

**RH-4-92 - Volume 4**

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**NATIONAL ENERGY BOARD**



**OFFICE NATIONAL DE L'ÉNERGIE**

**Order No. RH-4-92**

**Ordonnance N<sup>o</sup> RH-4-92**

**Trans Quebec & Maritimes Pipeline Inc.**

**an Application by Trans Quebec & Maritimes Pipeline Inc. for certain orders respecting tolls  
specified in a tariff pursuant to Part IV of the National Energy Board Act;**

**Hearing held at  
Audience tenue à**

**Montreal, Quebec**

**4 December 1992  
4 décembre 1992**

**Volume 4**

**Canada**

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as represented by the National Energy Board

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représentée par l'Office national de l'énergie

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I

ORDER NO. RH-4-92

ORDONNANCE No RH-4-92

IN THE MATTER OF the National Energy Board Act and the Regulations made thereunder; and

IN THE MATTER OF an Application by Trans Quebec & Maritimes Pipeline Inc. for certain orders respecting tolls specified in a tariff pursuant to Part IV of the National Energy Board Act;  
RELATIVEMENT a la Loi de l'Office national de l'énergie et ses reglements d'application; et

RELATIVEMENT a une demande de Gazoduc Trans Quebec & Maritimes Inc. concernant les droits en vigueur au 1er janvier 1993 et au 1er janvier 1994.

- - -

Hearing held at Montreal, Quebec on Friday,  
4 December 1992

Audience tenue a Montreal, Quebec, le vendredi  
4 decembre 1992

- - -

PANEL:

J.-G. Fredette

President/Chairman

R. Priddle

Membre/Member

A. Cote-Verhaaf

Membre/Member

II

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TRANSCRIPT CORRECTIONS  
CORRECTIONS A LA TRANSCRIPTION

Volume 3 -3 December 1992

Page	Line	
400	21	delete quotation marks around "great interest in chaos", and insert around "chaos"
417	23	"a financial models company" should read "Financial Models Company"
462	24	add "process" after "regulatory"
483	14	delete "to"
484	23	insert "of" between "thought" and "the"
506	25	"Bank" should read "Canada"
530	11	"incentive" should read "insensitive"

- - -  
565  
Montreal, Quebec  
Friday, December 4, 1992  
Le vendredi 4 decembre 1992

--- Upon commencing at 8:30 a.m./A l'ouverture de l'audience a 8 h 30

LE PRESIDENT: Bonjour, mesdames et messieurs; good morning, everyone.

Monsieur Leclerc.

Me LECLERC: Monsieur le President, madame Cote, monsieur Priddle, avant de commencer notre plaidoirie, nous avons demande dans notre correspondance anterieure de rembourser la balance accumulee au 31 decembre 1992 dans le compte de report existant.

Ce remboursement sera effectue par un paiement net global le 1er janvier 1993 a TransCanada PipeLines et, a titre d'information, nous aimerions vous remettre un estime de ce remboursement.

J'ai distribue des copies de ces documents a mes collegues ce matin, et je le depose comme derniere piece au dossier.

LA GREFFIERE: Ce document portera le numero B-36.

PIECE No B-36: Document intitule/Document entitled

"Trans Quebec & Ma  
Accumulated in Def  
December 31, 1992"  
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PLAIDOIRIE AU NOM DE GAZODUC TRANS QUEBEC & MARITIMES INC.  
INTRODUCTION

Me LECLERC: Avant de traiter des diverses composantes du cout de service de la requerante ainsi que des sujets enumeres en annexe de l'Ordonnance RH-4-92, je desire en guise d'introduction vous faire part de quelques remarques applicables a la demande de la Compagnie dans son ensemble.

J'aimerais tout d'abord preciser que la demande qui est devant vous ainsi que les pieces et les temoignages deposes au soutien de celle-ci ont tous ete prepares suivant les regles de l'Office tant au niveau du contenu qu'au niveau de la forme. Ils constituent donc, a notre avis, un dossier complet vous permettant de rendre une decision eclairee.

En second lieu, je desire preciser que la demande tient compte des principes generaux enonces dans les decisions anterieures de l'Office. Nous cherchons par cette approche a assurer une certaine constance aux droits

de la Compagnie et a ne pas modifier des principes generaux qui ont bien servi la Compagnie et ses utilisateurs dans le passe.

C'est ainsi que nous demandons a nouveau, au niveau de la conception des droits, l'approbation de droits fixes mensuels correspondant a un douzieme du cout

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de service global approuve par l'Office pour chacune des deux annees d'essai, suivant l'approche mise de l'avant des la premiere cause tarifaire aux termes de l'Ordonnance TG-2-83.

Il y a lieu enfin de reiterer la mise en garde que nous avons formulee lors des dernieres auditions a l'effet que des projections couvrant deux annees d'essai ne peuvent, malgre une preparation rigoureuse, etre aussi precises que des projections couvrant une periode de moitie plus courte. Malgre cette mise en garde, nous n'envisageons pas cependant, a ce stade-ci, des changements importants et sommes confiants qu'advenant qu'il en survienne, nous pourrons en disposer dans le cadre des parametres de la loi sur l'Office national de l'energie.  
Demande

Ayant fait ces remarques preliminaires, je compte maintenant traiter du cout de service de la Compagnie.

Tel qu'on peut le constater dans la cedula 1.0 sous la rubrique "Cout de service" de la piece B-28, le cout de service pour les annees 1993 et 1994 s'eleve respectivement a 74 064 000\$ et 72 693 000\$, ce qui correspond a des droits mensuels respectifs de 6 172 000\$ et 6 058 000\$, soit une baisse de 3,2 pour cent en 1993

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par rapport a 1992 et une baisse additionnelle de 1,9 pour cent en 1994 par rapport a 1993.

Les diverses composantes du cout de service sont constituees des frais d'exploitation et d'entretien, du recouvrement des couts d'exploitation de l'Office, de la depreciation et de l'amortissement, des impots autres que l'impot sur le revenu, d'allocations pour l'impot sur le revenu et du rendement sur la base des taux desquels sont deduits les revenus provenant des services de transport et de stockage rendus au distributeur.

Je crois qu'il est important de noter que l'annee de base utilisee dans cette demande-ci correspond aux douze mois consecutifs prenant fin le 30 juin 1992, soit la derniere periode annuelle se terminant par un semestre qui etait complete au moment de la preparation de la demande.

