First Topic: Risk assessment framework

Reference: Company evidence page 9

Preamble:

The company discusses three main sources of risk: income risk; regulatory risk and financial risk.

Question 1:

1.1 Please provide a table for both HQT and HQD with the annual allowed and earned ROE from 2001-2012 so that actual performance can be viewed in one document.

1.2 Please confirm that financial risk is captured in the earned ROE, since the ROE is after the payment of fixed interest charges, ie. reflects the financing of each division. If not please explain why not.

1.3 Please confirm that business risk for a non-regulated firm is normally captured in either earnings before interest and tax (EBIT) or earnings before interest tax and depreciation (EBITDA) since these measures capture earnings before taking into account how a firm is financed, that is, financial risk. If not why not.

1.4 Please confirm that regulatory risk also shows up in a utility's ability to earn it's allowed ROE, that is, firms lacking regulatory protection in terms of deferral accounts and frequent rate hearings are less likely to earn their allowed ROE than ones with significant regulatory protection? If not please explain why not.

1.5 Please discuss any significant deviations from the allowed ROE provided in answer to 1.1 above for both HQD and HQ. Please define what HQD and HQT would judge to be a significant under-earning relative to the allowed ROE.

1.6 Normally business risk is judged to have both a short run and a long run dimension. Short run is the income risk discussed above, whereas long run risk is the risk of fundamental changes in the supply and /or demand for the product being transported and/or distributed. Is the fact that Hydro Quebec does not mention this risk an acceptance that such risk does not exist or is not material for either HQT or HQD? If not please discuss in detail why such risks have not been discussed.

1.7 Please provide the average economic life of the assets of both HQT and HQD and copies of the last depreciation studies filed with the Regie. Have there been any material changes in the economic useful life over the last ten years for either HQD or HQT?

Second Topic: Business Risk

Reference: Company evidence pages 10-13

Preamble:

The company discusses in a general way the risks faced by HQD and HQT.

Question 2:

2.1 Would HQD and HQT agree that ultimately the risk for both utilities is derived from the demand and supply of the underlying product being transported and distributed? If not, why not.

2.2 Please provide any studies that either HQD or HQT have relied on that estimate the sensitivity of the demand for electricity to income and its own price.

2.3 Please provide the income and revenue breakdown for HQD in terms of industrial, commercial and residential for each year since 2001 and whether HQD regards any changes as being material.

2.4 Please provide a cost comparison for the types of users in 2.3 above and the fuel source that HQD regards as most competitive, for example, fuel oil, natural gas etc.

2.5 Please provide the data in 2.4 for 2001 and 2007 and discuss whether in the judgment of HQD there has been a material change in the competitive potion of electricity in Quebec.

2.6 Please provide a cost comparison of electricity with natural gas (or any more competitive fuel) for residential customers in BC (Fortis Energy BC (FEI)), Alberta (Atco Gas) and Ontario (Enbridge Gas Distribution (EGDI)) and discuss whether electricity in Quebec has a greater or lesser competitive advantage over alternative fuels.

2.7 Please confirm that the Regie allows Gaz Metropolitain a higher total equity ratio (common plus deemed preferred shares) at 46% than the OEB allows EGDI and Union Gas (36%), the AUC allows Atco gas (39% or the BCUC allowed FEI (38.50%).

2.8 Please confirm that the higher risk profile of Gaz Metropolitain relative to other large gas distributors in Canada can alternatively be viewed as the lower risk profile of HQD. If not please explain why not?

Third Topic: Fair ROE

Reference: Company evidence pages 15-16

Preamble:

Hydro-Quebec defines the stand alone principle as treating the utility "as if it were seeking to attract capital on the financial markets independently from the rest of the enterprise to which t belongs."

Question 3

3.1 Please provide a justification for this definition of the stand-alone principle.

3.2 Please confirm that in economic terms the stand alone principle simply means that the consumer pays minimum average cost determined without the impact of subsidies or excessive (uneconomic) costs imposed by its owners. That is, regulation is designed to mimic the act of perfect competition and remove the impact of market power

3.3 Please confirm that Hydro-Quebec's owner is the Province of Quebec and indirectly the people of Quebec and indicate all major policy actions by the province that have directly or indirectly instructed Hydro Quebec to take uneconomic actions in the public interest.

3.4 Please indicate the charge the Province of Quebec levies on Hydro Quebec in return for the provincial guarantee of its debt. Would Hydro Quebec judge this to be a violation or confirmation of the stand-alone principle?

3.4 Further to 3.3 above please indicate the current debt cost to Hydro Quebec as the cost of the Provincial guarantee charge plus the current Province of Quebec yield spread over the 30 year long Canada bond yield (Cansim V39056), relative to the current thirty year utility yield spread using the Bloomberg utility yield (C29530Y) and the 30 year Government of Canada bond series (Cansim V39056). Please provide these two spreads for each month since June 1, 2013.

3.5 3Further to 3.4 please provide the same utility spread for the following major utilities since June 1: Enbridge Gas Distribution (EGDI), Canadian Utilities, Fortis Energy Inc (FEI), Union Gas and Gaz Metropolitain.

Fourth Topic: Capital structure Differences

Reference: Company evidence page 16

Preamble:

Hydro-Quebec indicates that a 30% common equity ratio for HQT and 35% for HQD are appropriate based on their risk differences.

Question 4

4.1 Please confirm that Hydro Quebec is asking for the same ROE for both HQD and HQT of 9.20% and it judges the differential common equity ratios to totally adjust for the risk differences.

4.2 Please confirm that Hydro Quebec no longer judges HQD to warrant a 0.12% higher ROE than HQT (page 14 of company testimony).

4.3 Since the risk compensation for HQD relative to HQT is reduced (no ROE premium but same higher common equity ratio) please indicate all factors that lead to this decline in relative risk assessment for HQD relative to HQT.

Fifth Topic: Earnings Sharing mechanism

Reference: Company evidence page 17

Preamble:

Hydro-Quebec seeks a 1.0% dead-band for HQD and 0.50% for HQT.

Question 5

5.1 Please confirm that Hydro Quebec is not seeking performance based regulation for either HQT or HQD?

5.2 Please provide the average excess of the actual versus the allowed ROE for both HQD and HQT from the answer to 1.1 above.

5.3 Please indicate the average $ amount that HQD and HQT would have “kept” had its requested earnings sharing mechanism been in effect since 2001.

5.4 Please confirm that the bulk of the excess earnings are due to under-spending of expenses as indicated in the Regie’s additional request #13, Tables 13.1 and 13.2 rather than to efficiency gains.

5.5 Please indicate what controls Hydro Quebec is putting in place to prevent the persistent under-spending of requested expenses in the future should the Regie approve the requested dead-bands.