

Written Direct Testimony of David B. Charleson and Lori A. Stickles

Q 1: Please state your names and positions.

A 1: My name is David Bryce Charleson. I am the General Manager of Enbridge Gas New Brunswick Inc., the general partner of Enbridge Gas New Brunswick Limited Partnership (“EGNB”). My Curriculum Vitae is attached as Exhibit A, Schedule 1.

My name is Lori Ann Stickles. I am the Manager, Financial Services for EGNB. My Curriculum Vitae is attached as Exhibit A, Schedule 2.

Q 2: What is the purpose of this pre-filed evidence?

A 2: On June 15, 2010, a procedure conference was held to establish the process for the review of EGNB’s 2009 Financial Results and Natural Gas Sales. As part of this procedure conference, the Board determined that a prospective review of EGNB’s 2011 revenue requirement would also be conducted as part of the review and that this proceeding would also serve to determine if the first “end of the Development Period test” has been satisfied. The schedule established at the procedure conference allows EGNB the opportunity to submit evidence related to the matters included in this review. This is EGNB’s evidence on these matters.

Q 3: Has EGNB already submitted evidence in relation to any of these matters?

A 3: On March 15, 2010, EGNB filed its Commodity Sales report for the fiscal year ended December 31, 2009 and on April 19, 2010 EGNB filed a revised version of its 2009 Regulatory Financial Statements. Both of these have been marked as exhibits in this proceeding.

Q 4: What matters are EGNB addressing in this evidence?

A 4: EGNB is submitting evidence in relation to four areas:

1. proposed adjustments to its cost allocation methodology;
2. comments on the report submitted by Mr. Butler;
3. the 2011 Budget; and
4. the end of the Development Period tests.

Cost Allocation Methodology

Q 5: What do the costs to be allocated to EGNB by the cost allocation methodology represent?

A 5: They represent costs allocated by Enbridge Inc. (“Enbridge”) for services and overheads that are not associated with any of the Affiliate Service Level Agreements (“SLAs”) that EGNB has in place. These costs reflect internal or external costs incurred by Enbridge that support several or all business units, but do not relate to one specific business unit, and therefore must be allocated on a basis that relates the cost to the cost driver. The costs have been allocated to EGNB through a fair, consistent and simple allocation process, in accordance with Enbridge’s Cost Allocation Methodology, which can be found in Exhibit A, Schedule 3.

Q 6: How have the costs allocated to EGNB historically been included in the revenue requirement?

A 6: Since 2004, such cost allocations have been included in EGNB's revenue requirement based on the review conducted by the Board's financial consultant, Mr. Easson, as part of the 2004 annual review process. Mr. Easson reviewed the costs allocated to EGNB by Enbridge based on its cost allocation methodology at that time and based on his judgment identified costs that he believed would be reasonably incurred if EGNB were a stand-alone business. In discussions with EGNB Management, Mr. Easson also indicated his belief that the annual amount by which these costs could increase should be limited. This review and discussion with Mr. Easson formed the basis on which EGNB has determined which of the allocated costs should be recoverable in rates since that time.

Q 7: How has this methodology affected EGNB's recovery of the allocated costs?

A 7: The continued use of Mr. Easson's assessment of the costs to be included in the revenue requirement has precluded EGNB from recovering an increasing amount of allocated costs that EGNB believes legitimately form part of the overall cost of operating its business and that customers have derived benefit from. In the 2004 review, when the methodology was first applied by Mr. Easson, \$353,176 of costs were excluded from the revenue requirement. Since that time, due to the limits that have been applied to increases, the amount excluded from regulation was \$1.0 million in 2008 and would be \$1.2 million in 2009. While this number has increased over the years, the amount excluded as a percentage of distribution revenue is much lower today than in 2004.

A summary of costs allocated to EGNB in 2009 can be found in Exhibit A, Schedule 4.

Q 8: What is EGNB's proposal regarding the treatment of the allocated costs?

A 8: EGNB believes that it should be allowed complete recovery of all costs allocated to it by Enbridge and has restated its 2009 Regulatory Financial Statements in Exhibit A, Schedule 5 to reflect this. A black-line of the statements showing the changes to the statements filed on April 19, 2010 can be found in Exhibit A, Schedule 6.

Q 9: What is the basis for EGNB suggesting that all Enbridge costs allocated to EGNB should be recoverable in rates?

