DEMANDE DE RENSEIGNEMENTS N° 1 D'OPTION CONSOMMATEURS (OC) À PACIFIC ECONOMICS GROUP RESEARCH (PEG)

DEMANDE RELATIVE À L'ÉTABLISSEMENT DES TARIFS D'ÉLECTRICITÉ POUR L'ANNÉE TARIFAIRE 2019-2020

R-4057-2018

PERFORMANCE INDICATORS AND THE ESM

1. Reference : i) Pièce C-AQCIE-CIFQ-0018, p. 10.
ii) Pièce C-AQCIE-CIFQ-0018, p. 17.

Preamble :

i) *"We believe that the weights for an IMQ should reflect the relative importance of the performance dimensions and the need for penalties to discourage bad performance. While empirical evidence is lacking on these matters we believe that the five service quality areas do not merit equal weights. For example, employee safety does not warrant the same weight as reliability. HQD is already incentivized to mind its employee safety by its exposure to the risk of injury and damage expenses. This financial incentive to avoid injuries and damages should increase during the MRI.*

Another concern is that if a dimension of performance has a single metric, that metric may comprise 20% or more of the global indicator. This is the case for safety, where HQD has proposed a single metric"

ii) *"We recommend the following revisions to HQD's proposed service quality mechanism.*

- *The weights on safety, power supply, and customer service should each be reduced to 10%. These weights should be transferred to the reliability metrics. The weight on the reliability metrics would then be 50%.*
- *A reliability metric should be added which addresses service in more rural areas. First call resolution rate should be added as a customer service metric."*

Requests :

1.1 Please provide justifications for reducing power supply and customer service weights. In general, please explain why reliability metrics in an incentive mechanism should receive higher weights than other areas of performance.

1.2 Please provide examples of rural reliability metrics used in other jurisdictions.

1.3 Please provide a table with all indicators as proposed by PEG and corresponding weights.

Responses :

1.1 Generally speaking, the weights for service quality metrics should reflect the relative importance to customer welfare of a change in the dimensions of quality that each metric represents. We showed in our testimony that reliability metrics have substantially higher weights in a sample of approved service quality incentive mechanisms than the modest 20% weight that HQD proposes. If the weight on reliability is higher than the weight that they propose, the weights on some other metrics must be lower. We believe that customers care much more about the reliability of service than they do about the responsiveness of Hydro-Québec to their occasional telephone calls and connection requests. Furthermore, the quality of customer services is also addressed by the R-C-A customer satisfaction survey, which retains a full 20% weight in our proposal.

1.2 Table 1 of our testimony details two examples of performance incentive mechanisms with metrics that address the reliability of rural service. The first requires Commonwealth Edison in Illinois to present SAIFI results for that company's Northeastern and Southern regions. The Southern region includes more rural areas surrounding Chicago. The state of Massachusetts requires jurisdictional power distributors to report an average interruption duration index and an average interruption frequency index for each of their circuits. If distributors meet their SAIDI and SAIFI targets, penalties for poor circuit remediation are still possible. In a 2010 report on reliability, PEG noted that National Grid reported reliability metrics separately for the coastal and capital regions of Rhode Island.

1.3 Please see our response to *Régie de l'Energie demande de renseignement* ("DDR") 3.1.

2. Reference : i) Pièce C-AQCIE-CIFQ-0018, p. 17-18.

Preamble :

i) *"There are ways to avoid a dead band in the penalization for declining quality which are fair to HQD. For example, the Company can be subject to a revenue penalty only at the end of the plan and in the event that there is an average decline in IMQ scores on balance over the four years of the MRI term. Improvements in quality in some areas would be allowed to offset quality declines in other areas. However, HQD would receive no reward for a rise in the IMQ.*

The Régie should reconsider its decision to penalize HQD for poor quality only when the Company has surplus earnings. In principle, it can approve a supplemental revenue adjustment that doesn't conflict with its decision to link the MTÉR to service quality. Here is an example.

