

ADDITIONAL OBSERVATIONS PREPARED BY

BRIGID ROWAN

ECONALYSIS CONSULTING SERVICES

34 King East, Suite 1102, Toronto ON M5C 2X8

ON BEHALF OF

OPTION CONSOMMATEURS

PRESENTED IN THE CASE OF

SOCIÉTÉ EN COMMANDITE GAZ MÉTRO'S REQUEST

RELATIVE TO THE AUTHORIZATION TO CREATE A DEFERRAL ACCOUNT
RELATED TO AN EVENTUAL EXPANSION OF THE GAS SYSTEM TO
THE CÔTE-NORD

FILE R-3791-2012

RÉGIE DE L'ÉNERGIE

JULY 20, 2012

SCGM has stated that what is under consideration in this proceeding is merely the creation of a deferral account for expenses relating to feasibility studies and preparatory work¹ related to a project to eventually expand SCGM's system to the Côte-Nord ("the Project"). Thus, according to SCGM, the current application has no direct consequences in terms of rates:

La demande de Gaz Métro ne vise d'aucune façon à faire approuver les dépenses ici visées et encore moins leur traitement éventuel. Il n'y a aucun aspect tarifaire.²

Moreover, SCGM has emphasized that there will be ample opportunity in subsequent proceedings to address rate recovery for expenses relating to feasibility studies, either as part of an application to construct the Project, or in a rate case if the Project is abandoned:

Au contraire, Gaz Métro allègue explicitement dans sa demande qu'elle proposera soit lors de la demande d'investissement, soit lors de la cause tarifaire qui suivrait la décision d'abandonner ce projet, des règles de disposition du solde du compte de frais reportés. À cette occasion, les intervenants auront la possibilité d'examiner les dépenses ainsi comptabilisées et de faire leurs commentaires à la Régie. Cette dernière décidera alors d'accepter ces dépenses, en tout ou en partie, et fixera les règles visant leur récupération par l'intermédiaire des tarifs.³

OC respectfully submits (for the reasons discussed below) that it would be problematic for the Régie to merely approve SCGM's request in this proceeding without providing some further guidance as to how SCGM should proceed in regard to the activities relating to the proposed deferral account.

SCGM maintains that the situation in this proceeding is not unusual and is analogous to the expenditures routinely undertaken by SCGM for feasibility studies. Moreover, SCGM claims that ratepayers (and not shareholders) should bear any costs for feasibility studies if the Project does not proceed:

¹ For the purposes of these observations, "feasibility studies" will include both the feasibility studies and preparatory work (*études de faisabilité et travaux préparatoires*), for which the deferral account is being requested in the current proceeding.

² B-0007, Réplique de Gaz Métro aux commentaires formulés par OC.

³ B-0007, Réplique de Gaz Métro aux commentaires formulés par OC.

En termes de principes applicables, la situation qui prévaut dans le présent dossier n'est pas exceptionnelle. Chaque année, Gaz Métro doit envisager de desservir telle ou telle région ou tels ou tels clients, ou reçoit des demandes en ce sens. Après des études plus poussées, certains projets se concrétisent, d'autres pas. Ceux qui ne sont pas réalisés voient malgré tout leurs coûts récupérés dans le coût de service de Gaz Métro pour assurer une logique de traitement équitable du distributeur.⁴

[...]

[Régie IR 7.4] La Régie comprend que si la faisabilité du Projet n'est pas démontrée et que le budget au montant de 40 M\$ a été partiellement ou complètement dépensé, la clientèle retirera peu ou pas de bénéfice. La Régie se questionne sur la possibilité de limiter le risque financier assumé par la clientèle en le partageant avec les actionnaires de Gaz Métro. Veuillez élaborer.

[Response to Régie IR 7.4] Gaz Métro ne croit pas qu'il revienne à son actionnaire de limiter le risque financier assumé par la clientèle dans la mesure où les tarifs demeurent justes et raisonnables, tout en permettant le développement des infrastructures sur le territoire québécois.⁵

But in fact, this situation is unusual, with potential consequences that are very significant. The Project, and associated feasibility studies, have many attributes that are exceptional, including the following:

- large (450 km, 2 new compressor stations)
- costly feasibility studies (\$50 million by the end of September 2013)
- very costly Project (\$750 million, would increase rate base by 40%)⁶
- special purpose (mainly serving a few large metals and mining customers far removed SCGM's existing system),
- dependent upon complicated cost-sharing and other contractual arrangements (with industrial customers, as well as the Quebec government)
- expedited (to permit a Project in-service by end of 2015 or 2016).