A 9: In Mr. Easson's 2004 annual review, he assessed the costs from Enbridge on a line item basis in terms of what a stand-alone business may reasonably incur. This assessment failed however to recognize the overall value that EGNB derives from being part of the Enbridge group of companies. A holding company will incur costs as part of its overall structure to manage the various operating entities that it owns. These costs are incurred to optimize resources, take advantage of synergies and minimize duplication of effort. As a holding company, Enbridge uses sound and reasonable allocators to allocate its operating costs to its subsidiaries to fairly represent costs to run that business on a full cost basis. In the case of EGNB, since all of its business activities are regulated it is reasonable that all of these allocated costs be recoverable within regulation.

There are a number of cost efficiencies that EGNB achieves by being part of the Enbridge group of companies. The benefit of being part of Enbridge was recognized when EGNB was awarded the General Franchise for the Province of New Brunswick and was recently acknowledged during the Cost of Capital proceeding, where the Public Intervenor's expert Dr. Booth on several occasions attached value to "the Enbridge name". This value is not however conveyed directly through services provided to EGNB by Enbridge and the exclusion of certain costs allocated to EGNB by Enbridge means that some of this value is not reflected anywhere within EGNB's revenue requirement. At the same time,

EGNB's customers are receiving the benefit through lower costs than would be incurred if EGNB was not part of a larger group of companies.

Q 10: Can you provide examples of these benefits?

A 10: Yes. While it is difficult to quantify many of the benefits, EGNB believes that some examples of the benefits that customers derive from Enbridge are related to access to established policies, procedures and best practices, utilizing the purchasing power of a large organization and the ability to support the financing of EGNB.

As a large organization, Enbridge has well defined policies, procedures and best practices that EGNB is able to leverage within its business. These are applicable to areas such as human resources, internal controls, governance, safety and reliability. In the absence of Enbridge, EGNB would need to incur costs to research, develop and maintain policies, procedures and practices in all of these areas. EGNB believes that material costs would be incurred to draw on the level of experience and expertise that is included in the Enbridge policies, procedures and practices. While some tailoring of these approaches may need to be done for the New Brunswick market, Enbridge provides a sound and regularly updated resource of knowledge.

As a relatively small utility, EGNB has limited buying power and derives direct benefits from being able to obtain goods and services under the Enbridge umbrella. Obtaining materials such as pipe, meters, vehicles and computer hardware as part of Enbridge's purchasing arrangements provides EGNB with access to the buying power of a utility nearly 200 times the size of EGNB. Similarly, EGNB believes that services such as liability insurance can be obtained at a lower cost as part of an overall Enbridge policy than if EGNB were to seek

out its own insurance arrangements. EGNB's customers are the direct beneficiaries of these cost savings.

EGNB has required financing in the form of debt and equity to develop its business and ongoing financial support is important to any business. As Dr. Booth commented in the Cost of Capital proceeding, the Enbridge name will help support improved credit metrics with investors and the capital markets (Transcript, p. 481). Further value from Enbridge is derived through Enbridge being the guarantor under EGNB's General Franchise Agreement. In the absence of Enbridge, there would certainly be costs associated with providing the financial assurances required by the Province. Also, EGNB has been able to raise equity for the business at a much lower cost than if it were not part of Enbridge. The cost of raising equity on a stand-alone basis in the equity markets would likely have come at a much greater cost than if there were not a majority unit holder like Enbridge. All of these reduced financing costs provide a direct benefit to customers.

Q 11: Can any of these benefits be quantified?

A 11: While it is difficult to quantify the full benefits customers receive by EGNB being part of Enbridge without incurring unnecessary cost, EGNB believes it is possible to attach some quantifiable value to the benefit received in relation to raising the necessary financing for the business.

EGNB has generally been able to raise equity for its business without having to engage an agent, largely due to the smaller amount of equity required from the markets due to Enbridge investing its proportionate interest, approximately 70% of the equity required. However, due to the size of the equity to be raised from independent investors in 2005, EGNB did engage an agent for a portion of the equity raised. This resulted in a fee of 5.75%, or \$628,187, on the \$10.9 million

of equity raised by the agent. Had similar arrangements been required to raise all of the equity in 2005, 2007 and 2008 the total equity call costs would likely have been \$6.9 million more, if EGNB was not part of Enbridge.

Q 12: Why has EGNB not brought forward a similar proposal in earlier financial reviews?

A 12: EGNB has been concerned for some time with the allocated costs that have been excluded from its revenue requirement. However, it was not until the 2008 Financial Review that the Board's consultant suggested that a review of the allocation may be warranted. In Teed, Saunders, Doyle's May 1, 2009 report, they suggested "that the current allocation methods are several years old" (page 14) and recommended that "EGNB prepare new allocation rationale to determine allowable costs for regulation for corporate overhead apportionments, and that the Board review these methodologies." (ibid) In its November 13, 2009 Decision, the Board directed EGNB to conduct such a review. This review has led EGNB to bring forward the proposed change.

