

Hydro-Québec Distribution

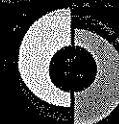
Cause Tarifaire 2004-2005

Dossier R-3541-2004

Preuve de FCEI/ASSQ

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Topics Covered - Drazen

- Basis for regulatory analysis
- Quality of data
- HQD cost of service
- Efficiency indicators
- Deferral accounts
- Rate rider (cavalier)



Topics Covered - Mikkelsen

- Management of Heritage supply
- Management of post-Heritage supply
- Rights of HQD vis-à-vis HQP for imports
- Allocation of post-Heritage supply cost



Major Themes

- Costs

What are the appropriate costs to use for setting rates?

- Risk

What are the appropriate risks that the utility should bear?



Basis for Regulatory Analysis

Fundamental question:

Are requested costs reasonable?



Basis for Regulatory Analysis

Fundamental question:

Are requested costs reasonable?

Reasonable compared to what?



Bases for Comparison of Costs

- Item-by-item evaluation
- Compared to previous year
 - Actual
 - Allowed by regulator
- Comparison of previous forecasts to actual
- Compared to costs, cost trends of others



Comparison to Previous Years

- Build a “regulatory history”
- Complicated by re-organization
- Recognize regulators’ decisions



Masse Salariale

2005 en comparaison avec 2004

| | 2004 | 2005 | ↑\$ | ↑% |
|--------|---------|---------|--------|-------|
| Hyp. 1 | 559,7\$ | 621,4\$ | 61,7\$ | 11,0% |
| Hyp. 2 | 674,5\$ | 698,8\$ | 24,3\$ | 3,6% |
| Hyp. 3 | 683,7\$ | 715,1\$ | 35,4\$ | 5,2% |



Efficiency Indicators

- Same issues as cost comparison
 - Need consistent basis for analysis
 - Recognize regulatory decisions
- 2004 to 2005 indicators not favourable



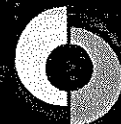
Post-Heritage Deferral Account

- Types of risk
 - Price risk
 - Volume risk
- How much risk should HQD bear?
 - What is size of risk?
 - How different from previous years?
 - Relationship with return on equity



Post-Heritage Deferral Account, 2

- Analysis
 - Price variability is new
 - What is size of price variability per MWh?
 - What is size in total cost?
 - Recent contracts
 - Volume variability is not new
 - Effect of volume variance similar to past
 - Direction has reversed



Rate Rider

- General regulatory practice
 - Most places: no exact match
 - Alberta does allow
 - Costs go up and down
- Issue specific to HQD: Post-Heritage energy
- Conclusions
 - Not needed if there is deferral account
 - Appropriate if there is no deferral account



Recommendations

- Cost of service: reduce by 15,5\$-22,5\$ million
- Better quality and detail of data
- Deferral accounts not needed for 2005
- Rate rider
 - Appropriate for post-Heritage costs if no deferral account
 - Not needed if adopt deferral account



Topics Covered - Mikkelsen

- Management of Heritage supply
- Management of post-Heritage supply
- Rights of HQD vis-à-vis HQP for imports
- Allocation of post-Heritage supply cost
- Can rates signal the cost of new supply?



Management of Heritage Supply

- What are the goals for managing Heritage energy?
- What risks are being recognized in decision making?
- Is maximum benefit extracted from flexibility of Heritage supply?



Post-Heritage Supply Management

- Short term purchases/sales
- Opportunity to lower costs
- Risk of higher cost
- Requires market knowledge
- Risk must be managed
- Evaluating outcomes requires information



Rights of HQD vis-à-vis HQP for imports

- Limited capability to import
 - HQ-D and HQ-P may or may not conflict in goals
 - Who gets access to transmission?



Post-Heritage Supply Cost Allocation

- Maintain ratio of \$/MWh to average?
- Maintain spread of \$/MWh to average?
- Uniform energy charge to all?
- Other?
- All but first require assessment of what is included in existing differentials



Is it Possible to Provide Signal of Post-Heritage Energy Cost?

- Average cost differs from incremental cost
- Current: Heritage much cheaper than new supply. Not a new issue.
- Is it possible to give signal of new cost within rate that preserves benefit of Heritage cost?
- “Solutions” have been unworkable or arbitrary