Ici, monsieur le President, j'aimerais attirer votre attention sur l'effort particulier de la requerante pour rapprocher le plus possible l'annee de base du commencement de la premiere annee d'essai. La derniere demande tarifaire de la Compagnie en 1990 s'appuyait sur une annee de base se terminant le 31 mars 1990, laissant ainsi une periode de neuf mois avant la premiere annee d'essai debutant le 1er janvier 1991. Cette fois-ci, il n'y a donc que six mois entre la fin de

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l'annee de base et le 1er janvier 1993.  
Frais d'exploitation

Tenant compte du fait qu'il y a quand meme dix-huit mois entre la fin de l'annee de base et la fin de la premiere annee d'essai, un facteur de majoration de 3,42 pour cent pour tenir compte de l'inflation a ete utilise pour cette periode, soit 0,9 pour cent pour les deux derniers trimestres de l'annee 1992 et 2,5 pour cent pour l'annee 1993. En ce qui a trait a l'annee 1994, le facteur utilise est 2,3 pour cent pour tenir compte de l'inflation entre les deux annees d'essai.

Nous avons explique a la reponse a la question numero 34 (piece B-10) que les facteurs mentionnes plus haut et utilises par la Compagnie dans la preparation de la demande correspondent aux taux d'inflation projetes pour les annees 1992, 1993 et 1994 par deux organismes specialises dans ce domaine, soit le Conference Board of Canada et le Groupe WEFA. Il vaut la peine de mentionner que le 1,8 pour cent d'inflation projete par le Conference Board pour l'annee 1992 se rapproche deja beaucoup du taux reel de 1,4 pour cent que nous avons connu jusqu'en octobre de cette annee. Encore une fois, monsieur le President, madame et monsieur les membres, nous vous soumettons que l'utilisation par la Compagnie d'un facteur base sur la projection de ces deux organismes specialises est des plus raisonnable et devrait

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recevoir l'approbation de l'Office.

D'autre part, toutes les demarcations importantes dans les depenses d'exploitation projetees pour chacune des annees d'essai ont ete expliquees sous l'onglet 2 de la demande tarifaire (piece B-1). La majorite de ces demarcations sont detaillees de facon exhaustive, item par item, a la reponse aux questions 36 et 37 (piece B-10) et a la reponse aux questions 61, 62, 63 et 65 (piece B-18). De plus, la Compagnie a explique les variations des depenses d'exploitation entre 1992 (RH-2-90) et 1993 a la reponse aux questions 1.2, 1.3, 1.4 et 1.5 de Gaz Metropolitain (piece B-11) et a la reponse aux questions 66 et 67 (piece B-18). Enfin, il y a lieu de reveoir la reponse a la

question 74 (piece B-27) car elle s'adresse a la comparaison entre les depenses reelles et celles recouvertes dans les droits autorises.

Puisque les changements dans le niveau des depenses d'exploitation peuvent etre attribues soit a l'inflation, soit a des changements d'activites, la Compagnie a fait part a l'Office, dans sa reponse a la question 35 (piece B-10), des changements attribuables au taux d'inflation ainsi que ceux resultant d'un changement dans ses activites.

Vous avez donc devant vous un dossier complet vous permettant d'evaluer le bien-fonde des

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projections de la Compagnie. Que doit-on conclure de cette preuve?

D'abord, il faut conclure, sur cet aspect du cout de service, qu'il n'est pas pertinent ou utile de tenter d'etablir des comparaisons entre la Compagnie et les autres compagnies sous la juridiction de l'Office, surtout au niveau de la difference dans les pourcentages d'ecart entre les projections de depenses et celles reellement encourues. Ce genre de comparaison peut trop facilement mener a des resultats trompeurs.

Tel que mentionne dans notre reponse a la question 2.1 (piece B-11), il est evident que le montant global du budget de depenses aura une influence directe sur le pourcentage des ecarts. Ainsi, un ecart de 10 000\$ peut correspondre a un pourcentage important dans un cas, alors que le meme ecart correspondra a un pourcentage negligeable pour une autre compagnie.

La Compagnie a donc souligne que la comparaison de ses depenses avec la compagnie TransCanada PipeLines Ltd. effectuee par Gaz Metropolitain a la question 2.1 (piece B-11) n'est pas pertinente et n'est surement pas utile.

D'autre part, nous sommes surpris du fait que l'on ait qualifie les ecarts survenus dans le passe entre les depenses reelles et les projections comment

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etant des "inexactitudes apparentes" au niveau des projections de la Compagnie, alors que ces ecarts resultent plutot des efforts constants de la Compagnie pour reduire au minimum ses couts d'exploitation tout en assurant un service securitaire efficace.

La Compagnie n'a en effet jamais hesite, des qu'une occasion se presentait, a adopter des mesures ayant

pour effet d'améliorer son efficacité et de réduire ses coûts d'exploitation. La Compagnie n'a pas hésité non plus par le passé à refléter dans ses demandes, aussitôt qu'elle l'a pu, la réduction des coûts découlant de ces mesures.

Ce ne sont donc pas les écarts entre les coûts réels et les projections qui doivent être soulignés et faire l'objet d'une analyse, mais bien le succès de la Compagnie à réduire à nouveau ses dépenses.

Il ne faut pas perdre de vue que la plupart des mesures adoptées par la Compagnie en réduction de ses coûts sont de nature permanente et entraînent forcément une réduction du coût de service de la Compagnie puisque les nouveaux coûts réduits forment, suivant la méthodologie de l'Office, la base des projections pour l'année suivante.

Il est certain cependant qu'il devient de plus en plus difficile d'adopter de nouvelles mesures en

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ce sens et que les écarts que nous avons connus dans le passé s'atténueront à l'avenir.

Finalement, il faut conclure que les variances projetées entre l'année de base et les années d'essai ont été justifiées avec toute la précision requise et sont raisonnables.

#### SALAIRES ET AVANTAGES SOCIAUX DES EMPLOYÉS

En ce qui a trait aux augmentations de salaires pour les deux années d'essai, la Compagnie a retenu les services de madame Maureen Elizabeth Pallett de la firme Towers Perrin dans le but de la conseiller sur la situation concurrentielle de son programme de rémunération par rapport à son marché ainsi que sur les augmentations de salaire anticipées dans le marché canadien au cours des deux prochaines années.

Madame Pallett arrive à la conclusion que le programme de rémunération, incluant les avantages sociaux, offert par la Compagnie à ses employés en 1992 était de fait concurrentiel. Ceci fut expliqué dans la réponse à la question 32 (pièce B-10).

