

REQUEST FOR INFORMATION NO. 10 FROM THE RÉGIE DE L'ÉNERGIE (THE RÉGIE)
CONCERNING THE APPLICATION RESPECTING COST ALLOCATION AND RATE STRUCTURE

Marginal costs that may be affected when customers move

- 1. References:**
- (i) Exhibit B-0230, p. 3;
 - (ii) Exhibit C-ROEE-0082, p. 25;
 - (iii) Exhibit C-OC-0023, p 6 to 7;
 - (iv) Exhibit C-OC-0023, Exhibit WM-2, p. 1 and 2.

Preamble:

(i) *"The issue of opening a billing file in years subsequent to the first year appears to be in dispute as well. It seems that the dispute is based on an argument about what happens when a new occupant of a premise causes a customer connection after year one. In the analysis it is assumed that year one applies to the customer not the premise. Where that is the case there should be no dispute over the zero value for first year costs in subsequent years."* [emphasis added]

(ii) *"[...] Every time a new customer moves into the building or unit, Gaz Métro will incur the cost of opening a billing file, setting up a new contract, and conducting a credit check (for non-residential customers). Gaz Métro should develop estimates of the rate of customer turnover by class of market, so that can include multiple events in the profitability analyses."* [emphasis added]

(iii) *"When a line extension is involved (instead of an attempt to charge money to each customer who moves), suddenly the marginal cost becomes only \$9.66 for the new applicant and nothing for any future customers. We will add the \$9.66 multiplied by 10% of customer as an ongoing long-run marginal cost for both residential and CII customers."*

(iv) Table of costs proposed by OC, for the residential sector and CII.

Requests:

- 1.1 Please explain Gaz Métro's position (Reference (i)) in relation to the "cost of opening a billing file", the "cost of setting up a new contract" and the "cost of conducting a credit check" for customers other than residential customers, that are incurred when the same customer moves (References (i) and (ii)).

Response:

Dr. Overcast is of the opinion that: “Both Mr. Marcus and Mr. Chernick are incorrect in their analysis of one-time costs. It is not efficient to consider multiple occupancy as a marginal cost of a new connection and to require the current customer to be responsible for those future costs that the customer does not cause. Marginal cost is correctly defined as the additional costs of inputs to produce the output – in this case customer connection, thus a change in occupant does not create a change in the output produced.”

Gaz Métro shares Dr. Overcast’s opinion. The proposed profitability analysis should not consider events and costs that are unknown when connection is requested. The contamination of an analysis by the addition of such costs would artificially reduce profitability for certain projects, limiting their potential for completion, which would have an adverse effect on existing customers since an erroneous and overstated marginal cost would inhibit volume growth and therefore limit possible rate reductions for existing customers.

- 1.2 Please comment on the OC expert's estimate of the cost of opening a billing file for relocations of the same residential or CII customer as of the second year (References (iii) and (iv)).

Response:

As a complement to the response to request 1.1, after reading Mr. Marcus’ report filed as Exhibit C-OC-0023 (pages 6 and 7), Gaz Métro questions his interpretation of the data. He cites cost estimates to turn meters on and off for both residential and CII customers. Gaz Métro submits that Mr. Marcus’ calculation is inappropriate since it does not reflect Gaz Métro’s business practice described in its proposal presented in the 2012 Rate Case. In addition, without more specific information about actual turnover in Gaz Métro’s customer categories, which is not available, the quality of Mr. Marcus’ estimate is questionable. That said, Gaz Métro reiterates that since the analysis of a project’s profitability should not consider events and costs that are unknown when connection is requested, it is inappropriate to include costs related to customer turnover.

**Marginal costs for processing CRP grant applications and for the inspection
and maintenance of meters**

- 2. References:**
- (i) Exhibit B-0144, Schedule 1 of Schedule A, p. 1 to 3;
 - (ii) Exhibit B-0209, Schedule 1, p. 1;
 - (iii) Exhibit B-0145, p. 9 to 11.

Preamble:

- (i) Tables of long-term marginal costs proposed by Gaz Métro for all markets.
- (ii) Explanatory table of certain weighted costs by market.
- (iii) Tables of long-term marginal costs proposed by Gaz Métro and by Black & Veatch.

Requests:

- 2.1 The Régie notes that unlike other costs allocated to all customers, such as the costs of bad debts, the minimum thresholds for marginal costs associated with processing a CRP application for the first and subsequent years in the residential and CII markets, is zero (reference (i)). Please explain this treatment.

