

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

DEMANDES DE RENSEIGNEMENTS DE L'ASSOCIATION QUÉBÉCOISE DES CONSOMMATEURS INDUSTRIELS D'ÉLECTRICITÉ (AQCIE) ET DU CONSEIL DE L'INDUSTRIE FORESTIÈRE DU QUÉBEC (CIFQ) DANS LE CADRE DU DOSSIER SUR LA DEMANDE D'APPROBATION DU TAUX DE RENDEMENT DES CAPITAUX PROPRES ET DU MÉCANISME DE TRAITEMENT DES ÉCARTS DE RENDEMENT

Demande de renseignements adressée à Hydro-Québec

Premier sujet – Contexte de la demande

1. Référence:

HQTD-1, Doc-1, page 7

Préambule

HQ présente deux tableaux démontrant l'évolution des taux de rendement autorisés des capitaux propres d'HQT, HQD et de trois groupes de référence.

Question:

1.1. Veuillez fournir les données utilisées pour préparer ce tableau, en format Excel (.xls). Pour les deux groupes de référence ainsi que pour le groupe des entreprises gouvernementales, veuillez fournir les données propres à chaque entité réglementée ainsi que le facteur de pondération utilisé pour établir la moyenne du groupe.

2. Référence:

HQTD-1, Doc-1, page 8, ligne 25

Préambule

HQ explique que dans la décision D-2012,97, la Régie « *reconnaissait la nécessité de traiter les dossiers de révision des politiques financières du Transporteur et du Distributeur conjointement avec celui du MTÉR* ».

Question:

2.1. Où la Régie exprime-t-elle la notion de nécessité?

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

3. Référence:

HQTD-1, Doc-1, page 9, ligne 11

Préambule

HQ explique que dans la décision D-2012-119, la Régie soulignait « *le besoin d'examiner de façon simultanée les sujets du traitement des écarts de rendement et de l'établissement du taux de rendement des capitaux propres* »

Question:

3.1. Où la Régie exprime-t-elle la notion de besoin?

Deuxième sujet – Analyse de risque

4. Référence:

HQTD-1, Doc-1, page 12, ligne 18

Préambule

HQ explique que le risque réglementaire « *découle quant à lui des incertitudes sur les décisions de l'organisme de réglementation économique (...) qui peuvent avoir une incidence sur la récupération des coûts et le rendement des capitaux propres.* »

Question:

4.1. À votre avis, considérant que l'État québécois est (l'unique) actionnaire d'Hydro-Québec, ce risque est-il réduit par l'octroi de pouvoirs extraordinaires au gouvernement par l'article 7 de la *Loi concernant principalement la mise en œuvre de certaines dispositions du discours sur le budget du 20 novembre 2012*, à savoir le droit d'établir les charges - ou charges nettes, selon le cas - d'exploitation aux fins de la fixation des tarifs de ces entités? Veuillez détailler votre réponse.

5. Référence:

HQTD-1, Doc-1, pages 13-14

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

Préambule

« Le risque d'affaires du Transporteur résulte essentiellement d'évènements fortuits qui auraient un impact à la hausse sur ses coûts au cours d'une année tarifaire. En effet, bien que le Transporteur présente une structure de coûts relativement fixe, il demeure assujéti, à l'intérieur de la période pour laquelle ses revenus requis projetés ont été établis, à une variabilité de certains coûts pouvant entraîner des impacts défavorables notables sur sa performance financière. » (page 13, lignes 1 à 6)

Aux paragraphes suivants, HQ donne des détails sur ces évènements fortuits ainsi que des éléments qui, à son avis, sont de nature à favoriser de tels évènements. Il est essentiellement question de bris, défaillances (notamment sur le réseau de télécommunications), dépannage, maintenance et retrait d'actifs.

À la page 14, à partir de la ligne 7, HQ traite aussi de deux autres problèmes qui seraient selon lui exacerbés par une hausse importante du budget des investissements, à savoir la pression accrue sur les flux de trésorerie et la pression exercée sur les échéanciers des projets par les démarches réglementaires. Il ne semblerait pas que ces autres problèmes aient un impact sur le rendement réel en fin d'année.

Questions:

Aux questions 5.1 à 5.5, nous cherchons à évaluer le risque que représentent les évènements fortuits mentionnés en préambule.