Pour chacune des années 1993 et 1994, madame Pallett recommande des augmentations de 3,5 pour cent. Tel que mentionné à la page 10 de son témoignage (pièce B-3), ce taux permettra à la Compagnie de maintenir, à l'intérieur des échelles et des fourchettes salariales, sa

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position actuelle par rapport au marché qui devrait



s'accroître de 3,2 pour cent par année au cours des deux prochaines années, soit de 0,5 pour cent à 1 pour cent au-dessus du taux d'inflation prévu. Ceci permettra également à la Compagnie la possibilité d'offrir à ses employés un facteur additionnel de 0,3 pour cent, lui permettant ainsi de se rapprocher du niveau concurrentiel du marché. Le facteur de 3,2 pour cent couvre le mérite, la progression, les promotions et la croissance économique.

Madame Pallett souligne également à la page 10 de son témoignage (pièce B-3) que, même avec les taux d'augmentation de 3,5 pour cent pour chacune des années 1993 et 1994, la Compagnie demeurera tout de même dans une position difficile étant donné la reprise économique prévue pour ces deux années, particulièrement pour 1994, ce qui amènera des pressions à la hausse sur le marché salarial.

Nous vous soumettons donc que les augmentations de salaire envisagées dans la demande sont raisonnables et devraient donc être approuvées par l'Office puisqu'elles reflètent les conditions prévalant dans son marché et sont conformes aux recommandations de son conseiller.

En ce qui a trait au nombre d'employés, la Compagnie a clairement stipulé à la question 74 (pièce

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B-28) que le nombre actuel d'employés lui est nécessaire pour assurer le fonctionnement efficace et sécuritaire de son réseau.

#### BASE DES TAUX

Traitant maintenant de la base des taux, vous noterez que le niveau moyen de celle-ci au cours des deux années d'essai (cédule 4.0 de la pièce B-28) se situe respectivement à 321 777 000\$ et 309 589 000\$.

Les montants mentionnés plus haut correspondent à la base des taux approuvée antérieurement par l'Office auxquels se sont greffés les changements aux Installations de Gazoduc en Service (GPISI) identifiées et justifiées, tel que requis dans la requête (Exigences de la Partie V, article 4(e) de la pièce B-1, Question 24 de la pièce B-10, Question 59 de la pièce B-18), amortie suivant les taux approuvés lors de la dernière demande. En effet, la Compagnie ne recherche aucun changement aux taux de dépréciation mentionnés dans les motifs de la décision rendue suite aux audiences tenues aux termes de l'Ordonnance RH-2-90.

Tel que mentionné dans le témoignage de monsieur Laforce (pièce B-5), le système comptable informatique de la Compagnie permet maintenant d'enregistrer le transfert aux "Installations de Gazoduc en Service" dans le mois de délivrance d'une ordonnance de

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mise en service par l'Office. La Compagnie demande donc de suivre cette procedure a compter de janvier 1993.

#### FONDS DE ROULEMENT

Les montants du fonds de roulement en 1993 et 1994 s'elevent respectivement a 2 112 000\$ et 2 197 000\$. Cette augmentation resulte du fait que la Compagnie avait prevu en 1991 et en 1992 collecter un montant de TPS important sur la facturation de ses droits a TCPL. Subsequemment, Revenu Canada a stipule que cette taxe ne s'appliquait pas, laissant la Compagnie avec un manque a gagner en ce qui a trait au fonds de roulement pour les annees 1991 et 1992.

Comme par les annees passees, l'encaisse est soutenue par une analyse effectuee en fonction du decalage de temps (Exigences de la Partie V, article 4(f) de la piece B-1).

#### IMPOTS AUTRES QUE L'IMPOT SUR LE REVENU

En ce qui a trait aux impots autres que l'impot sur le revenu, nous reclamons 2 336 000\$ pour l'annee 1993 et 2 368 000\$ pour l'annee 1994. Le montant pour 1993 comprend 1 795 000\$ pour les taxes scolaires et municipales et 541 000\$ pour l'impot sur le capital, alors que les montants correspondants pour 1994 sont de 1 833 000\$ et 535 000\$.

La majoration des taxes municipales est

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basee en grande partie sur les facteurs de majoration d'inflation dont j'ai deja parle et tient compte egalement de la reforme de la taxe municipale du Quebec.

Pour ce qui est de l'impot sur le capital, vous constaterez, a la lecture de la cedula 3.0 de la piece B-1, qu'il est passe de 629 000\$ pour l'annee de base a 541 000\$ en 1993 et, enfin, a 535 000\$ en 1994.

#### IMPOT SUR LE REVENU

La Compagnie a effectue ses calculs de l'impot sur le revenu conformement aux directives de l'Office.

La cedula 7.0 de la piece B-28 fait etat des calculs effectues par la Compagnie. L'allocation de l'impot sur le revenu pour chacune des annees d'essai s'eleve a 9 744 000\$ et 10 117 000\$ respectivement et est basee sur le taux d'imposition combine des societaires.

Le taux combine de 43,59 pour cent correspond a la moyenne de 43,44 pour cent pour NOVA et de 43,741 pour cent pour TransCanada.

#### COUT DE LA DETTE

En conclusion de cette partie de la plaidoirie, je desire vous entretenir brievement du cout de

la dette de la Compagnie ainsi que de notre demande d'approbation d'un compte de report pour tenir compte, au cours des deux années d'essai, de l'écart entre le niveau

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reel du taux préférentiel et les projections de ce taux incluses dans la demande, tel que présentement en vigueur pour les années 1991 et 1992.

L'on doit d'abord se rappeler que dès la fin de 1984 et le début de 1985 la dette de la Compagnie a en grande partie été financée à long terme et à taux fixe, le reste de la dette ayant été financé sur la base d'un prêt à terme négocié auprès de quatre institutions financières.

Vous vous souviendrez en effet que la Compagnie avait alors émis des obligations de série A, portant intérêt au taux de 13,10 pour cent et venant à échéance le 23 octobre 1994, pour un montant de 100 000 000\$, des obligations de série B au taux de 13,20 pour cent venant à échéance le 23 décembre 2004 et comportant un fonds d'amortissement obligatoire de 4 000 000\$ par année à compter du 23 décembre 1988, également pour un montant de 100 000 000\$, ainsi que des obligations de série C au taux de 11,70 pour cent échues le 23 novembre 1990 pour une somme de 85 000 000\$, le reste de la dette de la Compagnie ayant été financé au moyen d'un prêt à terme de 55 000 000\$ auprès de trois banques et de la compagnie Montreal Trust.

