

## **Réponse d'Option consommateurs (OC) à la Demande de renseignements no 2 de Société en Commandite Gaz Métro (« Gaz Métro ») à OC**

### **Dossier R-3809-2012 Phase 2**

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**1 Référence :** (i) Pièce C-OC-0047, Mandate, page 5, l. 19 et 20

i) « *We note that Ms. Rowan received expert-consultant assistance from Dr Higgin for subjects 1 to 3 and Mr. Wilson for subject 4.* »

**Demande :**

**1.1** Fournir les références précises (pages et lignes) des passages dans la pièce C-OC-0047 qui se fondent sur l'assistance fournie par les Dr Higgin et Wilson.

**Réponse :**

In this file, Dr. Higgin and Mr. Wilson are acting as expert-consultants (*experts-conseils*) as that term is defined in S. 1 of the *Règlement sur la procédure de la Régie de l'énergie*. As such, Dr. Higgin and Mr. Wilson have both counselled and assisted OC in the preparation of its evidence. However, OC's external analyst Brigid Rowan is the sole author of the report.

As specified in OC's budget justification letter (C-OC-0020) and in reference (i), Dr. Higgin assisted Ms. Rowan with subjects 1 to 3, which are detailed in the OC Report (C-OC-0047) on pp. 4-5):

1. Operating Costs
2. 2013 Revenue
3. Other Cost Drivers – Affiliate Transactions

These subjects are covered in Sections 3, 4 and 5 of the OC Report.

Similarly, as specified in OC's budget justification letter (C-OC-0020) and in reference (i), Mr. Wilson assisted Ms. Rowan with subject 4, Interim Sharing Mechanism for Underearnings and Overearnings (TP/MAG) for 2013 (OC Report, p. 5). This subject is covered in Section 6 of the OC Report.

It is not possible to identify the precise pages and lines since Dr. Higgin and Mr. Wilson counselled and assisted Ms. Rowan in the preparation of the respective above-mentioned sections of the report as a whole.

**2 Référence :** (i) Pièce C-OC-0047, 3.1.1 Reasonableness of 2012-2013 Salary and Wages Budget, page 8, l. 9 à 14

i) « *Our analyses defined the average increases in the Salaries and Wages over the period of the IM in the following ways:*

- *Salaries and Wages Projected and Actual (Current \$)*
- *Salaries and Wages Projected and Actual (Constant \$)*
- *Salaries and Wages Projected and Actual (CPI-X \$).* »

**Demande :**

**2.1** Fournir chacune des analyses auxquelles il est fait référence dans l'extrait i).

**Réponse :**

Please find attached a copy of our analyses at the end of this document, entitled Attachment to IRR #2.1.

Note 1: In our analyses we have included salary and wages (*salaires*) and benefits (*avantages sociaux*). In other words, the components of operating costs that have been analyzed are based on the first two lines of the tables in B-0261, GM-18, Doc 5, Annexe 1 (questions 4.1, 4.3 and 4.4), respectively entitled *Salaires* and *Avantages sociaux*. It should also be noted that the data source for the current actual and current project salaries and benefit has been the sum of the first two lines of the above referenced tables on pp. 2, 3, 5 and 6 of Annexe 1. B-0254, GM-18, Doc 1, Response to Régie IR 9.1 is another corroborating source of data on salaries and wages, and benefits, but it only covers the period of 2007-2008 to 2012-2013

Note 2: In Attachment to IRR #2.1, all amounts referred to as "Real" are in fact "Actual" amounts.

Note 3: In Attachment to IRR #2.1, data sources for CPI Quebec (line 1 of the attachment) and the Cumulative CPI Index (line 2 of the attachment) are found in B-0261, GM-18, Doc 5 (mislabelled as Doc 4 in the hardcopy of the GM response), Annexe 1 (questions 5.1 and 6.1), p. 7 of 8 (or Tab *Annexe 1 Q5.1 et*

6.1 in the Excel spreadsheet), lines 10 and 11, respectively. Given that the expired IM formula used CPI Quebec, this is the CPI used in our analysis.

Note 4: In Attachment to IRR #2.1, data sources the IM Factor X (line 3) and GDPPI (line 4) (not used and presented for information only) are found at B-0261, GM-18, Doc 5, Annexe 1 (question 7.1) p. 8 of 8 (or Tab *Annexe 1 Q7.1*) in the Excel spreadsheet), lines 2 (*Facteur X*) and 1 (*Taux inflation*), respectively.

