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Request from: CLF and Acadia Center

Question:

(Performance-based Regulation) Refer to Exhibit CLP-PBR-1, page 67. Please confirm whether or not the Company's penalty allocation methodology was modeled on any PIM structure proposed in the RE02 Proposed Final Decisions.

Response:

The Proposed Final Decisions in Docket No. 21-05-15RE02, did not include a specific penalty allocation methodology for the four proposed PIMs, as implementation for the potential PIMs would be considered as part of the EDC's future rate amendment proceedings once a final decision is received.[1] Please refer to Exhibit CLP-ELP-1, at 115-117, for the Company proposal to establish a maximum financial penalty pool that is allocated to each PIM. The Company's response to information request OCC-562[i], also includes information on the Company's proposed penalty cost threshold.

Prior Referenced Response:

[i] OCC-562 Question:

(Performance incentive mechanisms) Refer to Exhibit CLP-PBR-1, p. 66. As stated, the Company's PIM proposal for exposure to financial penalties is limited to an amount equal to 0.5% of the Company's total distribution revenues. How was this limit determined to be the maximum reasonable threshold for penalty exposure?

OCC-562 Response:

As explained in Exhibit CLP-ELP-1, at page 115, the Company proposes to establish a maximum financial penalty that is allocated to each PIM, annually. The maximum financial penalty pool is $10 million annually, which is equal to the exogenous cost threshold. The exogenous cost threshold of $10 million is intended to represent a point at which the exogenous cost change is significant to the Company in a given year. Setting the maximum financial penalty equal to the exogenous cost threshold ensures that the maximum penalty pool represents a significant financial risk but not an overly burdensome amount that may unnecessarily jeopardize the overall financial health of the Company.

[1] See, e.g.,, Docket No. 21-05-15RE02, Proposed Final Decision, at 1, "Finally, the Decision establishes reporting parameters, including the commencement of Scorecards and Reported Metrics as soon as practicable, *and the development of EDC-specific PIMs through subsequent rate case proceedings.*" Emphasis added.

For context, the Company's total level of operating and maintenance ("O&M") expense included in the cost of service is approximately $350 million, net of vegetation management expense and storm fund contributions. Thus, the amount of $10 million is approximately three percent of total O&M expense, which is comparable to the annual adjustment that would be allowed under the PBMRP at a three percent inflation rate. A *single* cost change rising to the level of three percent of total O&M expense would be a substantial change in circumstances and the Company does not expect to encounter *singular* cost changes equal to the rate of inflation on the total base of O&M expense on a regular or recurring basis.

The Company's proposed use of an exogenous cost materiality threshold in establishing the financial exposure associated with the proposed PIM framework is consistent with principles employed in PBR frameworks in other jurisdictions. Exogenous cost, or "Z-Factor", thresholds are commonly used to establish the level of financial materiality at which an event warrants extraordinary treatment, thereby distinguishing material impacts from the ordinary operating and business risks that a utility is expected to manage.

Please refer to the Company's response to information request OCC-430[i], for further information on the Company's proposed exogenous cost threshold.