5.1. Nous comprenons du premier extrait cité en préambule que le risque d'affaires du Transporteur résulte essentiellement de la possibilité de réaliser, pour une année donnée, un manque à gagner, c'est-à-dire de voir son bénéfice net réglementé affecté négativement par des coûts qui n'ont pas été pris en compte dans les revenus requis, et donc, dans les tarifs de cette année là. Notre compréhension est-elle correcte? Sinon, veuillez expliquer.

5.2. Nous comprenons par ailleurs du reste de cette section que les coûts visés à 5.1 seraient uniquement en lien avec des bris et des défaillances, des activités de dépannage et de maintenance ainsi qu'avec des retraits d'actifs. Notre compréhension est-elle correcte? Sinon, veuillez expliquer en indiquant notamment les autres types de coûts visés à 5.1.

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

- 5.3. Quel est le plus important manque à gagner subi par HQT au cours de la période 2004-2012 en lien avec les coûts visés à 5.1 et 5.2? Le cas échéant, veuillez faire référence aux documents des rapports annuels du Transporteur sur le site internet de la Régie.
- 5.4. Avez-vous réalisé une étude de la variabilité des coûts ou sur le risque en lien avec des bris et des défaillances, des activités de dépannage et de maintenance, des retraits d'actifs et tout autre type de coût mentionné en réponse à 5.2? Si oui, veuillez la déposer.
- 5.5. Veuillez identifier, pour les années 2004 à 2012, le montant prévu aux revenus requis ainsi que le montant réel en ce qui a trait aux coûts liés aux bris, défaillances, dépannage, maintenance, retraits d'actifs et tout autre type de coût mentionné en réponse à 5.2.
- 5.6. Nous comprenons que les autres problématiques que vous soulevez, à savoir la *pression accrue sur les flux de trésorerie* et la *pression exercée sur les échéanciers des projets par les démarches réglementaires*, n'entraîneraient pas des problèmes de coûts tels que ceux mentionnés aux articles 5.1 et 5.2. Notre compréhension est-elle correcte? Sinon, veuillez expliquer en indiquant de quel ordre de grandeur seraient ces coûts.
- 5.6.1. Pourriez-vous expliquer de manière plus détaillée de quelle façon ces problématiques affectent votre risque d'affaires?

6. Référence:

HQTD-1, Doc-1, page 14, ligne 27

Préambule

Vous invoquez la part des ventes faites aux clients industriels pour affirmer que le Distributeur fait face à un risque d'affaires important étant donné que ses ventes sont soumises à de grandes fluctuations.

Questions:

- 6.1. Devons-nous comprendre que lorsque la part des industriels dans les ventes d'HQD diminue, le risque d'HQD diminue aussi? Autrement dit, si la part des ventes aux industriels, dans l'élaboration des tarifs d'une

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

année donnée, est plus bas que la part des ventes aux industriels dans l'élaboration d'une année antérieure, doit-on conclure que le risque d'HQD a diminué à ce niveau entre ces deux années? Veuillez expliquer.

6.2. HQD subit-elle un manque-à-gagner lorsque les ventes aux contrats spéciaux sont moindres que prévu pour des raisons autres que climatiques?

6.2.1. Si oui, est-il du même ordre que celui subi lorsque la même situation se produit chez un client du tarif L?

6.2.2. Quel est l'impact, le cas échéant, de ce manque-à-gagner sur le *pass-on* et l'ajustement des contrats spéciaux?

7. Référence:

HQTD-1, Doc-1, page 15, ligne 11

Préambule

« [B]ien que le Distributeur puisse satisfaire ses besoins en énergie en ayant recours au contrat patrimonial, qui lui procure un approvisionnement de 165 TWh, il doit composer avec les incertitudes des contrats post-patrimoniaux qui prennent de plus en plus d'importance avec les années (possibilités de contestations, délais de réalisation) »

Questions:

7.1. Veuillez expliquer le lien entre ces « incertitudes » et le risque d'affaires du Distributeur.

7.2. Ces incertitudes peuvent-elles affecter le bénéfice net réglementé du Distributeur? Si oui, veuillez expliquer de quelle manière et l'ordre de grandeur du manque à gagner auquel HQD s'expose.