**3 Référence :** (i) Pièce C-OC-0047, 4.2 Analysis of Historic Forecast, page 17, l. 18 à 20

i) « *One important finding is that customer number Projections and Actuals are not symmetrically distributed. There is an average consistent and obvious annual customer addition forecast error of about 1000.* »

**Demande :**

**3.1** Comment l'erreur alléguée moyenne de 1000 clients est-elle calculée? Fournir tous les calculs au soutien de ce résultat.

**Réponse :**

Please find attached a copy of our analyses at the end of this document, entitled Attachment to IRR #3.1. It is important to note that we have focussed our analysis on D1 customer projections and actuals. Note that the average variation between D1 customer projections and actuals for the years 1998-1999 through to 2011-2012 is -976 (which is the basis for our characterization of GM's annual customer addition forecast error of about 1000).

In Attachment to IRR #3.1, the Data Sources for this analysis have been provided as GM-9 Doc 1, GM-12 Doc 5 and GM-16 Doc 1 Pg 1-4 (A-0074).

To further clarify:

1. The source of 2012-2013 projected customer numbers is B-0164, GM-12, Doc 5, p. 1.
2. The source of 2011-2012 projected and actual customer numbers is A-0064, (R-3831-2102, GM-9, Doc 1), p. 1.
3. The source of the remaining projected and actual customer numbers is A-0074, (R-3831-2102, GM-16, Doc 1), pp. 1-4.

- 4 Références :** (i) Pièce C-OC-0047, Conclusions method to hold regulated customers harmless, page 29, l. 29 et page 30, l. 1  
(ii) Pièce C-OC-0047, Conclusions method to hold regulated customers harmless, page 30, l. 8  
(iii) Pièce C-OC-0047, Conclusions method to hold regulated customers harmless, page 30, l. 15 et 16

- i) « [...] to cover potential transaction costs associated with increased complexity [...] »
- ii) « [...] any potential costs/risks and to provide a reasonable sharing [...] »
- iii) « [...] since GM was unwilling to proceed given a quite limited share of benefits (\$3 million) flowing to ratepayers. »

**Demandes :**

- 4.1** OC parle de « potential transaction costs ». De quels frais de transaction OC parle-t-elle ici?

**Réponse :**

Ms. Rowan, the author of the OC Report is an energy economist, and the Régie is an economic regulator. She has therefore defined transaction costs in their classic economic sense, i.e. the cost of participating in a market. Dahlman further divides transaction costs into three broad categories: search and information costs, bargaining and decision costs, policing and enforcement costs. (Dahlman, Carl J. (1979). "The Problem of Externality," Journal of Law and Economics 22 (1): 141–162).

Indeed there are transaction costs for the regulated customers in all three of Dahlman's categories, including:

- a) search and information: the regulatory cost incurred for the Régie and representatives of consumer groups to review GM's proposal and determine if regulated customers are indeed held harmless;<sup>1</sup>

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<sup>1</sup> A very proximate example of a search and information transaction cost that will be borne by ratepayers is the time we are taking to have this IR exchange. We have already indicated that without a finance expert, who could incur potentially prohibitive transaction costs, OC cannot ascertain if in fact regulated customers are truly being held harmless in this transaction (which is in the interest of the unregulated customers (and ultimately the shareholders)).

- b) bargaining costs: the regulatory cost required to come to an acceptable agreement with GM regarding how GM should ensure that regulated customers are held harmless;
- c) policing and enforcement costs: the costs that ensure that GM adheres to the terms of regulatory decision (i.e. monitoring and follow-up) and the costs of consequent action for failure to adhere to these terms (i.e. further regulatory action).

The point that the OC report is making is there are transaction costs for the regulated customers with respect to this debt transfer that GM is not recognizing and has not accounted for in its proposal to hold ratepayers harmless. And this is not reassuring for the ratepayers, who have nothing to gain from GM's proposal; but who are now being asked to bear unrecognized transaction costs.

OC also makes the point that the more complex a transaction, the higher the transaction costs. As we have indicated in the OC report, this debt transfer is a complex transaction (involving hundreds of millions of dollars and various financial instruments) and OC cannot ascertain if in fact regulated customers are truly being held harmless in this transaction without a finance expert.