Response:

The method proposed by Gaz Métro applies a marginal cost to each customer corresponding to the customer's specific characteristics. As noted in reference (ii), those characteristics are:

- type of market;
- type of meter;
- corrective instruments and telemetry;
- CRP application;
- addition of a cellular line; and
- length of line.

Thus, if a customer applies for CRP, its marginal cost for the purpose of the profitability analysis will contain the marginal cost associated with the preparation of a CRP application, i.e. \$23.83 for residential and \$32.90 for commercial, and if there is no CRP application, that cost will be 0, which is why a minimum of zero is given.

- 2.2 Please explain why costs for processing a CRP application vary between zero and \$23.83 for the residential market and from zero to \$32.90 for the CII market, for both the first and subsequent years (Tables 1 and 2 of reference (i)), given that their weightings (reference (ii)), are, respectively, 85% and 62%. Also, please explain why Gaz Métro did not apply the cost indicated in reference (ii), namely \$20.26 for the residential market and \$20.40 for the CII market (reference (ii)), for both the first year and subsequent years.

Response:

With respect to weighted costs (e.g. \$20.26 for residential and \$20.40 for CII), Gaz Métro explained in its initial proof that the weightings used were only to evaluate the method's impact on the development plan's overall profitability. The method proposed by Gaz Métro applies a marginal cost to each customer corresponding to that customer's characteristics. Thus, if a residential customer applies for CRP, its marginal cost will include a cost of \$23.83 whereas the marginal cost for a customer who does not apply for CRP will not include that cost. This is binary data for which there are only two options—zero or the cost.

This method aims to apply specifically to each customer the marginal costs they cause. Use of a weighted cost, namely the cost noted in reference (ii), does not give the same precision.

- 2.3 Please confirm that no CRP grant application was accepted for line extension projects for the MIS sector. If this is not so, please explain why that cost was considered to be zero in the Distributor's analysis (Table 3 of reference (i)).

Response:

CRP applications for new MIS customers are rare. No data is therefore available regarding their processing time and the cost could not be calculated.

- 2.4 The Régie notes that inspection costs for the "*spin test for turbine (less than 12 in)*" vary between zero and \$79.20 for the CII and residential markets. However, in the MIS market, those costs vary inversely, namely from \$79.20 to zero (Table 3 of reference (iii)). Please explain and, if necessary, correct.

Response:

In its initial proof, Gaz Métro indicated:

[Translation] “Inspection of meters and corrective instruments

The maintenance plans vary depending on the type of meter and measuring instruments installed at the customer’s premises. The costs shown in the maximum threshold represent equipment with greater capacity and more complex technology which may be installed in each market. The maximum cost for residential and CII is therefore the cost associated with a less than 12-in turbine whereas for MIS it is a 12-in or more turbine.”¹

In the response to request 1.1 of the Régie’s Request for Information No. 5, Gaz Métro indicated:

[Translation] “Also, in establishing minimum and maximum thresholds, certain assumptions were used for the different markets.

- Although the meter showing the highest inspection costs is the 12-in or more turbine, the maximum shown by Gaz Métro in the table for the residential and CII markets is a less than 12-in turbine since it is very unlikely that a customer in these markets would have a sufficiently high consumption volume to justify installing a larger format turbine. [...]”²

Thus, when preparing table 3 of reference (iii), the assumption used for MIS customers is that the meter installed for this type of customer would be a less than 12-in turbine or 12-in or more turbine. The minimum cost for the spin test would therefore correspond to that of a less than 12-in turbine (\$79.20) and the maximum cost would correspond to that of a 12-in or more turbine (\$237.59). This is why the line “Inspection spin test for turbine (less than 12 in)” shows an amount of \$79.20 in the minimum column and \$0.00 in the maximum column whereas the line “Inspection spin test for turbine (12 in and up)” shows an amount of \$0.00 in the minimum column and \$237.59 in the maximum column.

In addition, as explained, the tables showing minimums and maximums are only used to present the information in a format showing in detail the costs included in Gaz Métro’s analysis. However, as explained in the response to requests 1.1 and 1.5 of the Régie’s Request for Information No. 5 as well as the response to request 2.1 of the Régie’s Request for Information No. 8 (B-0236, Gaz Métro-8, Document 10), the cost related to the type of meter that will be included in the marginal cost for a customer will correspond to the type of meter that will be installed, regardless the customer’s market. The cost of

¹ B-0144, Gaz Métro-6, Document 1, Schedule 2, p. 1.