8. Référence:

HQTD-1, Doc-1, page 15, ligne 15

Préambule

Hydro-Québec traite *des risques associés à l'étendue de son réseau de distribution*. Nous comprenons qu'il invoque ici le même type de risque que celui

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

invoqué à l'égard du réseau de transport, à savoir la possibilité de voir son bénéfice net réglementé affecté négativement par des coûts imprévus reliés aux facteurs suivants : bris, défaillances, maintenance, dépannage, retrait d'actifs et autres facteurs mentionnés en réponse à 5.2.

Questions:

Par ces questions, nous cherchons à évaluer le risque lié à ces facteurs.

- 8.1. Notre compréhension est-elle correcte? Sinon, veuillez expliquer énumérant les autres facteurs, le cas échéant.
- 8.2. Quel est le plus important manque à gagner subi par HQD au cours de la période 2004-2012 en lien avec ces coûts? Le cas échéant, veuillez faire référence aux documents des rapports annuels du Transporteur sur le site internet de la Régie.
- 8.3. Avez-vous réalisé une étude de la variabilité de ces coûts ou sur le risque en lien avec ces facteurs? Si oui, veuillez la déposer.
- 8.4. Veuillez identifier, pour les années 2004 à 2012, le montant prévu aux revenus requis ainsi que le montant réel en ce qui a trait à ces coûts.

9. Référence:

HQTD-1, Doc-1, page 15, ligne 26

Préambule

« Le Distributeur encourt aussi un risque important en raison de la hausse des comptes en souffrance et de la diminution des ententes de paiement avec sa clientèle résidentielle en période hivernale. »

Question:

- 9.1. L'adoption d'une nouvelle méthode de calcul de la dépense de mauvaises créances dans le dossier R-3814 a-t-elle permis de réduire ce risque? Veuillez expliquer.

10. Référence:

HQTD-1, Doc-1, page 16, ligne 1

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

Préambule

« Enfin, il demeure que lors de l'établissement de ses tarifs, le Distributeur fait face au risque de ne pas se faire reconnaître l'ensemble de ses coûts, incluant un rendement raisonnable, et ce, malgré le fait qu'il bénéficie de comptes d'écart qui lui assurent une protection contre les fluctuations importantes d'éléments qui sont hors de son contrôle. »

Questions:

10.1. Considérant que la Régie rend généralement sa décision avant le 1^{er} avril de l'année pendant laquelle ses tarifs doivent s'appliquer, de quelle façon le bénéficiaire réglementé du Distributeur est-il à risque dans ce cas précis? Veuillez expliquer.

10.2. Vous dites que *le Distributeur fait face au risque de ne pas se faire reconnaître l'ensemble de ses coûts, incluant un rendement raisonnable*. Veuillez donner un exemple d'un dossier dans lequel la Régie aurait refusé de reconnaître un rendement raisonnable au Distributeur, et expliquer en quoi le rendement autorisé n'était pas raisonnable.

11. Référence:

HQTD-1, Doc-1, page 21, ligne 18

Préambule

« L'utilisation d'un même taux de rendement des capitaux propres pour les deux divisions réglementées est justifiable du point de vue d'Hydro-Québec par le fait que l'utilisation de structures du capital différentes prend en compte la différenciation du risque des deux divisions réglementées. Cette façon de procéder n'est pas nouvelle et est utilisée notamment en Alberta. »

Question:

11.1. Veuillez indiquer quelles entités sont réglementées de la sorte, en faisant référence aux décisions appropriées de l'*Alberta Utilities Commission*.

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

Troisième sujet – Autres propositions**12. Référence:**

HQTD-1, Doc-1, page 26

Préambule

HQ propose de mettre à jour le coût de la dette en même temps pour HQD et HQT, soit en décembre. À l'appui de cette proposition, HQ invoque la simplicité d'une telle démarche.

Questions:

- 12.1. À quelle fréquence HQ met-elle à jour les informations relatives à sa dette qui sont utilisées par HQT et HQD pour calculer le coût de leur dette?
- 12.2. Veuillez faire état des difficultés, le cas échéant, découlant d'une mise à jour à deux dates différentes, soit en décembre pour HQT et en mars suivant pour HQD. Si possible, veuillez quantifier la différence en nombre d'heures de travail additionnelles requises ou autrement.

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

Information Request addressed to Drs. Coyne and Trogonoski (Concentric)**First topic: Credit ratings****1. Reference:**

- (i) HQTD-2, Doc-1, pages 16-17
- (ii) <http://www.hydroquebec.com/investor-relations/about-financing/credit-ratings.html>

Preamble

- (i) Concentric Advisors (CA) refer to credit ratings by S&P, Moody's and DBRS. They also refer to a credit opinion by Moody's and a rating report by DBRS.
- (ii) Hydro-Québec presents credit ratings by S&P, Moody's, DBRS and Fitch.