**4.2** OC parle de « potential costs/risks ». Selon OC, quels pourraient être ces risques?

**Réponse :**

This is a complex transaction involving hundreds of millions of dollars and various financial instruments. GM is playing a dual role in this transaction, since it involves both regulated and non-regulated activities. As proposed by GM, this transaction is to benefit non-regulated activities (and thus GM shareholders), while providing no benefits to GM ratepayers. As we have seen in the very recent past, things do go wrong in financial transactions and markets, and the resulting losses are often socialized. A debt transfer worth hundreds of millions may come with some risk, and there are more risks involved in the absence of independent expert review. Regulated consumers do not have access to an independent financial expert to assess the exact nature of potential costs and risks and to ensure that ratepayers will be held unharmed.

**4.3** OC détermine à 3 M\$ la portion du « bénéfice » que Gaz Métro devrait payer aux clients. Comment OC a-t-elle déterminé ce montant?

**Réponse :**

\$3M is only 1/6 of the \$18M value that GM attributes to this natural hedge.<sup>2</sup> OC suggested the \$3M amount to share in the benefit of the debt transfer provided by the regulated customers, as well as to offset potential transaction costs and risks (as defined above).

During recent rate cases, in which GM has hired financial experts to review its ROE, GM and intervenors have incurred approximately \$1M per year in regulatory costs,<sup>3</sup> so the Distributor is familiar with the high transaction costs involved in bringing in financial experts to review complex transactions. But complex transactions also involve transaction costs for the Régie and representatives of consumer groups to review GM's proposals. Given that the debt transfer will likely be an isolated transaction, it may not be worthwhile to incur the costs associated with an expert review. As such, OC has suggested that a reasonable sharing of the benefit could be in the order of \$3M. OC's suggestion for sharing of the benefit was intended to provide a limited sharing of the benefit that could be readily implemented absent expert review and the associated high transaction costs of such a review. Based on expert review, a different (and likely larger) sharing of the benefit might be found to be appropriate. But if in fact expert review will be required to resolve this issue, then the costs of this expert review should be borne (in part and probably in whole) by GM shareholders and not the ratepayers, since this transaction is being undertaken to benefit non-regulated activities.

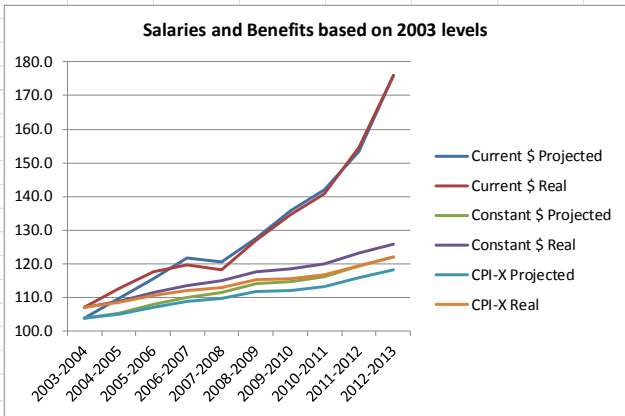
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<sup>2</sup> According to GM's response to OC IR 15.11 (B-0261, GM-18, Doc 5, p. 37), GM estimates the cost to obtain a similar hedge on the market for its US investments to be approximately \$18 million in October 2012.

<sup>3</sup> According to B-0242, GM-18, Doc 10, GM's Response to OC IR 1.1, pp. 1-2, during the four rate cases that examined ROE since 2007 with the assistance of external experts (this excludes R-3720-2010 and R-3662-2008 but includes the current case), the average amount per year spent on the ROE portion of the application has been \$909K. As GM has discussed in this same document, these costs are likely higher given that not all the associated costs could be estimated. Thus \$1M/year may be an understatement in terms of total costs associated with the ROE portion of each application.