Tel que discuté lors de la dernière cause, la Compagnie a dû, en novembre 1990, remplacer les obligations de série C par de nouvelles obligations de

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série D portant intérêt au taux de 12,30 pour cent et venant à échéance le 23 octobre 1994, pour un montant de 55 000 000\$ et par un prêt à terme de 30 000 000\$ auprès de la compagnie Montreal Trust, à toutes fins pratiques aux mêmes conditions que dans le cas du premier prêt, lesquelles se sont avérées très avantageuses dans le contexte du marché, ce qui avait d'ailleurs été confirmé par le témoin expert de la CPA lors de la dernière audience. Malgré que les obligations de série A étaient rachetables au gré des détenteurs en 1989, aucun d'entre eux n'a exercé cette option.

La Compagnie devra procéder au refinancement de la série A et de la série D le 23 octobre 1994. Elle a donc projeté d'émettre les obligations de série E pour un montant de 90 000 000 \$ à un taux prévu de 10,00 pour cent venant à échéance le 23 décembre 2004; les obligations de la série F pour un montant de 35 000 000\$ à un taux de 9,50 pour cent, venant à maturité le 23 décembre 1999; et un emprunt bancaire de 30 000 000\$ à un taux variable.

La structure et le cout de la dette de la Compagnie sont tels qu'etablis aux cedules 6.0 et 6.1 de la piece B-28.

Vous noterez a la lecture de ces cedules que le cout de la dette consolidee de la Compagnie est respectivement 13,03 pour cent et 12,66 pour cent pour les

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annees 1993 et 1994. Le taux de 1993 comprend le cout des obligations en place, tel que detaille dans les Exigences de la Partie V, Article 4(n), page 3 de 10 de la piece B-1. Le calcul du taux de 1994 est detaille a la page 7 de 10 de la meme piece. Ce dernier calcul comprend les couts des obligations actuellement emises et celles prevues en 1994.

La Compagnie a determine le cout des obligations de serie E en utilisant une prevision independante du taux des obligations du Canada de 10 ans et plus (question 1, piece B-9), a laquelle une prevision d'ecart ("Spread"), egalement independante fournie par ScotiaMcLeod (question 52, piece B-18), a ete additionnee.

La Compagnie a determine le cout des obligations de la serie F en utilisant le meme procede et les memes sources independantes.

Malgre le fait que le temoin expert de la CAPP/APMC ait ete invite a faire sa propre prevision de l'ecart a utiliser, il a convenu (Tr. page 517, ligne 21) que les ecarts prepares par ScotiaMcLeod et utilises par la Compagnie dans son calcul n'etaient pas deraisonnables.

Nous croyons donc que les previsions utilisees par la Compagnie (question 1, piece B-9) sont independantes, ont surement fait l'objet de beaucoup de

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reflexion avant leur publication et ont ete emises par des organismes reputes dans leurs differents champs d'expertise. Elles devraient donc etre retenues.

Vous noterez, a la lecture des cedules 6.0 et 6.1 de la piece B-28 que le cout de la dette non consolidee de la Compagnie a ete fixe respectivement au taux de 6,50 pour cent et de 7,27 pour cent pour 1993 et 1994.

Ce cout, tel qu'explique dans nos reponses aux demandes de renseignements de l'Office, est base sur les attentes de la Compagnie quant au taux preferentiel

moyen au cours de ces deux années.

La projection de ces taux est basée sur la moyenne des projections formulées par les sept institutions financières consultées par la Compagnie et dont les noms apparaissent au bas de la cédule 1.C de la pièce B-9.

Comme expliqué plus tôt, l'emprunt bancaire maintenant en place avec Montreal Trust se terminera le 23 octobre 1994. Les intérêts calculés selon cette entente sont établis au taux préférentiel moins 1/2 de 1 pour cent et ont été utilisés pour le calcul de la dette jusqu'à la maturité de cet emprunt.

Toutefois, la Compagnie a été informée (question 1, pièce B-9) par Montreal Trust que celle-ci

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serait intéressée à renouveler le financement mais que, à cause des conditions du marché actuel et envisagées au moment du renouvellement, le taux d'intérêt en vigueur serait probablement situé au taux de base et non plus au taux de base moins 1/2 de 1 pour cent. La Compagnie a donc utilisé cette prévision dans son calcul.

De plus, monsieur Laforge a clairement indiqué les différences entre le marché actuel et celui prévalant pour les Trusts lors des financements précédents.

Il est important à ce stade-ci de mentionner que la Compagnie a des emprunts avec Montreal Trust depuis 1984 à un taux d'intérêt situé au taux de base moins 1/2 de 1 pour cent et que la Compagnie a toujours par le passé reflété dans ses prévisions ce coût au taux préférentiel moins 1/2 de 1 pour cent.

Étant donné que les modifications au système financier qui placent les Trusts pratiquement sur un pied d'égalité avec les banques et que celles-ci n'ont jamais pu offrir à la Compagnie un taux inférieur au taux de base, la Compagnie se voit dans l'obligation d'en tenir compte dans ses prévisions.

Le témoin expert de la CAPP/APMC a suggéré (Tr. page 527) à monsieur Laforge de s'adresser à nouveau à Montreal Trust. Toutefois, il est douteux que le témoin soit mieux placé que le vice-président adjoint de Montreal

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Trust pour déterminer le taux que peut offrir cette dernière à ses clients.

L'anecdote du témoin sur la visite de représentants d'institutions bancaires à ses bureaux n'est pas inusitée. La Compagnie maintient des contacts et est

visitee par plusieurs banques mais celles-ci n'ont jamais fait d'offre au taux preferentiel 1/2 de 1 pour cent pour autant par la suite.

Nous vous soumettons respectueusement que l'utilisation de la moyenne des projections des taux des institutions financieres reputees et les hypotheses du futur emprunt sont raisonnables et constituent les meilleurs outils accessibles a la Compagnie pour etablir ses propres attentes dans le cadre de la presente demande.

L'on doit de plus se rappeler que, compte tenu des circonstances particulieres de la Compagnie, celle-ci a des le debut ete obligee et devra a l'avenir financer une partie de sa base des taux par de la dette a court terme.

En effet, la Compagnie doit faire face a une reduction constante de sa base des taux. Elle doit donc utiliser la dette a court terme pour maintenir le rapport dette/avoir propre au niveau autorise par l'Office. Ses engagements envers ses creanciers sont a l'effet de ne jamais permettre que la composante dette excede 75 pour

cent.