Questions:

- 1.1. Why did you refer to credit ratings by S&P, Moody's and DBRS but not by Fitch?
- 1.2. At footnote 13 of reference (i), you refer to a credit opinion by Moody's dated August 6, 2012. We understand that this is the same report that you mention at page 27 of your report and that you filed in response to the Régie's request 1.1 on August 27.
 - 1.2.1. If not, please provide us with a copy of this document.
 - 1.2.2. Has Moody's issued a similar document since then in relation to HQ? If so, please provide us with a copy of this document.
- 1.3. At footnote 14 of reference (i), you refer to a rating report by DBRS dated April 12, 2012.
 - 1.3.1. Please provide us with a copy of this document.
 - 1.3.2. Has DBRS issued a similar document since then in relation to HQ? If so, please provide us with a copy of this document.

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

- 1.4. Please provide us with the latest credit opinions, rating reports or similar documents on Hydro-Québec by Fitch.
- 1.5. Please provide us with the latest credit opinions, rating reports or similar documents on Hydro-Québec by S&P.
- 1.6. The excerpts of DBRS's rating report that you quote discuss financial leverage and capital spending for Hydro-Québec at large, not just HQT. Considering the stand-alone principle, please explain how this would be relevant to the determination of HQT and HQD's ROE.

2. Reference: HQT-2, Doc-1, pages 26-28

Preamble

Your American proxy group is composed solely of companies with a credit rating from S&P of at least A-. This threshold is lower than Hydro-Québec's actual credit rating (A+). To support this, you claim that "*absent the government debt guarantee, the credit rating for Hydro-Québec would be several notches lower.*"

Questions:

- 2.1. What is the impact of Hydro-Québec's non-regulated activities (HQP, etc.) on its credit rating? Please quantify in terms of the S&P credit rating system.
- 2.2. Please define the terms "operating income" and "revenues" as used on page 28, lines 8 and 9 or your report.
- 2.3. Please quantify Hydro-Québec's "operating income" and "revenues" for 2011 and indicate where in its 2011 annual report this information is found.
- 2.4. Please quantify the share (in %) of Hydro-Québec's "operating income" and "revenues", respectively, that stem from regulated electric utility service for 2011.
- 2.5. For each company in your American proxy group and for Hydro-Québec, please indicate the share of company assets that are used for regulated electric utility service, in M\$ and as a percentage of total assets.

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

Second topic: Proxy groups**3. Reference: HQTD-2, Doc-1, page 23****Preamble:**

Your Canadian Utility Proxy group is comprised of six companies. You explain that “no specific screening criteria were used to derive the proxy group”.

Questions :

3.1. Canadian Utilities Limited (CUL) and ATCO are affiliated companies. Both of them are publicly-traded. Why did you choose CUL to be part of your proxy group instead of ATCO?

3.2. Besides the six companies in your proxy group and ATCO, are there other publicly-traded regulated Canadian electric or natural gas utility companies?

3.2.1. If so, why weren't these companies included in your proxy group?

4. Reference : HQTD-2, Doc-1, pages 24-25**Preamble:**

You mention that your US proxy group is a subset of a set of 48 companies that Value Line classifies as Electric Utility Companies. We understand that this subset is comprised of six companies which meet the seven criteria that you mention (credit ratings of at least A- from S&P, etc.).

Questions :

4.1. Please explain the rationale behind each of the seven criteria. When a criterion contains a specific limit or threshold (e.g. credit rating of at least A-, electric/regulated revenue above 60 percent, etc.) please explain why this specific limit or threshold was chosen.

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

4.2. Please provide the full list of all 48 companies that Value Line classifies as Electricity Utility Companies and mention, for each of the 48 companies, (i) its latest Beta according to Bloomberg and (ii) which of the seven criteria it meets. For the following criteria, please provide the following information for each of the 48 companies:

4.2.1. "Have credit ratings of at least A- from S&P": Please indicate actual credit rating from S&P, Fitch and Moody's

4.2.2. "Have earnings growth rates": Please indicate from how many industry analysts.

4.2.3. "Derived at least 60 percent of their revenue from regulated operations": please indicate the actual percentage of revenue derived from each of (i) electricity distribution and (ii) electricity transmission.

