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Mark N. Lowry, Ph.D.



Pacific Economics Group Research, LLC

Madison, WI, December 15th, 2016

Guy Sarault

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Hi Guy,

Attached please find a spreadsheet that calculates the funds needed for Phase 1 of the proceeding on a mechanism de réglementation incitatif for Hydro-Quebec Transenergie (“HQT”). The estimated cost of the work is **CAD 135,000 \$**.

In preparing this estimate, the hourly billing rates have been escalated by 1.0125x1.0075 from those we charged AQCIE in Phase 1 of the HQD proceeding. The escalation is based on the sluggish 1.25% inflation in the US Gross Domestic Product Price index which occurred between the third quarters of 2015 and 2016. These hourly rates constitute good value for the services of highly qualified U.S. consultants thanks to the currently strong value of the US dollar. PEG continues to be North America’s leading MRI consultancy, with large projects this year in Alberta, Ontario, and the United States in addition to Quebec. We are prepared to charge these rates because our work in Quebec is in the public interest and we have a long term commitment to advance the cause of MRI in Canada. Private ownership of our firm makes pricing flexibility to reflect such considerations possible.

The itemization of the tasks, and the hours we propose for each task, reflect our knowledge of how much work was involved in Phase 1 of the proceeding for HQD. The budget spreadsheet shows that the proposed cost is well below the cost (restated in 2017 dollars) which we spent on the Phase 1 proceeding for HQD. Economies were possible for several reasons.

- We are not planning to do any more of the preliminary empirical work using US transmission data which we undertook in Phase 1 to gain confidence that we could develop a sensible revenue cap index for HQT.
- There is less need to do background research on HQT or Quebec regulation since a lot of this research has already been done.
- Some of the ground covered in Phase 1 of the HQD proceeding may not have to be revisited, or at least can be revisited at much lower cost.
- HQT has not made large changes in its MRI proposal or evidence.

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- PEG Staff members Matt Makos and Kaja Rebane played important roles in the Phase 1 HQD proceeding and are thus able to “hit the ground running”.
- Some of the work will be delegated to a talented but low cost intern (Zachary Legge) who is graduating from the University of Wisconsin next spring with a triple major in economics, math, and classical humanities.

The cost of our work (and that of Kaja Rebane) is also reduced by our good reading knowledge of French.

The cost of an effective program of work in the Phase 1 proceeding for HQT is nevertheless substantial, for several reasons.

- It will be necessary for me to read the voluminous evidence, information request responses, and procedural rulings in this proceeding, as well as the Regie’s decision in the HQD proceeding.
- Evidence in the latest rate case of HQT should also be reviewed.
- We would like to update and restate some of our argumentation on MRI plan design to reflect insights we gained from work in various proceedings in 2016.
- It is desirable to have another round of consultation with other Quebec intervenors. One reason is that they too will have different perspectives on an MRI for HQT following their participation in the HQD proceeding. We propose to consult via emails and a conference call rather than a visit to Montreal.
- There is a modest budget for additional work on the regulation of power transmission in other jurisdictions. We did little work on this in the previous proceeding, and Concentric has alleged a lack of MRI precedents for transmission.
- We would like to update and, if necessary, upgrade our research on the historical and expected future cost trends of HQT. This work seemed to suggest the feasibility of a revenue cap index for HQT.
- It’s a good idea to have a modest fund for unforeseen developments such as assistance with a motion by HQT to strike evidence.
- Oral testimony and briefs will still require quite a bit of time for preparation, attendance at the hearing, and travel.

In general, it can be said that the request by Hydro-Quebec to bifurcate the hearing and provide new evidence on MRI for HQT after the passage of many months was bound to raise the eventual cost of the Phase 1 proceeding substantially.

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Our budget estimate may require revision when the Regie issues its decision concerning the funding for our work in Phase 1 of the HQD proceeding. Their willingness to fund our empirical work on MRI for HQT is one concern. If the cost of this or other work in the prior proceeding is disallowed because it pertains to HQT, we may seek to recover these expenses in this proceeding. Another concern is the Regie's willingness to pay for special tasks they asked for such as a second round of challenging information requests. An unwillingness by the Regie to pay for any cost overruns may prompt us to reconsider our budget for contingencies.

I plan to be around all next week and look forward to discussing and finalizing a proposal for Phase 1 of the MRI proceeding for HQT. Thank you for the opportunity to continue our enjoyable work and important work for AQCIE and CIFQ.

Sincerely,

Mark Newton Lowry, PhD

President, PEG Research LLC