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En d'autres mots, la dette de la Compagnie ne doit en aucun temps etre superieure a trois fois le montant de l'avoir des actionnaires.

Il va de soi que le montant de l'emprunt bancaire a court terme doit etre suffisant pour permettre le remboursement de la dette de facon concomitante a la reduction de la base des taux, tout au moins jusqu'au refinancement, en tout ou en partie, de la dette a long terme a taux fixe. C'est ce qui explique que le montant du pret bancaire soit relativement eleve lors de la mise en place du refinancement a long terme et qu'il decroisse de facon constante jusqu'au refinancement subsequant.

Par exemple, le pret de 30 000 000\$ negocie en novembre 1990 sera ramene a environ 4 000 000\$ lors du refinancement des obligations de serie A et de serie B en 1994 et l'emprunt bancaire de 30 000 000\$ prevu pour octobre 1994 sera pratiquement repaye au moment de l'echeance des obligations de serie F.

Il va de soi egalement que le niveau de l'emprunt a court terme finance a un taux variable peut avoir un impact serieux sur le rendement de la Compagnie dont l'importance variera evidemment selon les ecarts pouvant survenir au cours des deux prochaines annees entre le niveau reel du taux preferentiel et celui approuve par

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l'Office dans sa decision.

Voila pourquoi nous vous soumettons qu'il est necessaire que la compagnie soit mise a l'abri des consequences des variations dans le taux preferentiel qui, l'on doit se rappeler, est un taux administre par la Banque du Canada, donc hors du controle de la Compagnie, repondant a des imperatifs qui ne sont pas toujours d'ordre financier et qui a fluctue de facon tres importante durant les dernieres annees, et tout particulierement recemment.

Nous croyons donc qu'un compte de report fonctionnant exactement avec les memes criteres que celui qui est en place pour les anees 1991 et 1992 devrait etre accorde pour les anees 1993 et 1994.

Pour toutes ces raisons, nous soumettons que le cout de la dette et les projections de la Compagnie quant au taux preferentiel pour les deux anees d'essai, tels qu'utilises dans la piece B-27, sont raisonnables et devraient donc recevoir l'approbation de l'Office.

Nous vous soumettons egalement que dans les circonstances particulieres de la Compagnie, il est raisonnable, voire meme souhaitable, d'approuver le compte de report tel que demande par celle-ci.

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I will now deal with the issue of  
Rate of Return.  
RATE OF RETURN

The Board has been called upon in these proceedings to establish a fair rate of return for TQM. The Board has before it the recommendations of two witnesses. On the one hand, Dr. Morin is recommending a range of 13 to 13 1/4 per cent and, on the other, Dr. Waters is recommending a range of 11.5 to 11.75 per cent.

In our Argument, we will explain why Dr. Waters' recommendation should, in our view, be increased towards that of Dr. Morin, and point out the methodological and conceptual problems in Dr. Waters' approach.

Before doing this, I will comment on Dr. Morin's evidence.  
DR. MORIN

In the case of Dr. Morin, he used the same approach as he did in the 1990 Evidence. While the presentation of his evidence has been slightly changed, it still involves the three principal methods of developing a recommendation for a return on common equity: namely, DCF,

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Comparable Earnings, and Risk Premium.

His approach is to provide an array of results so that the Board may be informed of the kinds of numbers that are generated by using each of the main techniques. He believes that the results must be considered as a whole, rather than selectively, and that it would be inappropriate to select any one particular number to infer TQM's equity cost.

In the detailed application of the major techniques, he has involved his Risk Premium estimates by making greater use of the more modern market-based CAPM technique. This produces results that are somewhat lower than average, but more rigorously developed, and thus sounder.

His Risk Premium analysis is further expanded by examining data from the U.S. gas industry. The use of the new data has contributed to the correctness of his analysis by addressing the paucity of undiversified gas utilities in Canada by providing a more conservative benchmark estimate of equity costs, by using the more unbiased analysts' long-term growth forecast, and, finally, by utilizing the degree of integration between the Canadian and the U.S. capital markets,

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all leading to development of more accurate estimates of cost of capital.

He continues to provide a Comparable Earnings estimate, in view of the importance of this technique in the history of regulation and because of the fairness element that is so central to the regulatory process, but he gives it less weight than the market-based measures by using only one Comparable Earnings number.

With regard to his DCF estimates, he calls for caution in judgment in interpreting the results (pp. 10 and 11 of Appendix B to his Written Evidence), but he still uses two DCF estimates out of a total of seven estimates in his Summary Table.

Dr. Morin particularly cautions against the use of shorter-term periods to estimate growth rates, since they would not be representative of the long-term growth rates specifically required by the DCF model. He relies on 15-year historical growth rates to provide more



representative estimates of investors' expected growth rates.

In his Opening Statement, Dr. Morin formally updated his original recommendation from

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a range of 13 1/4 to 13 1/2 down to a range of 13 to 13 1/4 per cent, to incorporate the decrease in long-term interest rates that has occurred since the filing of his Testimony in June of 1992.

In this manner, Dr. Morin provides the Board with a diversity of information that can be of use in assessing the cost of common equity. Overall, Dr. Morin, in utilizing and implementing his techniques, strikes a proper balance between the use of judgment and the need to maintain the integrity of the techniques used.

DR. WATERS

I now turn to Dr. Waters' evidence.

In contrast to Dr. Morin, Dr. Waters uses only two techniques; i.e., DCF and the Risk Premium. His analysis, however, shows that his recommendation places no weight on the DCF results, since they produce very low rates of returns, according to Dr. Waters.

I propose to begin my discussion of Dr. Waters' evidence by addressing the issue of the most appropriate mean to calculate the market equity risk premium.

The record before you unequivocally shows that the financial literature on this

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subject is unanimous in holding that the arithmetic mean is the most appropriate technique to develop an estimate of the cost of capital, which is the very essence of this hearing.

Indeed Dr. Brealey and Dr. Myers, both well-known for their widely-used textbook entitled "Principles of Corporate Finance", are of the view that and I quote "arithmetic mean returns should -- and I emphasize the word "always" -- always be used as benchmarks for the opportunity Cost of Capital." (Exhibit B-30).

Professors Ibbotson and Siquefield,

for their part, take the position that the arithmetic mean is "the correct rate for cost of capital estimation, forecasting and discounting" (Exhibit B-32, p. 91), while recognizing of course that the geometric mean, which is "backward looking", measures the change of wealth over time.

Professors Hatch and White take the same position in their work entitled "Canadian Stocks, Bonds, Bills and Inflation: 1950-1983" (Exhibit B-31), an updated version which is used by Dr. Waters as historical data in support of his Risk Premium estimate.

