
**ÉNERGIR, L.P.'S RESPONSES (ÉNERGIR) TO
REQUEST FOR INFORMATION NO. 13 FROM THE RÉGIE DE L'ÉNERGIE (RÉGIE) TO ÉNERGIR
RELATING TO THE GENERIC FILE ON COST ALLOCATION
AND RATE STRUCTURE**

- 1. Reference:** (i) Exhibit [C-OC-0047](#), line 19;
(ii) Exhibit B-260, Excel file, tab GM9 doc4-Q7.1 SMACII.

Preambles:

(i)

	Evaluation Methods and Common Inputs	Gaz Métro Proposal (Black & Veatch)	OC	ROEÉ
19	Mains	2.254% (equivalent to 44 year life)	Agree with Gaz Métro - but risk of shorter useful life identified by ROEÉ is one factor considered in OC's higher threshold P. I. for portfolio	3.33% (30 years) B-0258, OC 7.2

The Régie understands that Énergir's proposal for mains is to apply, in the evaluation method, an amortization rate corresponding to that used by the distributor in its required revenue of 2.254%, equivalent to an amortization over 44 years, for the mains over a 40-year project evaluation period. For its part, the ROEÉ proposal consists in applying a mains amortization rate based on the project evaluation period (i.e. $100\%/30 \text{ years} = 3.33\%$).

(ii) Énergir presents an Excel file containing the details of the calculations of a profitability analysis. The Régie observes that the cash flow associated with the project does not contain amortization of capitalizable expenses but rather all the capitalizable costs in year 0. The rate impact uses the amortization rates of the capitalizable expenses based on the useful life of the assets.

Request:

- 1.1 Using the Excel file in reference (ii), please illustrate the impact of Énergir's proposal and the ROEÉ proposal on the IRR, PI and rate impact on the assumption that the project evaluation period is 20 and 40 years. Please comment on the results of the different approaches. Please submit your results as an Excel file.

Answer:

The following table summarizes the results of economic and rate analysis for the project in reference (ii). The Excel file supporting these results is provided in Appendix Q-1.1.

Période d'amortissement des conduites : 44 ans (2,254%)

Horizon d'analyse	40 ans	30 ans	20 ans
TRI	3,11%	1,90%	-1,19%
Indice de profitabilité	0,76	0,68	0,54
Impact tarifaire (\$)	42 280	48 437	53 113

Période d'amortissement des conduites : 30 ans (3,333%)

Horizon d'analyse	40 ans	30 ans	20 ans
TRI	3,29%	2,10%	-0,98%
Indice de profitabilité	0,78	0,69	0,55
Impact tarifaire (\$)	41 298	56 426	63 252

The ROEÉ proposal to shorten the booked depreciation period for mains by making it equal to the suggested 30-year analysis horizon would have a major effect on the rate impact for customers if it was applied on an accounting basis and they would be subject to a substantially higher depreciation expense in the service cost during the first 30 years (although that increase would be offset by the reduction in the tax on public services and the rate base return). However, it is important to note that the rate impact of that shorter depreciation period is only theoretical because it definitely does not correspond to reality since the mains depreciation period would not actually be shortened to 30 years in Énergir's accounting practices. Separate treatment for specific assets in specific projects or markets would move Énergir away from the concept of homogenous asset classes by introducing exceptional cases that would have to be treated differently. The updates to the depreciation rate study approved regularly by the Régie provide a reasonable guarantee that adjustments will be made over time based on the periodic evaluation of the assets' expected actual lifespan.

Moreover, since depreciation is not a cash flow, and all things being equal, the impact on the IRR and PI would be slightly positive for an equivalent analysis horizon. A change in the depreciation expense would affect the IRR and PI only indirectly via an adjustment in the tax on public services and income taxes. However, the suggested reduction in the analysis horizon from 40 to 30 years would reduce the IRR and PI by removing many years of positive net revenue from the cash flow.