² B-0196, Gaz Métro-8, Document 1, p. 3.

each of the characteristics, including the inspection cost for each type of meter, is shown in Schedule 2 of Exhibit B-0196, Gaz Métro-8, Document 1.

2.5 The Régie notes that for the residential and CII markets, the following costs related to inspection of meters:

- "Turbine"
- "spin test for turbine (less than 12 in)"
- "telemetry»
- "corrective instruments"

vary between zero and a capped cost, for both the first year and for subsequent years (reference (i)). However, this is not the case for the MIS market, the minimum and maximum values being the same. Please explain this difference in treatment.

Response:

Please see the response to request 2.4.

2.6 The Régie notes that for the MIS market (Table 3 of reference (i)), the inspection costs for the "spin test for turbine (12 in and up)" and the "Cost of a cellular line -telemetry", vary between zero and a capped cost, which is not the case for other cost headings associated with meters. Please explain this difference in treatment.

Response:

These are assumptions used by Gaz Métro for the purpose of preparing the proof. As noted in the response to request 2.4, the assumption used for MIS is that the minimum meter installed is a less than 12-in turbine without telemetry. However, in applying the method, the cost associated with the type of meter and instruments will depend on what is expected to be installed, regardless the type of customer.

2.7 Please specify if Gaz Métro has residential and CII customers that use meters that are 12 or more inches in length and, if so, the telemetry.

Response:

Gaz Métro does not have any residential customers and only one CII customer that uses a meter that is 12 or more inches. All meters that are 12 or more inches are installed with telemetry.

2.8 The Régie notes that for the residential and CII markets, Gaz Métro presented in reference (ii) weightings of 0.07% and 0.42% for costs associated with "Telemetry Inspection", representing costs of \$0.09 and \$0.50, respectively, for the first and subsequent years.

However, the Régie notes that for those markets (reference (i)), a range of costs varying between zero and a maximum cost of \$118.79 was defined for the first and subsequent years.

2.8.1 Please explain why, in reference (i), Gaz Métro did not use an average cost of \$0.09 for the residential sector and \$0.50 in the CII sector, for the first and subsequent years.

Response:

Please see the response to request 2.2.

2.8.2 Please repeat the exercise in sub-request 2.8.1, for "*turbine*", "*spin tests for turbine (less than 12 in)*", and "*corrective instruments*" costs to explain why the cost ranges defined in reference (i) were selected rather than the weighted costs in reference (ii), for the first and subsequent years.

Response:

Please see the response to request 2.2.

2.9 In light of your answers to the foregoing sub-requests, please revise and resubmit the costs related to processing CRP applications and to the inspection and maintenance of meters, for all markets. Please submit the costs specifically in the form of a weighted average, according to type of customer (residential, CII and MIS), both for the first year and for subsequent years (without minimums and maximums).

Response:

In light of our responses to the foregoing sub-requests and because the proposed methodology does not use weighted averages, Gaz Métro understands that it is not necessary to revise and resubmit the costs related to processing CRP applications and to the inspection and maintenance of meters. The cost of each is shown in Schedule 2 of Exhibit B-0196, Gaz Métro-8, Document 1.

The weighted averages of these costs, based on 2013 sales and used only for the purpose of calculating the impact on profitability of the development plan, are shown in Schedule 1 of Exhibit B-0209, Gaz Métro-8, Document 3.

**Marginal costs of processing a standard customer call and the costs of
customer retention**

- 3. References:**
- (i) Exhibit B-0144, Schedule 1 of Schedule A, p. 1 to 3;
 - (ii) Exhibit C-ROEE-89-0082, p. 12.

Preamble:

- (i) Tables of long-term marginal costs proposed by Gaz Métro for all markets.
- (ii) "**Customer calls:** *Gaz Métro assumes that the average residential customer puts the same burdens on customer service as the average CII customer. This seems unlikely, especially for the large CII customers and interruptible customers, who are likely to have more interactions and more complex interactions with Gaz Métro, regarding choices of rates, load-factor computation, subscribed volume, and other rate complications.*"

Requests:

- 3.1 Please specify if the following costs: "*Cost of processing a standard customer call*", "*Cost of bad debts*" and "*Collection and recovery costs*" for the MIS market (Table 3 of reference (i)) are included in the amount of \$1,197.16 for "*Customer retention costs - Major industries*" for years 1, 2 and other years. Please also specify if other activities and costs are included in that figure.