Dr. Morin supports the position of

these authors (pp. 31 and 32 of his Evidence) and mentioned, during his cross-examination, that the debate on this issue in the United States had long been resolved (Tr. 146).

Dr. Waters recognizes that none of these authors suggest that utilities should be treated any differently than other stocks (Tr. 468). His inference to the effect that such equal treatment of utilities and other stocks may have resulted from an oversight on their part simply cannot be sustained. For one, it is incompatible with the word "always", used by Drs. Brealey and Myers.

Secondly, no reason whatsoever is advanced by Dr. Waters to explain why they would have wanted to treat utilities on a different basis.

Are not utilities part of the market, like any other company?

Dr. Waters knew of no financial literature reference in support of his views (Tr. 457), nor of any other rate of return witness who took a similar position. He, himself, had used a combination of both means in all of his previous testimonies on the Risk Premium technique

since he started using this technique in 1988 and it is only in the most recent TransCanada evidence that he would have started to use a geometric average exclusively.

Interestingly enough, there is absolute unanimity among all concerned, including

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Dr. Waters, that the geometric average will always be less or equal to the arithmetic average, equality occurring only when returns are constant.

The only explanation given in support of his position is found in Appendix XIII of his Evidence.

We submit that the content of his analysis is simply and completely wrong, for a number of reasons.

The first one, and certainly not the least, resides in the fact that Dr. Waters isolates utilities from the market as a whole and then, based on and because of his observations on the book return of these utilities, he would have the Board apply the geometric mean to the market in its entirety, in complete disregard for the fact that most companies in the market do not share the same characteristics.

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I emphasize "book returns" because there is no logical relationship between the volatility of book returns and market returns -- the latter being, of course, the basis of the Risk Premium technique.

Furthermore, given his opinion of accounting book values, it is indeed most surprising to see him use them.

Treating utilities differently implies market segmentation, which itself is inconsistent with a financial environment where securities are traded in a competitive manner. The literature in Finance and Economics is replete with evidence opposing the existence of such segmentation.

His approach further implies that such segmentation will occur for lower-risk securities, which is consistent with his explanation for the alleged shortfall of achieved returns over expected values for long-term Canada bonds.

Secondly, his approach amounts to nothing else than double counting and constitutes a fundamental change to an essential element of the Risk Premium technique.

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Stated differently, he is in fact tampering with the "machine", instead of passing judgment on what comes out of it.

Furthermore, notwithstanding his disclaimer, his approach obviously involves a large amount of circularity. Utilities are in fact taken out of the market because their returns are less volatile, therefore less risky. Because of this, he applies the geometric means to the market as a whole, thus reducing the market risk premium because of the lesser risk of utilities.

It is double-dipping because, having already accounted for the lesser risk of utilities through the geometric average, he again reduces his market risk premium by half, to account for the lower risk of utilities.

Thirdly, in showing that there is very little difference between the allowed and achieved rates of return for the utilities he has looked at, he is in fact suggesting that their return is constant.

He recognized (Tr. 475) that constant return would be perceived by investors as implying no risk at all; in other words, a beta of zero.

This, of course, is in stark contrast

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to his conclusion, at page 53 of his Evidence, where he states that utilities are half as risky as the market as a whole.

However, the most eloquent illustration of the unreasonableness of his approach resides in his admission (Tr. 474) that an investor, looking prospectively at Cases I and II (Tr. 150 to 152) developed by Mr. Yates would not be indifferent between the two if offered a return of 10 per cent in both cases.

Dr. Morin -- of course, for obvious reasons -- held the same view.

For all of these reasons, we would urge the Board to reject Dr. Waters' proposal and analysis and to settle this issue once and for all.

Had he applied the arithmetic mean to his historical data, Dr. Waters' achieved values would have risen from a range of 4.0 to 4.7 per cent to a range of 5.4 to 5.7 per cent (Tr. 451),

thereby increasing his market risk premium to a midpoint of 5.55 per cent.

The application of his 60 per cent estimate of TQM's relative risk to this number would increase his investor-required return for

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TQM to a range of 11.58 to 12.08 per cent, and his final recommendation to a range of 12.08 per cent to 12.58 per cent.

The second concern we have with Dr. Waters' testimony is his adjustments for the alleged shortfall between the achieved versus expected returns of long-term bond investors and for the purchasing power premium.

We are indeed concerned with Dr. Waters' sudden and unexplained retreat from the quantification of these adjustments and his request that they now be considered qualitatively, particularly in view of the fact that he has placed such great emphasis on these adjustments and that the Board most likely took them into consideration.

Given his recognition of the somewhat higher results for the U.S. market, these two adjustments, combined, do not now represent more than a potential 25 basis point adjustment, when in the past he was recommending almost 300 basis points, which is more than ten times his current position.

In light of its Reasons for Decision in the RH-1-92 Westcoast case, we urge the Board

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not to give any weight to the purchasing power premium. Dr. Waters recognized that the 2.75 per cent (Tr. 484) consensus inflation forecast constituted a low inflation environment.

With regard to the adjustment for the shortfall between achieved and expected returns, we submit that, not only should no weight be given to it, but it should be discarded altogether by the Board because it is inaccurate and based on a wrong premise, as clearly appears from the graph filed as Exhibit B-33.

Investors have sometimes earned more and sometimes earned less than they expected. Dr. Waters recognized (Tr. 490) that, in the long

run, achieved and expected returns tend to be the same. Furthermore, Dr. Waters admits that the regression lines shown on Exhibit B-35 demonstrate that the difference is statistically insignificant.

Since the slope of the regression line is very close to zero, the differences between achieved and prospective yields should be expected to be zero in the future. Hence, no adjustment would be necessary to estimate the market risk premium.

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My final remark on this issue is that Dr. Waters appears to be comparing the equivalent of one-year bonds with the yields of long-term bonds. In order to achieve the yield, one must keep the bond to its maturity. Obviously, it is not very likely that one would receive the prospective yield in any year during the term of the bond if it were sold prior to maturity.

#### CHANGES TO THE METHODOLOGY

TQM is also concerned with the changes Dr. Waters performs to the techniques which are designed to test, in an objective manner, the validity of his conclusions.

In so doing, Dr. Waters allows his personal judgment of economic events to change some of the fundamental underpinnings of the techniques used in his analysis, thus impairing the objectivity of the results obtained.