It is important to note certain elements:

- ♦ The Excel-format profitability calculation tool, commonly referred to as the “required income tool,” has two separate purposes. This tool, which has been used for many years, makes it possible, on the one hand, to evaluate the internal rate of return generated by a project (and PI), and on the other hand, to evaluate the rate impact and break-even point of the same project, hence the name “required income tool.” Its main purpose is to determine the revenue needed in order to recover the costs associated with a new project, compare that required revenue against the project’s forecast revenue and quantify the new investment’s upward or downward impact on rates. As a result, the profitability calculation software is directly aligned with Énergir’s required revenue determination method from the rate file (R-3987-2016, B-0288, Gaz Métro-12, Document 1), using depreciation periods based on a pool of assets (R-3879-2014, B-0466, Gaz Métro-107, Document 11). These two types of analysis (IRR/PI and rate impact) have been combined to ensure consistency. That is why the booked depreciation period is the same whether the rate impact or the project’s economic impact is being calculated.
- ♦ To measure a project’s rate impact as accurately as possible, the booked depreciation used in the analysis must therefore be as close as possible to the actual depreciation expense associated with the project under Énergir’s depreciation policies. It should be noted in this regard, as explained in various responses to requests for information in this file, that the depreciation rates are determined according to a rate study that Énergir conducts every five years in cooperation with an expert. The study of depreciation rates considers, among other things, the fact of being in a pool of assets: for each category of fixed assets, there are assets acquired for several years (already in use) and new assets that are added annually. The average useful life of all these assets (old and new) is calculated to establish the depreciation period of the class.
- ♦ Booked depreciation is one of the major components of a project’s service cost and, in that respect, any change to a project’s depreciation period has a direct rate impact on customers. A change in the depreciation period also has an impact on how the rate base associated with a project evolves over time and therefore directly impacts the return on that rate base, the project’s income taxes payable and the tax on public services (which depends on the assets’ net book value); those three other service cost components are used in calculating the rate impact.
- ♦ When it comes to the economic evaluation, since booked depreciation is not a cash flow, a change in the depreciation period has only an indirect impact on the IRR and PI through the tax on public services and income taxes.

Énergir believes that modifying the booked depreciation period without taking into account the recognized practices currently in effect would negatively affect the quality of a project's rate impact evaluation and would also skew the economic evaluation, including the cash flow that must be as close as possible to Énergir's economic reality in order to be credible. The depreciation period for mains is a key parameter that should only be modified to reflect the accounting practices in effect. Any other approach could negatively affect the credibility of the economic and rate analyses.

2. **Reference:** Exhibit [B-0281](#), p. 9, response to question 8.1.

Preamble:

“8.1 Please clarify the exact amount of the budget planned for industrial park and road repaving projects.

Answer:

Gaz Métro clarifies that it put in place a budget of approximately \$1.5M which will be accessible in order to reach a PI of 0.8 for industrial park and road repaving projects which have an expectation of future densification. This budget can be revised each year and will be established during the rate case. Gaz Métro reiterates that this budget will be drawn from the overall profitability of the development plan.”

Request:

2.1 Please comment on the desirability of the exceptions (industrial parks and road repaving or other projects) being limited to a fixed amount that would be based on the overall profitability surplus observed in the last annual report.

Answer:

In Énergir's view, the proposal to allow exceptions based on a fixed amount according to the previous year's overall profitability is more complex and less practical than Énergir's proposal. The profitability surpluses indicated in the annual report would likely require a new deferred expense account (DEA) to be created in order to finance the following year's exceptional case projects. In addition, that method would prevent the distributor from adjusting the exceptional cases budget according to the identified needs and the projected profitability in the rate file's development plan and the profitability determined during the year in the actual development plan.

In addition, Énergir would like to refer the Régie to the replies to questions 7.1 through 7.7 as well as 15.7 of Request for Information No. 12 from the Régie (B-0378, Gaz Métro-9,

Document 17) concerning clarifications about the treatment for industrial parks and road repaving. Énergir prefers its proposal, as explained in the reply to question 7.1, which refers in particular to the fact that:

“During each rate case, Énergir will propose a budget based on an estimate of needs which will be based specifically on the future and the prospective information available. Budgeting should also ensure that the overall development plan achieves a profitability index greater than or equal to 1.1. This budget could thus vary from one year to another depending on the estimate of needs and the overall profitability level of the provisional development plan.

During the year, the sums will be used so that repaving and industrial park projects, which have an expectation of future densification and which have an IP of less than 0.8, will reach an IP of 0.08. The setting of an annual budget, which is an internal governance measure, allows Énergir to contain the downward marginal impact on the overall profitability of projects with an IP of less than 0.8. Note that despite the setting of a budgetary amount, the actual evolution of profitability during a year could affect its use. Indeed, the development plan must reach an overall profitability index greater than or equal to 1.1, which can influence the amounts invested in repaving and industrial park projects. For example, if in a given year, the sales plan was at risk of not reaching the minimum IP of 1.1, the actual sums used for repaving and industrial park projects will have an IP of less than 0.8 could be lower than the budget estimate.”

Appendix Q-1.1 is a separate Excel file.