Response:

Since customers in the MIS market contact their representative directly if they have requests, the cost of a standard customer call processed by customer service is not included in the cost for a MIS customer. Because this activity is done by MIS representatives, the call processing costs are included in the amount of \$1,197.16.

"Collection and recovery costs" and "Cost of bad debts" are not included in "Customer retention costs – Major industries".

No other activity shown in the tables for residential and CII markets is included in "Customer retention costs – Major industries".

3.2 Please explain why the cost of processing calls for residential and CII customers is the same, namely \$12.84 (Tables 1 and 2 of reference (i) and reference (ii)).

Response:

The study conducted by the customer service team covered all calls received by that group, all customer group types together. Information per market type is not available and current systems do not allow this cost to be determined.

**Marginal costs related to Preventative and Corrective Maintenance on
Connection Lines**

- 4. References:**
- (i) Exhibit B-0144, Schedule 1 of Schedule A, p. 1 to 3.
 - (ii) Exhibit B-0144, Schedule 1 of Schedule A, p. 1 to 3 (footnote)
 - (iii) Exhibit B-0145, p. 9 to 11.

Preamble:

(i) Tables of marginal costs for long-term service delivery proposed by Gaz Métro for all markets.

(ii) *"This Table does not take into account additional preventative maintenance costs (\$0.22/metre) and corrective maintenance costs (\$0.34/metre) applicable to projects that, based on earning requirements, will require additional metres of line. Moreover, the maximum does not take into accounts preventative maintenance costs (\$12.88) and corrective maintenance costs (\$17.99) per additional connection line required in the project."*

(iii) Tables of marginal costs of long-term service delivery proposed by Black & Veatch for all markets.

Requests:

4.1 Please specify if the diameter, materials for the lines and the equipment required for measuring, cleaning etc., can differ according to the gas flow required and according to type of customer (residential, CII and MIS) and hence affect connection lines and pipes maintenance costs.

If yes, please state why the marginal costs associated with Preventative and Corrective Maintenance on Connection Pipelines and Lines, do not differ from one category of customers to another (reference (i)).

Response:

The connection pipeline diameter and control/measuring equipment for a customer depend on the hourly maximum flow required by the customer. This flow is based on the total load of the connected equipment, not the type of customer or annual volume consumed.

The choice of materials used for the connection pipeline depends on operating pressure and characteristics specific to the network where the customer is located. This choice is unrelated to the type of customer served.

Lastly, a given line diameter or specific equipment covers a range of values (flow and pressure), not a single value. A commercial customer and an industrial customer with similar but not identical connected loads may have the same connection pipeline diameter and the same measuring/control equipment.

These factors have minimal impact on the preventive maintenance program for Gaz Métro's lines other than the fact that a steel line requires that potential be measured to ensure the integrity of the line (e.g. presence of corrosion). For service to buildings, inspection frequency is higher for high-flow customers.

With respect to the corrective program, the type of line material will impact corrective maintenance costs (repair or replacement of a line section, corrections to coating, etc.) but the type of customer does not necessarily determine the type of line material used to connect the customer. Moreover, there are customers from the three market types that are connected to the gas network using steel lines. There are also customers from all market types that are connected using plastic lines. It therefore cannot be said that costs differ according to market type; they differ according to the type of materials installed at the customer. However, data relating to maintenance costs are not available according to the type of material.

- 4.2 Please explain why the marginal costs related to Preventative and Corrective Maintenance on Connection Pipelines and Lines, for the first year for all markets, is other than zero. Please indicate as of which year such costs may occur.

Response:

The costs for preventive and corrective maintenance on connection pipelines for the first year are zero for all markets according to the proposal chosen by Gaz Métro (Exhibit B-0145, Gaz Métro-6, Document 2). The program cycles for preventive connection pipeline maintenance range from two to six years according to the type of material installed whereas corrective maintenance stems from deficiencies which may arise at any time. It is therefore reasonable to assume that preventive and corrective maintenance costs may be incurred as of the second year for certain connection pipelines.