4.2.4. "Derived at least 60 percent of their regulated revenue from electric utility operations": please indicate the actual percentage of regulated revenue derived from each of (i) electricity distribution and (ii) electricity transmission.

4.2.5. "Are not considered a small capitalization company": please indicate the capitalization (in M\$).

4.3. For the credit rating criterion, why did you choose S&P instead of another agency such as Fitch or Moody's?

4.4. Who determines whether a company is considered "small capitalization" for the purposes of your analysis? What are the applicable criteria?

5. Reference: HQT-2, Doc-1, Exhibit JMC-3, Schedule 2**Preamble:**

You indicate an S&P credit rating for the operating companies of the publicly-traded proxy groups.

Questions:

5.1. Does S&P actually provide a credit rating for individual operating companies, or are these credit ratings those of the parent holding company?

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

5.2. Please provide the latest S&P, Fitch, Moody's and DBRS credit ratings (if applicable) for the companies of the third proxy group, i.e. government-owned electric utilities in Canada.

Third topic : Risk analysis

6. Reference: HQT D-2, Doc-1, section VII-A (Business risk analysis) and Appendix A

Preamble:

At page 43, you define business risk as “changes in revenues and costs that may result in variability in cash flows and earnings and the ability of the utility to recover its costs including the faire return on, and or, its capital in a timely manner.”

In the following pages, as well as in Appendix A, you compare HQD and HQT's risk levels to those of the proxy group members for the purposes of a ROE benchmarking exercise. You examine eight specific risk factors. However, in some cases, you focus on the protection measure instead of focusing on the actual risk, whether the underlying risk or the residual risk, once the protection measure is taken into account.

For example, at pages A-6 and A-7, you do not examine the variability in cash flows and earnings stemming from Volume/Demand risk; instead, you examine what types of protection or mitigation measures are in place.

Questions:

6.1. How does an analysis of protection measures allow you to draw conclusions as to the level of risk when you do not also examine the actual risk level (whether underlying risk or residual risk)?

6.2. Are we led to believe that the underlying risk is the same for all entities?

7. Reference: HQT D-2, Doc-1, p. 49, lines 6-7

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

Preamble:

“Specifically, HQD faces more competitive risk due to its higher concentration of industrial customers, which suggest that HQD is more susceptible to risks associated with economic bypass and demand destruction, as well as more vulnerable to weak economic conditions.”

Question:

7.1. How do you define the terms “economic bypass” and “demand destruction”?

8. Reference: HQT D-2, Doc-1, p. A-1**Preamble:**

Operating companies that (i) accounted for less than 10 percent of the total distribution customers of the parent company (ii) provided service within the same jurisdiction as a larger entity or (iii) provided regulated natural gas distribution service were excluded.

Questions:

8.1. Please provide a list of the companies that were excluded.

8.2. What is the rationale behind each of these three exclusion criteria?

8.2.1. Why did you establish the threshold at 10 percent of the total distribution customers?

8.2.2. How would the list of excluded companies change if you established the threshold at 10% of total energy sales instead of number of customers?

8.2.3. Please explain why you exclude natural gas distribution companies from this group and not from the Canadian proxy group?

8.3. How do you define the term “jurisdiction” in this context? Does it correspond to a political division (state, county, etc.), a company’s territory, etc.?

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

9. Reference: HQT-D-2, Doc-1, exhibit JMC-4, schedules 1 to 7**Preamble:**

These schedules provide information on certain risk parameters determined by HQT-D experts. For each parameter, an average is calculated using the number of customers to determine the weight of each company in the average.

Questions:

- 9.1. Please provide an Excel (.xls or similar) version of these schedules.
- 9.2. In this Excel version, please add another column to these tables indicating total energy sales (in kWh) and total assets (in M\$) for each operating company.

10. Reference: HQT-D-2, Doc-1, page A-2 and exhibit JMC-4, schedule 1**Preamble:**

This schedule distinguishes companies with (i) regulated generation (ii) limited regulated generation and (iii) no regulated generation.

Questions:

- 10.1. At page A-2, you mention that “11 percent of those companies own limited generation, such as renewable resources like solar, wind and biomass”.
 - 10.1.1. What exactly are the criteria that you used to distinguish between “regulated generation” and “limited regulated generation”?
 - 10.1.2. Under which category would HQD fall with its “very limited diesel generation”?
- 10.2. For each company, please indicate the share that regulated generation occupies in relation to the total yearly energy needs (for sales to customers, losses, etc.) of this company.

