Date Filed: September 21, 2026

Witness: Douglas P. Horton
Request from: Office of Consumer Counsel

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?

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.

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.

Prior Referenced Response:

[i] OCC-430 Question:

Exhibit CLP-ELP-1 Please explain in detail how the Company determined that a threshold significance of 0.5% of total distribution revenue is appropriate for Z-Factor eligibility. Please explain why the Company proposes a 0.5% threshold rather than the 0.75% threshold proposed in the Docket No. 21-05-15RE01, Proposed Final Decision, and provide all analyses, calculations, benchmarks, or other information relied upon in selecting the proposed 0.5% threshold.

OCC-430 Response:

The 0.75% materiality threshold proposed in the Docket No. 21-05-15RE01, Proposed Final Decision is unnecessarily high, and inconsistent with other jurisdictions. Although the Company supports the intention of establishing a materiality threshold as a means of balancing administrative burden with the Company's need to cover the costs of service, including those over which it has no control, a materiality threshold set too high actually renders the mechanism increasingly ineffective, raising the likelihood that the utility cannot commit to the PBR stay-out because it will be unable to obtain a fair or reasonable level of recovery of its operating costs, also barring customers from benefitting from the efficiency gains that come from an extended stay-out.1

In the extreme, a materiality threshold of 10%, for example, would indicate that for an event to qualify as exogenous in terms of its materiality, it must be at least $192.19 million ($1,921.9 million revenue requirement x 10%, using the Company's cost of service filed in this proceeding). The likelihood of a single event meeting this criteria is exceedingly rare, meaning the Z-factor, in practice, would be effectively rendered moot.

Additionally, PURA provided no basis for how it determined a threshold of 0.75% was appropriate. In fact, in its proposed final decision, PURA stated, "[t]he threshold [of 0.75%] better aligns with the thresholds established in other PBR jurisdictions," and then provided the following footnote referencing those other jurisdictions, each one of which is substantially below the 0.75% it proposed:

> "*Hawaii set thresholds equivalent to 0.2%, 0.25%, and 0.28%; Ontario set a threshold equivalent to 0.5%; Massachusetts set a threshold equivalent to 0.37%; and Alberta Utilities Commission set a threshold equivalent to 0.25*%."2

The Company's proposed Z-Factor of 0.5% *is* more closely aligned to those other jurisdictions.