I would first draw the Board's attention to Dr. Waters' choice of the period over which the growth of dividends are estimated for the purpose of the DCF analysis.

You will recall that in his previous testimonies, Dr. Waters had used 5- and 8-year periods, and given no weight whatsoever to the

10-year period.

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His reasoning for not doing so was purely due to the high rates of inflation observed during the early 1980s. His justification rests on the premise that periods of high inflation would produce growth rates which are higher than what an investor would normally expect.

On the basis of the same logic, should it not follow that periods of unusually low inflation should also be discarded.

That is clearly impractical. Furthermore, in estimating the appropriate period for choosing economic parameters such as the rate of growth, one is well advised to adhere to the conceptual requirements of the models being used.

More specifically regarding the DCF model, the growth rates are expected to represent long-term phenomena, which should rationally be estimated over a long period of time.

That is precisely what Dr. Morin has done by utilizing the 15-year period, which encompasses various economic cycles and, hence, follows the precepts of the model.

Secondly, in his testimony, Dr. Waters performs a number of adjustments

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without providing empirical justification as to their magnitude. For example, the 1990 DCF non-utility results were adjusted downward by a range of 50 to 70 basis points, while this year's results are adjusted by a range of 60 to 80 basis points.

Another example of such adjustment resides in Dr. Waters' offer of a "cushion" to the rate of return required by low-risk utilities, to account for a number of factors, including flotation costs and the risks associated with the volatility in financial markets.

How is the Board to know whether such adjustments are too large or too small?

RISK ENVIRONMENT

In his testimony, Dr. Morin points out that, in his view, capital markets and the economy in Canada remain volatile, as evidenced by divergences in economic forecasts and the volatility of market rates, particularly focusing on the short term.

He further argues that the timing and the magnitude of the economic recovery in Canada are speculative at best. The restructuring of the Canadian economy remains an issue which is

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seriously debated in many financial circles, as acknowledged by Drs. Morin and Waters.

This situation, coupled with the recent volatility in foreign exchange markets around the world, the inability of central banks to control the erratic behaviour of their exchange rates, the increasing influence of international speculators with vast amounts of liquidity, the continuing Constitutional uncertainty in Canada, with particular focus on Quebec, together with the international indecisiveness as to future of the European Economic Community, signals an economic environment which is riskier than two years ago.

Clearly, the operating as well as the financial performance of any company is, and will continue to be, adversely affected in the short term. When the financial markets will eventually reach an equilibrium cannot be ascertained at this time.

This economic situation is particularly harmful to companies with high degrees of indebtedness, faced with the obligation of having to refinance a large portion of their debt.

In the jargon of finance, their debt

burden will be magnified by the existence of future interest rate risk associated with the refinancing prospects. Investors, in competitive capital markets, will take these prospects into consideration and will not be attracted by such corporations.

While we believe that recovery will materialize in the long run, we expect short run difficulties for corporations.

It is our submission that these circumstances have increased TQM's risk, thereby justifying a range in the order of magnitude suggested by Dr. Morin.

That concludes my remarks,  
Mr. Chairman.

The Board had asked whether we wished to comment on our request that our rates be deemed interim as of January 1, 1993.

The only thing that I would mention in that respect is that we expect that normally,

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since our previous rates were established on data for the two years, as of that date they would become interim, should the Board's Decision be rendered after January 1, 1993.

Thank you.

M. PRIDDLE: Maitre Leclerc, j'aimerais vous 0603 poser une question qui touche a la preuve de monsieur Laforge a la page 71.

--- (Courte pause/A short pause)

Me LECLERC: Oui, je l'ai.

M. PRIDDLE: Je reprends. A la page 71, je vous demanderais de lire de la ligne 9 a la ligne 15.

Me LECLERC: Oui, c'est fait, monsieur le President.

M. PRIDDLE: Vous noterez, maitre Leclerc, le double negatif dans la phrase principale. Je regrette de ne pas avoir reagi suffisamment vite pour poser cette question a monsieur Laforge.

Ce que je voudrais vous demander est ceci: Est-ce que l'Office doit s'attendre a la possibilite que, face a une fluctuation imprevue, presentement imprevue, dans les taux d'interet pour les series E et F a l'automne 1994, vous nous demandiez alors un compte de report, "a deferral account", pour faire face a des differences imprevues dans les taux d'interet, en depit du fait qu'en ce moment vous nous demandez une tarification fixe pour les deux prochaines annees?

Me LECLERC: Je comprends tres bien votre question, monsieur Priddle. J'ai ma propre reponse mais, si vous le permettez, j'aimerais verifier avec monsieur

Heider.

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--- (Courte pause/A short pause)

Me LECLERC: Je crois que la reponse de la Compagnie serait la suivante, monsieur Priddle. Ca dependrait, evidemment, de l'importance des variations. On reconnait, on saisit tres bien le fonctionnement d'une methodologie a base de taux fixe et on sait qu'il peut y avoir des montants qui seraient inferieurs comme il pourrait y en avoir qui seraient plus eleves. La decision resultera de l'importance des variations.

Si c'etait extraordinaire... Je crois que vous vous rappellerez que dans le passe ca nous est arrive une fois, je crois en 1984, lorsque les taux d'interet a court terme sur la dette avaient change a un point tel que nous avons fait une demande pour changer en cours de route ce qui avait ete decide par l'Office. Mais c'est quand meme un evenement tres rare; c'est arrive une seule fois.

A moins de circonstances exceptionnelles, on ne s'attendrait pas à ce qu'il y ait une demande à l'Office pour faire en sorte que cet élément fasse l'objet d'un compte différent.

M. PRIDDLE: Merci, maître Leclerc.

MR. YATES: Mr. Chairman, I wonder if we might have about a ten-minute adjournment at this point.

There are a couple of things that Mr. Leclerc has raised in his original argument that I would like to discuss with Dr. Waters, to determine whether we seek to reply to them. 0605

THE CHAIRMAN: Certainly, Mr. Yates.

MR. YATES: Thank you, Mr. Chairman.

THE CHAIRMAN: We will adjourn for ten minutes.

--- A Short Recess/Pause

--- Upon resuming

THE CHAIRMAN: Mr. Yates, please. 0606

ARGUMENT ON BEHALF OF THE CANADIAN ASSOCIATION OF PETROLEUM PRODUCERS:

MR. YATES: Thank you, sir.

Working out of a hotel room rather than an office, I have not been able to get additional copies of the notes of my Argument. What I will do is I will provide my copy of my notes to the Court Reporters when I am finished here, with the request that the evidentiary references be incorporated into the transcript.