11. Reference: HQT-D-2, Doc-1, page A-4, lines 8-13

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

Preamble:

“Similarly, all of the operating utilities in the U.S. electric utility proxy group have fuel cost recovery mechanisms that allow them to pass through fuel and purchased power costs to customers, where applicable. As such, the operating companies in the Canadian and U.S. proxy groups are not at risk for differences between the projected and actual cost of fuel with the exception of [Wisconsin and Nova Scotia Power]...”

Questions:

- 11.1. For each company in the Canadian and U.S. proxy groups, please describe the “cost recovery mechanisms” in place, if applicable.
- 11.2. Please confirm that each of these “cost recovery mechanisms” allow the operating company in question to recuperate any variance between projected fuel and power costs on which rates are based and actual costs and that therefore these costs cannot lead to overearnings or under-earnings by the company (i.e. no impact on real ROE). If not, please explain.
- 11.3. Please describe what costs are recovered by companies that have regulated generation.

12. Reference: HQT D-2, Doc-1, page A-4, line 15

Preamble:

“While HQD has more protection with respect to the price stability of its electricity supply, the Canadian and U.S. proxy group companies have protection with regard to recovery of fuel or purchased power costs.”

Questions:

- 12.1. Doesn't HQD also have protection with regard to recovery of fuel and purchased power costs?
 - 12.1.1. If so, what is the purpose of this statement?

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

13. Reference: HQTD-2, Doc-1, page A-5, line 14

Preamble:

“Since HQD has little risk associated with variations in fuel or purchased power cost...”

Question:

13.1. Please describe HQD’s risk associated with variations in fuel or purchased power cost.

14. Reference: HQTD-2, Doc-1, page A-6/A-7 and JMC-4, Schedule 3

Preamble:

You mention that 62% of the operating companies in the Canadian proxy group have RDMs or LRAMs, and 11% have weather normalization adjustment clauses or variance accounts. This leads you to conclude that HQD has “*somewhat less protection against changes in volume/demand than the operating companies in the Canadian proxy group*”.

You mention at JMC-4, schedule 3 that 9,25% of the Canadian operating companies have RDM’s and 52,66%, LRAM’s. In other words, about only 20% of the Canadian operating companies (using your terminology) have RDM’s or weather normalization instruments, yet this leads you to conclude that “*HQD has somewhat less protection against changes in volume/demand risk than the operating companies in the Canadian proxy group*”.

Questions:

14.1. What are “weather normalization adjustment clauses” and how do they relate to “weather-related variance accounts”?

14.1.1. Please specify how and to what extent they protect the operating company.

14.2. How do LRAM’s compare with weather-related variance accounts in terms of risk protection?

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

14.2.1. Should we understand that in your view, Canadian operating companies with an LRAM but no RDM or weather variance account would have, all else being equal, somewhat more protection against changes in volume/demand risk than HQD?

14.3. Generally, how did you compare the volume/demand risk of the different operating companies (including HQD) that face different risks (the weather risk may not be the same everywhere) and have different mechanisms (LRAM's etc.)?

15. Reference: : HQTD-2, Doc-1, pages 41-42 and A-7 to A-9

Preamble:

At pages A-7 to A-9, you discuss HQT's risk and compare it to that of other transmission providers. However, the purpose of your risk analysis, as mentioned at pages 41-42, is to "examine whether it is reasonable and appropriate to use Canadian and U.S. Proxy groups to establish the allowed ROE for HQD and HQT", and whether any adjustments should be made.

Questions:

15.1. Why are you not comparing HQT to the proxy groups in terms of volume/demand risk as you are doing for HQD?

15.2. Using the same methodology as for HQD (i.e. JMC-4, schedule 3), how does HQT compare with the proxy groups?

15.3. Why do you say "HQT is not exposed to risks associated with changes in demand" at page A-7, line 17, and then begin the next paragraph by saying that "Other transmission companies in the Canadian proxy group also have little risk with respect to fluctuations in demand"?

