

Summary of Evidence

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Gaz Métro - 7, Document 15
7 pages en liasse

Conclusions

It is important that the Régie undertake an updated, quantitative evaluation of Gaz Métro's allowed return.

- Investment risk for gas distributors has increased since 1999 and 2004.
- Returns anticipated by new pipeline projects suggest that NEB-formula returns are too low.

Gaz Métro's business and regulatory risk has increased since 1999 and 2004.

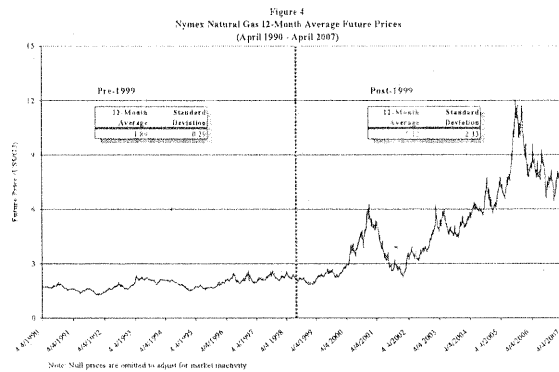
Gaz Métro is riskier than average Canadian and U.S. gas distributors, but its formula return is lower than that of U.S. distributors.

The ROE requested by Gaz Métro is conservatively low.

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|--------------------------|
| Régie de l'énergie |
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Investment Risk Has Increased Due to Changes in Market Environment

The market environment for gas utilities reflects greater uncertainty in the supply of gas, and greater uncertainty in the extent and timing of growth in gas demand.

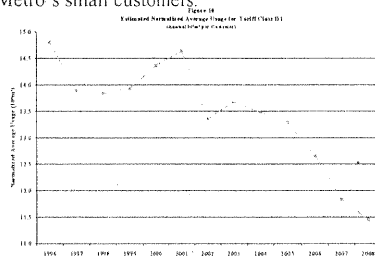


This has been reflected in recent increases in equity thickness for other Canadian gas utilities, and in the market return required by new projects (ROE's in the range of 11 to 14 percent on equity thickness of at least 25 percent.)

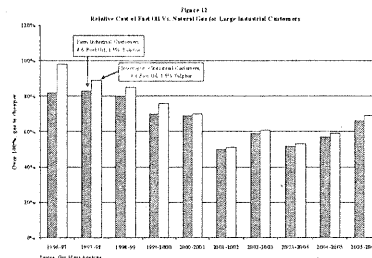
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What is Causing the Increased Business Risk for Gas Utilities and Gaz Métro?

- Increases in the level and volatility of gas prices have contributed to declines in usage per customer for Gaz Métro's small customers.



- The competitive position of natural gas has eroded for Gaz Métro's large industrial customers.



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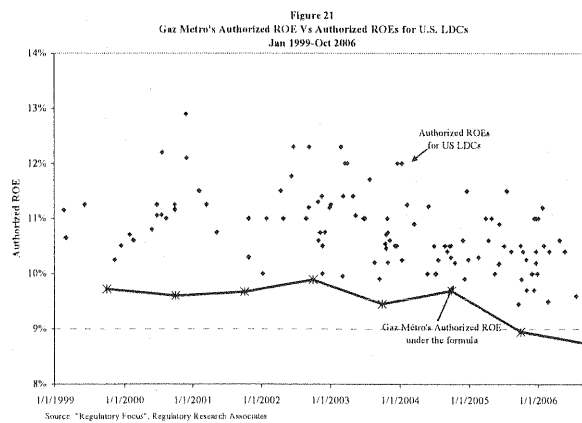
Gaz Métro Has Greater than Average Business Risk

- Gaz Métro's business environment is unique, and results in greater business risk than typical Canadian and U.S. gas distributors.
 - ▶ Natural gas has a significantly lower penetration rate in Québec.
 - ▶ Gaz Métro faces significantly stronger competition from electricity.
 - ▶ Gaz Métro serves a relatively large industrial load.

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Gaz Métro's Authorized ROE is Low Compared to U.S. Distributors

- Despite its greater than average business risk, Gaz Métro's allowed ROE is lower than that of U.S. gas distributors.



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Incentive Regulation Impact

- Gaz Métro operates under a “hybrid” incentive regulation plan.
 - ▶ All else equal, such a scheme increases business risks relative to a pure cost-of-service regime with deferral account protection.
- Recent changes in Gaz Métro’s incentive regulation plan have decreased its risks directionally.

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Gaz Métro’s Requested ROE is Conservatively Low

- Gaz Métro’s requested 10.19% ROE on 38.5% deemed equity thickness is at the low end of the range of required ROEs recommended by Prof. Chrétien.
- In my opinion, this is conservative given:
 - ▶ Gaz Métro’s higher business risk and somewhat lower regulatory risk than typical distributors in Canada and the U.S., and
 - ▶ Gaz Métro’s higher financial risk (at 38.5% deemed equity thickness) compared to the companies in Prof. Chrétien’s U.S. LDC sample.
- An increase in Gaz Métro’s ROE is appropriate given Gaz Métro’s increased business risks since the ROE formula was introduced in 1999 and reviewed in 2004.

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