Q 13: What is the impact on EGNB's 2009 revenue requirement as a result of this change?

A 13: Since many of the allocated costs are capitalized as part of Property, Plant and Equipment or Development O&M, the 2009 revenue requirement increases by \$523,016 due to the adjusted allocation methodology.

#### Purchase and Sale of Natural Gas Report

Q 14: Moving to the report prepared by Mr. John Butler of J.C. Butler Management Ltd. titled "Report to the New Brunswick Energy and Utilities Board on the Purchase and Sale of Natural Gas by Enbridge Gas New Brunswick During 2009", do you

have any comments on Mr. Butler's findings regarding the Enbridge Operational Services ("EOS") fees found on pages 14 to 16 of his report?

A 14: Yes. While Mr. Butler has raised some questions regarding the allocation of EOS fees, EGNB believes that the approach that it has used for their allocation between EUG and distribution is appropriate and reflective of EGNB's understanding of the work performed by EOS during that time. EGNB believes that any alternate allocation would create a cross-subsidy between EUG and gas distribution, which is to be avoided. As Mr. Butler noted in his report, his suggested options 3 and 4 would result in a cross-subsidy between EUG and distribution.

Mr. Butler has suggested that the Board may require EGNB to obtain justification from EOS for the changes that have been made to the allocation. EGNB notes that such justification is likely unavailable. EOS provides a basket of services to EGNB and other Enbridge companies. The SLA specifies an annual fee for the provision of these services rather than an hourly rate for each service. As a result, EOS does not document the time spent performing each discrete activity within the SLA. The adjustment to the allocation of the EOS fees was based on a discussion between EGNB and the EOS manager and is based on their best judgment of the division of the time spent and services provided.

As Mr. Butler notes, any concern regarding this issue "will probably be a matter of principle rather than materiality." (p. 16) EGNB agrees with this conclusion and, given the move to allocate more costs to EUG, believes it has erred on the side of being conservative to ensure that customers are not cross-subsidizing a competitive service.



2011 Budget

Q 15: Given that this is the first time that EGNB has brought forward a Test Year Budget for review by the Board, what evidence is being provided in relation to its 2011 Budget?

A 15: In developing its evidence related to its 2011 Budget, EGNB reviewed the NBSO minimum filing requirements (“MFR”) to obtain insight in terms of the type of information provided for a prospective review by another party regulated by the Board. While EGNB believes there are a number of aspects of the NBSO MFR that are not applicable to its business, the NBSO MFR was instructive on what would be of interest and value to the Board and Intervenors. Based on this review, EGNB has developed evidence that provides a comparison of its 2011 Budget to its 2010 Budget. In addition to the numeric comparisons, written variance explanations have also been provided where appropriate.

EGNB’s 2011 Budget, in Regulatory Financial Statement format, can be found in Exhibit A, Schedule 7 and an associated explanation of the 2011 Budget can be found in Exhibit A, Schedule 8. Assumptions used in preparing the 2011 Budget can be found in Exhibit A, Schedule 9.

Q 16: What conclusions does EGNB expect the Board to reach regarding the 2011 Budget?

A 16: EGNB expects that the Board will pre-approve EGNB’s operating and capital budgets and plans, recognizing that this approval would not fetter the Board’s discretion when the 2011 fiscal year is subject to a retrospective review. However, EGNB expects that this prospective review should limit the amount of review required on a retrospective basis, otherwise EGNB will be subject to an increased regulatory burden. EGNB would expect that the retrospective review

would focus primarily on what, if any, amount is to be added to the Deferral Account.

EGNB also expects that the Board will rely on its conclusions regarding the 2011 Budget to determine if the first test for the end of the Development Period has been satisfied.

End of Development Period Tests

Q 17: Does EGNB believe that the first test for the end of the Development Period will be satisfied in 2011?

A 17: No. The first test for the end of the Development Period as specified by the Board in its December 1, 2009 Decision is that: "Are the full costs equal to or below the currently available revenues?" (p. 6) As seen in EGNB's 2011 Budget at Exhibit A, Schedule 7, page 2, EGNB is forecasting that approximately \$7.4 million will be added to the Deferral Account in 2011. This clearly demonstrates that the first test will not be satisfied in 2011, as this test contemplates that not only is there no addition to the Deferral Account, but that full costs, including the recovery of the Deferral Account, would be recovered through the available revenues.

EGNB notes that the Board has not determined what action, if any, needs to be taken with regards to clarifying the second test for the end of the Development Period. EGNB believes that since the first test has not been satisfied in the 2011 Budget that concerns regarding the second test do not need to be addressed at this time.

\*\*\* I have no further questions