16. Reference: HQT-D-2, Doc-1, page A-10, line 2

Preamble: *"Capital spending is a two-edged sword for utilities. On the one hand, capital spending support dividend growth and share price appreciation; on the other, it can increase the need for external financing and place pressure on cash flows and credit metrics without ongoing accommodation in rates for system expansion."*

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

Question:

- 16.1. Please elaborate on this. Please explain exactly in what ways capital spending is a risk factor.
- 16.2. Assuming that a regulator approves 100% of capital spending before it is spent by the utility, how could capital spending affect the utility's business risk, or, as you define it, "*variability in cash flows and earnings and the ability of the utility to recover its costs including the faire return on, and or, its capital in a timely manner*"

17. Reference: HQTD-2, Doc-1, pages A-11-A-12

Preamble:

“Q. Why do equity investors and credit rating agencies prefer utilities that are allowed to earn a cash return on CWIP rather than AFUDC?”

Investors may be concerned that (1) multiple capital projects will place pressure on the company's cash flows and credit metrics during construction, (2) any project delays will further postpone cost recovery and (3) some portion of costs in excess of any pre-approved amounts may be deemed imprudent.

(...)

Therefore, from an investment and cash flow perspective, the opportunity to earn a cash return on CWIP is favorable, especially for large capital projects that are not expected to be completed for several years because it (1) provides more immediate cost recovery, (2) reduces pressure on cash flows and credit profiles during construction, and (3) reduces concerns about rate shock.”

Questions:

- 17.1. How do pressure on the company's cash flows and credit metrics, postponement of cost recovery and concerns about rate shock constitute business risks or affect business risks?
- 17.2. Assuming that, for a given project due to be in service on April 1st of a given year, HQD or HQT is granted pre-approval in time for this project to be included in that year's rate base, but this project is not put into

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

service until December 1st of the same year, how would this delay postpone cost recovery?

18. Reference: HQTD-2, Doc-1, Page A-14, line 3

Preamble:

“Based on Concentric’s research and analysis, our view is that HQD and HQT generally have comparable risk mitigation for capital cost recovery as the Canadian proxy group because regulated utilities in Canada file rate cases on a more frequent basis, meaning that utility companies are able to include capital investments in rate base once they are placed into service and start earning a return on those investments without significant regulatory lag. In addition, HQD and HQT receive pre-approval of capital expenditures (including specific approval for major projects), whereas many of the Canadian utilities do not. With respect to the operating companies in the U.S. electric utility proxy group, Concentric concludes that even though those U.S. companies generally do not file rate cases as frequently as those in Canada, they have similar or better risk protection on this factor as HQD or HQT through either approval of CWIP in rate base while the plant is under construction, or implementation of cost tracking mechanisms that provide accelerated recovery of capital costs for replacing aging infrastructure.”

Questions:

- 18.1. When you say “regulated utilities in Canada file rate cases on a more frequent basis”, do you include HQD and HQT in this group of regulated utilities in Canada, and who are you comparing this group to?
- 18.2. Considering that HQD and HQT can have their projects pre-approved, which is a factor on which Moody’s “places a high degree of emphasis” according to the quote on page A-10, and considering that 32% of the operating companies in the US may not request such pre-approval, how do you come to the conclusion that US Companies have similar or better risk protection on capital spending as HQD or HQT?
 - 18.2.1. How do you compare different protection measures (e.g. pre-approval vs. CWIP in rate base)?
 - 18.2.2. How does your “yes/no” analysis provide an accurate measure of business risk, i.e. an accurate measure (in \$ or %) of

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

“variability in cash flows and earnings and the ability of the utility to recover its costs including the faire return on, and or, its capital in a timely manner”?

19. Reference: HQTD-2, Doc-1, p. A-14-A-17

Preamble:

On other risk factors, you generally draw a conclusion as to whether HQT and HQD face more, less or as much risk as the operating companies of the proxy group. On this particular risk factor, you seem to conclude that HQT and HQD face less risk than both proxy groups since:

- (i) You mention that “[i]n general, as observed by DBRS, any change from cost-of-service regulation is considered an increase in risk for the utility”;
- (ii) Both HQD and HQT operate under traditional cost-of-service regulation; and
- (iii) According to your analysis, only 24% of the Canadian group and 42% of the American group operate under cost-of-service. We understand from your response 10.1 to the Régie’s request for complementary evidence that these numbers may have changed since then but are still well below 100%.

However, you do not explicitly mention this conclusion.