As indicated in the response to request 4.1, available data relating to maintenance costs do not allow segregation per type of material and Gaz Métro's past experience also does not allow it to say that these costs differ according to market type.

Gaz Métro agrees with Black & Veatch's position that, as of year 2, these costs are between zero and the maximum values of \$12.88 for preventive maintenance and \$17.99 for corrective maintenance. Since data that would allow us to determine a maintenance cost and schedule specific to each material used are not available, Gaz Métro is proposing a conservative approach for preventive and corrective connection pipeline maintenance costs

using the maximum values of \$12.88 and \$17.99, identical for all markets, as of the second year of the project.

- 4.3 Please specify if the description in reference (iii) of preventative and corrective maintenance on "*mains*", is actually a reference to the additional costs per metre of "connection pipeline" required for certain customers (reference (ii)). If this is not the case, please explain.

Response:

The cost of preventive and corrective maintenance on "mains" refers to the cost of maintaining lines, not connection pipelines. It is a maintenance expense directly associated with certain projects as shown in the examples given in Exhibit B-0208, Gaz Métro-8, Document 2, request 3.1 and Exhibit B-0236, Gaz Métro-8, Document 10, request 2.1. The explanations and limitations described in responses 4.1 and 4.2 indicate why Gaz Métro included preventive and corrective maintenance costs of \$0.22 and \$0.37 respectively per additional metre of line, regardless the market.

In Decision D-2013-106, the Régie asked Gaz Métro to:

[Translation] "[27] [...] *use a long-term marginal operating cost of \$157 in analysing profitability of the residential and CII development plan. This value may be revised in a future rate case when the distributor submits an evaluation of these costs.*"

When Gaz Métro prepared its initial proposal filed on October 8, 2014, B-0549, Gaz Métro-17, Document 4, File R-3879-2014, its goal was therefore to revise all operating costs including by definition line maintenance costs.

In the Black & Veatch report, reference (iii) filed on October 4, 2016 showing the line maintenance cost components, although the expert explains above on pages 4 and 5 of his report that those class 2 costs do not correspond to the definition of marginal operating costs. Gaz Métro also agrees that these costs are directly related to the investment. However, since the goal of this study is to evaluate all operating costs including by definition line maintenance costs, Gaz Métro has included those costs in its simulations provided for the requests for information.

Marginal costs related to bad debts

- 5. References:**
- (i) Matter No. R-3992-2016, Exhibit B-0088, p. 1 and 5;
 - (ii) Exhibit B-0236, response to request 1.2, p. 2.

Preamble:

[Translation:]

(i) *"In September 2016, Gaz Métro was informed by the receiver responsible for liquidating the assets of Québec Lithium inc., QLIMétaux inc., RB Energy inc. and Sirocco Mining inc., that the assets had been sold and that no sum would be paid to unsecured creditors, the list of which included Gaz Métro.*

[...]

As regards the financial contribution billed to, but not by, Québec Lithium, Gaz Métro can confirm that in light of the information received from the receiver on September 30, 2016, it will be unable to recover its claim in whole or in part. As explained in its 2015 Annual Report (R-3951-2015, B-0045, Gaz Métro-19, Document 1, pages 5 and 6), Gaz Métro wrote off Québec Lithium's \$2.8 million debt. The balance of that receivable was recorded against the provision for bad debts."

(ii) *"1.2 Please comment on whether "Distribution Gas Supply expenses" should be included in marginal costs for long-term service delivery as suggested by expert Chernick in reference (ii).*

Response:

Dr. Overcast is of the following view: "These are fixed costs that do not vary with the quantity of gas used by the system or the number of customers. As fixed costs they make no contribution to marginal costs by definition and should be zero." [emphasis added]

Request:

- 5.1 Please explain if costs associated with bad debts, such as those noted in reference (i) correspond to fixed costs for Gaz Métro (reference (ii)). If this is not the case, please explain if costs related to bad debts vary according to the number of customers or the quantity of gas used in the system.

Response:

Gaz Métro refers to the response to request 1.1 of Exhibit B-0236, Gaz Métro-8, Document 10, in which Dr. Overcast says the following about the cost of bad debts.

“[...] It is true that cost of bad debts and collection and recovery costs are more a function of revenues as opposed to added customers or added load. That does not change the fact that these are not marginal costs but rather are the result of social policies and should not be used as part of a line extension policy.”