Put simply, SCGM plans on spending \$50 million dollars to investigate the feasibility of a Project that is estimated to have an adverse rate impact of \$720 million (even if fully

⁴ B-0012, SCGM Response to Régie IR 7.2. All IR Responses cited are from document B-0012 therefore subsequent references will only include the IR number.

⁵ SCGM Response to Régie IR 7.4.

⁶ http://www.corporatif.gazmetro.com/corporatif/communiquer/html/3059689_fr.aspx?culture=fr-ca

utilized); SCGM will seek to mitigate this negative rate impact via cost-sharing arrangements with industrial customers:

La contribution tarifaire après 40 ans serait de + 720 M\$.

[...]

Ces volumes, pouvant éventuellement justifier la rentabilité du Projet sans contribution Côte-Nord, seraient cependant largement supérieurs à la capacité physique prévue du réseau raccordant la Côte-Nord.

C'est d'ailleurs pourquoi Gaz Métro proposera la mise en place d'une contribution Côte-Nord pour les clients industriels.⁷

In addition to possible cost-sharing arrangements with industrial customers, SCGM states that it has obtained letters of intention from potential customers and will execute 20-year firm contracts prior to applying to the Régie for Project authorization.⁸

The current proceeding is not the appropriate forum to consider the arrangements that SCGM may propose for cost-sharing and firm contracts with customers on the Project. Instead, these would need to be addressed in future case(s), with a process allowing for full and meaningful participation by intervenors. But it is now timely to point out that any such arrangements could entail sizable risks and costs for other SCGM ratepayers. The reality is that there are major asymmetries in terms of how the Project could affect potential customers and other SCGM ratepayers. The potential customers are primarily very large, very energy-intensive metals and mining companies.⁹ It is a given that these industrial customers will be highly active in seeking the best deal possible in any arrangements with SCGM (and the Quebec government), as well as in advocating their interests at the Régie.

Most SCGM ratepayers (especially in the Residential and CII classes) are individually small, and energy is not a major priority relative to other considerations. By comparison, large energy-intensive industrial customers have much more at stake and are much better positioned (in terms of both resources and bargaining/political leverage) to advocate their interests in regard to energy issues.

⁷ SCGM Response to Régie IR 2.2.

⁸ SCGM Response to Régie IR 1.4.

⁹ SCGM Responses to Régie IR 1.1, 1.2, 1.3, 1.4.

Groups such as OC will do what they can to advocate for the interests of smaller ratepayers. And the Régie will of course operate within its mandate to protect the public interest in this and future proceedings.

Still, OC respectfully submits that it is important at this juncture for the Régie to provide guidance, so as to avoid potential adverse impacts on ratepayers relating to feasibility studies for the Project. SCGM plans on spending tens of millions of dollars on these studies in the near future. So it is not sufficient to merely set up a deferral account and defer all consideration of rate consequences until future proceedings. Put simply, once large amounts of money are spent, it could be much more problematic to deal with who pays (notably for any costs not borne by the Quebec government or Project customers).

In this context, it is necessary to comment on the feasibility studies and cost-sharing (and other) arrangements between SCGM and the Quebec government in regard to these studies (and the Project). The feasibility studies would entail very sizable expenditures, on a very expedited schedule. These expenditures are estimated to be in the order of \$50 million by the end of September 2013; SCGM might thus seek to increase the amount of deferral account beyond the \$40 million now being requested:

Les dépenses (incluant les frais financiers) pour la période du 1er octobre 2011 au 30 septembre 2012 seraient de l'ordre de 10 M\$. Pour la période du 1er octobre 2012 au 30 septembre 2013, les montants devraient être de l'ordre de 39,6 M\$. Il est à noter que le montant dépasse le montant maximum du compte de frais reportés. Tel que déjà mentionné à la réponse à la question 5.3, dans le cas où le dépôt du Projet à la Régie ou que le processus réglementaire accuserait un retard, Gaz Métro pourrait mettre un frein aux études et travaux préparatoires et reporter la mise en service ou poursuivre les études et travaux préparatoires au-delà du montant de 40 M\$. Dans cette deuxième option, toute somme excédant ce montant de 40 M\$ devrait faire l'objet d'une nouvelle demande à la Régie afin que celle-ci autorise de hausser ce maximum.¹⁰

¹⁰ SCGM Response to Régie IR 6.3. For additional information concerning feasibility study expenditures, see SCGM Responses to Régie IRs 2.4, 5.3, 5.5, 6.1, 6.2, 6.5, 6.6.