**Attachment to IRR # 2.1**

			2003-2004	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012	2012-2013	Avg % 2003-12
	<b>Sources</b>	<b>Calculations 2003=100</b>											
	GMI-18 Doc 1 IRR 9.1	CPI Quebec	100	1.6	2.4	2	1.3	2.3	0.6	1.3	2.6	2.3	1.82
		Cumulative CPI Index	100	101.60	104.04	106.12	107.50	109.97	110.63	112.07	114.98	117.63	
	GMI-18 Doc 5 Annex 1 Q 4.1, 4.3 and 4.4	IM Factor X	0.3	0.3	0.5	0.5	0.5	0.3	0.3	0.3	0.3	0.3	
		GM-18 Doc 5 Q7.1	1.48	3.14	1.51	2.25	2.41	1.18	1.99	1.06	1.16	2.2	1.88
		GM-18 Doc 5 Q7.1											
		GDPPPI											
		CPI-X %		1.3	1.9	1.5	0.8	2	0.3	1	2.3	2	1.46
		CPI-X Cum	100	101.30	103.22	104.77	105.61	107.72	108.05	109.13	111.64	113.87	
		<b>Salaries and Benefits</b>	<b>2003-2004</b>	<b>2004-2005</b>	<b>2005-2006</b>	<b>2006-2007</b>	<b>2007-2008</b>	<b>2008-2009</b>	<b>2009-2010</b>	<b>2010-2011</b>	<b>2011-2012</b>	<b>2012-2013</b>	<b>Avg % 2003-12</b>
		Current \$ Projected	103.7	109.6	115.6	121.7	120.5	127.6	135.9	142.0	153.3	175.9	8.0
		Current \$ Real	107.0	112.6	117.6	119.5	118.2	127.0	134.5	140.9	154.6	175.9	7.7
		Constant \$ Projected	103.7	105.36	107.89	110.05	111.48	114.04	114.72	116.22	119.24	121.98	2.0
		Constant \$ Real	107.0	108.71	111.32	113.55	115.02	117.67	118.38	119.91	123.03	125.86	2.1
		CPI-X Projected	103.7	105.05	107.04	108.65	109.52	111.71	112.04	113.16	115.77	118.08	1.6
		CPI-X Real	107.0	108.39	110.45	112.11	113.00	115.26	115.61	116.77	119.45	121.84	1.6
		<b>Normalized Calculations</b>	<b>2003-2004</b>	<b>2004-2005</b>	<b>2005-2006</b>	<b>2006-2007</b>	<b>2007-2008</b>	<b>2008-2009</b>	<b>2009-2010</b>	<b>2010-2011</b>	<b>2011-2012</b>	<b>2012-2013</b>	<b>Avg % 2003-12</b>
		<b>Customers</b>	157718	162936	167561	167561	171152	175741	179311	182328	185848	189846	2.26
		S&W /Customer											
		Current \$ Real	678.43	691.07	701.83	713.17	690.61	722.65	750.09	772.78	831.86	926.54	4.06%
		Constant \$ Real	678.43	667.21	664.36	677.65	672.06	669.56	660.17	657.68	662.00	662.97	-0.25%
		CPI-X Real	678.43	665.24	659.17	669.05	660.26	655.87	644.75	640.42	642.74	641.79	-0.60%
		<b>Volumes</b> 10 <sup>6</sup> M <sup>3</sup>	5308	5476	5310	5490	6250	5805	5130	5437	5461	5152	
		S&W /c/ m3											
		Current \$ Real	0.0202	0.0206	0.0221	0.0218	0.0189	0.0219	0.0262	0.0259	0.0283	0.0341	
		Constant \$ Real	0.0202	0.0199	0.0210	0.0207	0.0184	0.0203	0.0231	0.0221	0.0225	0.0244	
		CPI-X Real	0.0202	0.0198	0.0208	0.0204	0.0181	0.0199	0.0225	0.0215	0.0219	0.0236	



**Attachment to IRR # 3.1**

<b>Customer Addition Forecast Tarif D1</b>																
Customers	1998-1999	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012	2012-2013	Avg Variation
Projected	148092	149594	150130	151496	150600	153248	156300	163152	169276	173885	171748	181202	184215	186553	191268	
Actual	147863	149489	151091	151578	153156	155487	160140	164855	168829	172981	177064	180046	183302	187274	191268	
Difference P-A	229	105	-961	-82	-2556	-2239	-3840	-1703	447	904	-5316	1156	913	-721	0	-976
Median Difference																-402
<b>Data Sources</b>																
GM-9 Doc 1																
GM-12 Doc 5																
GM-16 Doc 1 Pg 1-4 (A-0074)																

