 year-end audited statements was $3.2 million, which was slightly lower than the amount being requested for approval and clearance within this application of $3.4 million. In order to meet year end timing obligations, estimates for elements impacting the accrual are sometimes required in lieu of complete or detailed analyses along with the rounding of various actual amounts into millions of dollars for regulatory presentation. Following the year end close process, however, completion of analyses are performed for elements where estimates were used along with rounding finalizations, in order to ensure the earnings sharing amount is accurate. If required and appropriate, an adjustment is made to the earnings sharing results, which ultimately is reflected in following year financial statements. In certain other instances, new information becomes available which requires the earnings sharing amount to be recalculated.

2. The process followed is the same as that which was followed for earnings sharing amounts calculated for 2014 and 2015, and during the 2008 through 2012 incentive regulation term. For 2016, the year-end earnings sharing calculation did not properly consider the allocation of $5.6 million of base pressure gas to unregulated storage operations (resulting from the use of fully allocated costs for base pressure gas), as was agreed to as part of the Board Approved EB-2015-0114 (2016 Rate Adjustment proceeding) Settlement Agreement. Updating the earnings sharing calculation to reflect the approved allocation resulted in a $5.6 million rate base reduction, which creates a $0.4 million increase in the gross sufficiency to be

shared with rate payers, and a corresponding $0.2 million increase to the earnings sharing amount.

3. The amounts for each of the cost elements of utility rate base, utility income and taxes, and the utility capital structure components, which were used in the calculation of the earnings sharing amount, are summarized within Exhibit B, Tab 1, Schedule 2.

4. The earnings sharing amount was determined in accordance with the following prescribed methodology as identified within the EB-2012-0459 Board Decision, dated July 17, 2014, at pages 13 through 15, and within the pre-filed evidence at Exhibit A2, Tab 7, Schedule 1;
   - if in any calendar year during the customized incentive regulation term, Enbridge's actual utility ROE, calculated on a weather normalized basis, is more than the allowed ROE included in that year's rates (updated annually by the application of the Board's ROE Formula), then the resultant amount shall be shared equally (ie., 50 / 50) between Enbridge and its ratepayers;
   - for the purposes of the ESM, Enbridge shall calculate its earnings using the regulatory rules prescribed by the Board, from time to time, and shall not make any material changes in accounting practices that have the effect of reducing utility earnings;
   - all revenues that would otherwise be included in revenue in a cost of service application shall be included in revenues in the calculation of the earnings calculation and only those expenses (whether operating or capital) that would be otherwise allowable as deductions from earnings in a cost of service application, shall be included in the earnings calculation.

5. In addition, the following are examples of shareholder incentives and other amounts which are outside the ambit of the ESM: amounts related to Demand Side Management incentives, amounts related to Transactional Services incentives, and amounts related to Open Bill program incentives.

6. As shown within the summary of return on equity and earnings sharing determination, Exhibit B, Tab 1, Schedule 2, the Company has calculated earnings for sharing in two ways for confirmation purposes.

7. In part A) of the summary, a return on rate base method is shown, while in part B), a return on equity from a deemed equity embedded within rate base perspective is shown. Column 2 within the exhibit provides references indicating where additional evidence in support of the determination of the amounts in the summary can be found. Column 3 contains results shown in millions of dollars, or percentages.

<u>Part A)</u>

8. The level of utility income, $377.3 million (Line 17) divided by the level of utility rate base, $5,909.0 million (Line 22) generates a utility return on rate base of 6.385% (Line 23).

9. When compared to the Company's required rate of return of 6.301% (Line 24), as determined within the capital structure required in support of the determined rate base amount, there is a resulting sufficiency of 0.084% (Line 25) on total rate base.

10. As shown in Lines 26 through 28, the sufficiency of 0.084% multiplied by the rate base of $5,909.0 million, produces a net over earnings or sufficiency of $4.97 million which from a pre-tax perspective, ($4.97 million divided by the reciprocal, 73.5%, of

the corporate tax rate which is 26.5%) shows a $6.76 million total amount of over earnings to be shared equally between ratepayers and the Company. Column 2 provides supporting evidence references.

<u>Part B) (Confirming the Calculated Earnings Sharing)</u>

11. Net utility income applicable to common equity is first determined.

12. The $394.6 million (Line 31) of utility income before income tax, less utility taxes of $17.3 million (Line 36), produces the $377.3 million of utility income used in part A) above (at Line 17).

13. In order to determine utility net income applicable to a deemed common equity percentage within rate base, all long term debt, short term debt and preference share costs must also be reduced against the part A) $377.3 million utility income.

14. These reductions are shown at Lines 32, 33 and 34 which along with the utility income tax reduction already mentioned and shown at Line 36, results in a net income applicable to common equity of $200.5 million, shown at Line 37.

15. The $200.5 million, divided by the deemed common equity level of $2,127.2 million (Line 38, calculated as 36% of the $5,909.0 million rate base) produces a return on equity of 9.423% (Line 40). When comparing the 9.423% achieved return on equity to the threshold ROE percentage of 9.19% (Line 39), which is the Board approved formula return on equity for 2016, there is a sufficiency in ROE of 0.233% (Line 41).

16. The 0.233% multiplied by the common equity level of $2,127.2 million (Line 38) produces a net over earnings or sufficiency of $4.97 million which from a pre-tax

perspective ($4.97 million divided by the reciprocal, 73.5%, of the corporate tax rate), shows a $6.76 million total amount of over earnings to be shared equally between ratepayers and the Company. Column 2 provides supporting evidence references.

Process Description

17. The calculation of utility earnings and any sharing requirement starts with financial results contained within the Enbridge Ontario corporate trial balance.

18. From there, in order to calculate the Ontario utility rate base, income, and capital structure results, and supporting evidence exhibits, various adjustments, regroupings or eliminations are required. This is accomplished by following and applying regulatory rules as prescribed by the Board and the standards associated with cost of service rate related accounting processes. Examples are:
    - determination of rate base amounts using the average of monthly averages value concept,
    - elimination of corporate interest expense due to the treatment of interest expense as embedded in the capital structure balanced to rate base, and
    - elimination of corporate income taxes due to the determination of income taxes specific to utility results,

19. In addition, Enbridge has made the appropriate adjustments in relation to non-standard rate regulated items which the Board has either decided in the past, or are required in order to determine an appropriate utility return on equity. Examples are:
    - rate base disallowance from EBRO 473 and 479 Decisions (Mississauga Southern Link project amounts),
    - rate base disallowance from RP-2002-0133 (shared assets),

- exclusion of non-utility or unregulated activities,
- elimination of approved shareholder incentives.

20. As shown in the Column 2 references in the summary exhibit, supporting rate base information is found in Exhibit B, Tab 2, supporting revenue, volumes, customers and cost information is found in Exhibit B, Tabs 3 and 4, and supporting capital structure, required rate of return, utility income, and cost of capital information is found in Exhibit B, Tab 5.