- *Declining service quality will reduce allowed revenue formulaically. For* *example, the decline in revenue for a 100 basis point decline in quality can be the same as the decline in HQD's proposal from an IMQ of -2 assuming 100 basis points of excess earnings. To guard against excessive penalties, it is reasonable to place a cap (e.g., 3% of allowed revenue) on these penalties.*

- *If the indicated revenue reduction for declining quality is less than HQD's share of surplus earnings under the existing MTÉR formula, the Company's share will be reduced by this amount.*
- *If the indicated revenue reduction for declining quality exceeds the Company's share of surplus earnings, HQD will retain no surplus earnings. Allowed revenue will be further reduced by the amount necessary to achieve the indicated revenue reduction."*

Requests :

2.1 OC understands that PEG is proposing a one-time application, at the end of the MRI's term, of HQD's IQM proposal instead of annual applications. Please confirm.

2.2 Please explain how "average decline in IQM scores" would be tied to overearnings and the ESM. Please provide a numerical example.

2.3 Would the "supplemental revenue adjustment" proposed by PEG be applicable on an annual basis? Please provide a numerical example.

Response :

2.1 PEG confirms that its proposed service quality incentive mechanism would levy any penalty only at the conclusion of the MRI. However, we envision that HQD would report annually on its performance with respect to each quality metric and the summary IMQ.

2.2 Please see our response to Régie DDR 4.1.

2.3 No. Any supplemental quality penalty would be levied at the end of four years.

OFF-RAMP

3. Reference : i) Pièce B-0053, p. 6-7.

Preamble :

In its report, CEA discusses HQD's ROE and equity ratio, as compared to other electric and gas distributors. CEA states that "*This supports a lower threshold than might otherwise be appropriate to achieve a comparable percentage of earnings at risk."*

Requests :

3.1 Does PEG agree with CEA's statement? Please discuss.

Response :

3.1 Table 3 on p. 6 of the July report of Concentric suggests that the equity ratio of HQD is very similar to that of other sampled electric power utilities. Hence, this issue need not be considered. The target ROE of the Company is at the low end of those surveyed. This reflects in part the lower risk of operating a system that is principally engaged in the delivery of low cost hydroelectric power and ownership by the government of Québec. This low target ROE does increase the variance of earnings outcomes produced by a given *clause de sortie.*

Y AND Z FACTORS

Contributions à des projets de raccordement

4. Reference : i) Pièce B-0021, p. 10-15.

Preamble :

In reference i), HQD is asking the Régie to recognize contributions to connexion projects ("*Contributions à des projets de raccordement*") as a Y factor for the term of the MRI.

Requests :

4.1 To PEG's knowledge, are such contributions to connexion projects generally treated as Y factors or included in the I-X formula?

4.2 Please provide an assessment of HQD's proposal.

Response :

4.1 Please see our response to Régie DDR 6.1.

4.2 Please see our response to Régie DDR 6.1.

Révision de durée de vie utile des transformateurs

5. Reference : i) Pièce B-0021, p. 15.
ii) Pièce B-0010, p. 15-18.

Preamble :

In references i) and ii), HQD explains it has revised the service life of overhead transformers, from 30 to 40 years. HQD asks the Régie to create a Z factor to take into account the financial impacts of the revision.

Requests :

5.1 To PEG's knowledge, is it common to create Z factors to account for revisions in service life of assets?

5.2 Please provide an assessment of HQD's proposal.

Response :

5.1 PEG has not formally surveyed this issue but believes that, whereas changes in accounting standards are often eligible for Z factoring, changes in service lives are not.

5.2 Changes in service lives are typically addressed in rate cases and are less likely to be imposed upon a utility by another party than changes in accounting standards. Both considerations reduce the need for Z factor treatment. If changes in service lives can be Z factored there may in the future be an incentive for the Company to change (or not change) service lives in ways that bolster earnings. However, extensions of service lives are generally beneficial to customers.