Questions:

- 19.1. Is this correct?
- 19.2. If so, why did you not provide a specific and explicit conclusion as you did for other risk factors?
- 19.3. What is the impact of this conclusion on your general conclusion regarding HQT and HQD’s risk as compared to that of the proxy groups? On HQT and HQD’s ROE?

20. Reference: HQTD-2, Doc-1, page A-17-20 and Exhibit JMC-4, schedule 6

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec
et à Concentric Advisors
R-3842-2013

Le 17 septembre 2013

Preamble:

Regulatory lag

At pages A-19 to A-20, you mention that *“With respect to interim rates, HQD has somewhat more risk than the operating companies in the Canadian proxy group, and more risk than the operating companies in the U.S. electric utility proxy group, the vast of which have the ability to request interim rates”*.

At Exhibit JMC-4, schedule 6, you indicate that the rate case lag, which you define as *“the time between when a rate case is filed and when the decision is issued”* as 10 months for HQT.

Questions:

- 20.1. Does HQD experience regulatory lag? Please explain.
- 20.2. Since 2004, has the Régie ever rendered a final decision establishing HQD’s rates later than the date upon which these rates are set to come into effect, i.e. April 1st?
- 20.3. What is the purpose of interim rates when rates are reset every year at a given date, with the rate case beginning well in advance of this date?
- 20.4. How did you derive the 10-month duration for HQT rate cases?
 - 20.4.1. Is this based on historical duration of rate cases? If so, which cases were considered?

21. Reference: HQT-D-2, Doc-1, Pages A-20 to A-22**Preamble:**

Cost recovery mechanisms

Questions:

- 21.1. Please explain in greater detail how the following mechanisms function, and indicate, for each, if they shield the utility from over or under-earnings (for the specific cost or risk that they cover) or otherwise

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

ensure that it will recover its costs including the faire return on, and or, its capital.

Variance accounts
Rate riders
Surcharges
Cost tracking mechanism

For each type of cost recovery mechanism, please provide an example of such a cost recovery mechanism using HQT and HQD, or, failing that, from one of the utilities in the proxy groups (with reference to relevant regulatory documents).

- 21.2. For each type of cost recovery mechanism mentioned at table 13, please indicate (i) what risk is covered and (ii) any material differences (if any) between the specific mechanisms of the different operating companies (including HQT and HQD where applicable), notably whether the different mechanisms shield the utility from over or under-earnings (for the specific cost or risk that they cover) or otherwise *ensure that it will recover its costs including the faire return on, and or, its capital.*

22. References: HQT-D-2, Doc-1, Pages A-22 and A-23

Preamble:

“HQD faces more competitive risk due to its high concentration of industrial customers in Québec, which makes HQD more vulnerable to longer-term risk associated with an economic downturn that could cause those industrial customers to reduce their demand for electricity (...)”

Questions:

- 22.1. Please indicate in what way a potentially lower demand from industrial customers in the future represents a long-term business risk for HQD
- 22.1.1. Would this bring a *variability in cash flows and earnings*? If so, please explain how this would be detrimental to HQD.

AQCIE/CIFQ

Demande de renseignements numéro 1 à Hydro-Québec

et à Concentric Advisors

R-3842-2013

Le 17 septembre 2013

- 22.1.2. Would this be detrimental to HQD's *ability to recover its costs including the faire return on, and or, its capital in a timely manner*? Please explain.
- 22.2. Assuming that HQD derives a lower share of revenues from industrial in 2013 than it did at the time of its first rate case, when its ROE was set for the first time by the Régie, does this mean that this specific risk has since then been reduced? Please explain.

23. Reference: HQTD-3, Doc-1, Pages 27-28

Preamble:

At tables 13.1 and 13.2, the Régie provides a detailed account of HQD's and HQT's over or under earnings for the period 2007-2012 which HQ has indicated is correct. We find that since 2009, overearnings have been significant, at 97.6 M\$ for HQT and 122.4M\$ for HQD per year, on average.

Considering their respective rate bases in 2012 - roughly 17G\$ for HQT and 10G\$ for HQD - and the deemed equity in place (which you recommend maintaining) at 30% for HQT and 35% for HQD, these average over-earnings translate into an ROE "premium" of 1.9 percentage points for HQT and 3.5 percentage points for HQD.

Questions:

- 23.1. Did you take this into consideration in your risk analysis? Please explain.
- 23.2. Would you agree that a regulated utility that systematically has over-earnings of this magnitude has very limited short-term risk? Please explain.