SCGM asserts that the Quebec government has made a firm commitment to reimburse 75% of the first \$40 million in expenditures for feasibility studies (for a maximum of \$30 million):

Effectivement, le gouvernement du Québec garantit le remboursement de 75 % des premiers 40 M\$ dépensés advenant que le Projet ne se réalise pas.¹¹

[...]

De l'avis du gouvernement du Québec, toutes les conditions semblent aujourd'hui réunies pour permettre la réalisation du Projet. Son apport, tel que décrit dans l'extrait du texte du budget présenté à l'annexe 1, s'étend donc sur deux volets, soit celui des études et travaux préparatoires, ainsi que celui des infrastructures.

Le gouvernement a annoncé qu'advenant que la faisabilité du Projet ne soit pas démontrée, il assumera 75 % des premiers 40 M\$ qui auront été déboursés pour réaliser les études et travaux préparatoires nécessaires et ce, d'ici à la décision finale de la Régie autorisant l'investissement pour l'extension du réseau. Ainsi, 75 % des coûts portés au compte de frais reportés faisant l'objet de la présente demande seront assumés par le gouvernement du Québec, pour un maximum de 30 M\$.¹²

[...]

L'annonce du budget représente un engagement du gouvernement du Québec.¹³

The current proceeding is not the appropriate forum for a full review of SCGM's arrangements with the Quebec government and for evaluating how these arrangements might operate in a variety of scenarios.¹⁴ Suffice it to say that it remains uncertain how much of the feasibility study expenditures might actually be reimbursed by the Quebec government and how much might eventually be borne by SCGM (and in turn by SCGM shareholders and/or ratepayers). Governments change and can alter their plans.

¹¹ SCGM Response to Régie IR 2.4.

¹² B-0005, GM-1, Doc 1, p. 6, lines 10-19.

¹³ SCGM Response to Régie IR 2.1.

¹⁴ According to SCGM Response to Régie IR 2.1, SCGM and the Quebec government have entered into various agreements in regard to cost sharing, and other agreements will be concluded in the future if the Project is found to be feasible. The current proceeding has not permitted an opportunity for review of agreements now in place, nor has it allowed detailed consideration of any other agreements that might be concluded in the future.

Given all of the factors discussed above, OC respectfully submits that approval of the deferral account should be conditioned to insulate ratepayers (other than those potentially served by the Project) from any adverse rate impacts associated with the Project feasibility studies. Put simply, to the extent that any costs for the Project feasibility studies are not borne by the Quebec government, or Project customers (actual or potential), these costs should be borne by SCGM shareholders.

In making this recommendation, OC is seeking to provide the correct incentives. As discussed above, the Project (and associated feasibility studies) are dependent upon complicated cost-sharing and other contractual arrangements (with the Quebec government, as well as industrial customers). If SCGM shareholders are bearing any costs that cannot be recovered from the Quebec government or Project customers, SCGM management will have the correct incentives to minimize those costs. And it is particularly important for SCGM to have the correct incentives, since it will be undertaking complicated arrangements with sophisticated counterparties (the Quebec government and industrial customers) that are well positioned (in terms of both resources and bargaining/political leverage).

If SCGM believes that it would bear too much risk if OC's recommendation is implemented given the arrangements currently in place (with the Quebec government and potential customers), SCGM can accordingly negotiate better deals or not move forward with the feasibility studies.

Finally, in evaluating SCGM's incentives, the Régie should take into account that the Project would greatly expand the SCGM system in terms of both geographic scope and rate base. As noted previously, the Project would add new territories along a 415 km routing, and it would increase rate base by 40%. This Project represents an enormous growth opportunity for SCGM shareholders and management. In this context, it is

entirely appropriate that SCGM shareholders bear any costs that cannot be recovered from the Quebec government or Project customers (actual or potential).