This case is about regulation of a rate of return. If I spoke that sentence -- ten words -- to many people, their eyes would glaze over. I have seen it happen: narcolepsy could set in, or terminal ennui.

Others -- more knowledgeable others -- would say: "Oh, that is just smoke and mirrors. It is a way for consultants and lawyers to prosper, arguing about things that nobody cares about or understands."

Educated cynics could say: "Long Canadas plus 300 basis points. Why do we need a hearing!"

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The experts -- the Dr. Waters, Dr. Sherwins and Dr. Morins of the world -- might say: "Au contraire! What we are doing here is akin to that subset of gemology that involves the study of diamonds: It is multi-faceted; it is subject to different conclusions, depending on perspective; it is dramatically different in appearance when it is viewed in different lights; and it is infinitely valuable."

In this milieu, we run the gamut of views from "A" to "Z": We have agnostics -- like you, Mr. Chairman; we have those who thunder on in support of their particular viewpoints, like Dr. Sherwin is fond of doing in other proceedings; we have Dr. Waters, who very carefully analyzes massive amounts of theory and data before recommending particular techniques and results; and in the case of TQM, we have Dr. Morin.

That is what brought me, yesterday, to think about alchemy.

You will remember, Mr. Chairman and Members, that Dr. Morin told you that if he were a regulator, he would not reveal the recipe for his Decision (2T 323-325). And he used that view to argue that his methodology had particular merit

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for you (2T 323ff), apparently because it uses every methodology known to cost of capital analysts.

That perhaps is a slight exaggeration, because he does not use the Arbitrage Pricing Model -- yet. He did give us some indication that he may bring it back to you the next time that he appears.

But this utilization of different methodologies is not, in my submission, what is right with Dr. Morin's approach. It is precisely what is wrong with it.

We learned in school that alchemists were people who existed in the Middle Ages, whose primary purpose in life was to find a way to turn everything into gold. I remember drawings in my textbooks of those alchemists peering into large bubbling and steaming cauldrons, apparently wondering what to throw in next or what to filter out.

Dr. Morin is the rate of return

version of an alchemist. He throws in every method he can think of, he stirs it around, and discards this and that, and then he says to you that the result is gold. He says to you that the

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result is the gold which you are trying to find in this particular hearing process, and that is what is the just and reasonable rate of return for TQM.

Now, the alchemists asserted that they had succeeded in turning lead into gold, as I recall. They were wrong. In my submission to you, Dr. Morin is wrong. I submit to you that what Dr. Morin has created through his methodology is nothing more than lead, and it should be discarded by you as worthless.

Let's look at Dr. Morin's alchemy. When he first appeared at this Board, he had 11 ingredients (1T82), and that was in 1988. He threw out some. To use his word, he "truncated" them. He averaged the rest and, voila, he gave you a number. That exceeded the number which you ultimately decided was just and reasonable in that case. Dr. Morin came back in 1990, and here he had restricted his ingredients to seven (1T82). He added two new ones, the Capital Asset Pricing Model and the Empirical Capital Asset Pricing Model (2T80). He got rid of some others.

He did his truncation routine; he threw out some, and averaged the rest, and gave

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you a recommendation that again was higher than the number that you decided upon (RH-2-90, p. 28; 14.25-14.50% v. 13.75% awarded, p. 15).

In this case, we have yet another mixture from Dr. Morin. Here he started with nine tests: three risk premium, one comparable earnings, three discounted cash flow, the CAPM and the Empirical CAPM.

There were a couple of these tests that he had used before that he did not like this time, so he did not put them into the pot. Those were the DCF energy companies and the risk premium energy companies (1T85). He, in a word that we used, "pre-truncated" them, discarded them. That left seven. Were they the same seven as 1990? No.

Those seven -- the 1990 seven -- had not resulted in gold. And we have the 1992 seven that are different.

This year what Dr. Morin puts forward for you to look at are one Comparable Earnings Test, one Empirical Capital Asset Pricing Model, one Capital Asset Pricing Model, two DCFs, and two Risk Premiums (1T88-89).

He has added, since the last time, a U.S. Gas Utilities risk premium test (1T93). He has added "ranges" of values now (1T92). He has taken out a DCF test and he has replaced it with a risk premium test (1T89).

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And now he has six averages for you to look at. Those appear, in their final form, on the first page of Exhibit B-25, which you will recall is the twice-amended "Summary of Results", that reached its present form only after the cross-examination commenced in this hearing.

Now Dr. Morin puts forward averages and truncated averages of high points, of low points, and of midpoints. Depending on the column on his table, we can truncate five of his seven tests, if we want -- not if we want; if we follow what he asks us to do.

The Comparable Earnings Test, the U.S. Gas Utilities risk premium test, the DCF Telco's Test, the Empirical CAPM, the CAPM (1T111-112), each one of those comes out in one of these arithmetic processes.

In my submission, this is not analysis. This is mechanistic arithmetic. This is not a way for you to find the gold of the fair and reasonable rate of return for Trans Quebec &

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Maritimes; it is simply a way to create sludge, to create lead at the bottom of the pot.

I am not suggesting to you that methods should not evolve. They should, and they do. Dr. Waters told you about that yesterday (3T560).

What I am saying is that the evolution should have direction. It should not be just to add another "wing of bat" or "tongue of

dog" to the brew, hoping to add insight. It should be for the purpose of enhancing the reliability and credibility of the technique.

That is why it is, in my submission, critical for you, as regulators, to give guidance to the participants in these hearings. It is not enough to say: "Our reasons are because we think so." That approach only operates to expand the regulatory process, because it discourages the parties from focusing on the aspects that the Board thinks are important.

We are all seeking to minimize the time that is spent in the regulatory process, and we can go closer to that goal by getting greater guidance from the regulators as to what you consider to be important.

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(Yates)

In this regard, the Canadian Association of Petroleum Producers strongly supports the views which were expressed to you by Dr. Waters yesterday on this topic (3T558ff). Without going back to repeat those, let me simply commend them to you.

If I may say so, your Decision in the last TQM case, the RH-2-90 Decision, was both good and bad in this regard (RH-2-90, p. 14).

What you said at page 14 under "Views of the Board" relating to the topic of Rate of Return on Equity was this, and I quote:

"The Board gave some weight to the results of each of the cost estimation techniques employed in this proceeding."

That, in my submission, is the "bad" part. But you go on to say:

"However, after taking into account its concerns relating to the application of the various approaches used by the expert witnesses, the Board, in reaching its decision on a fair and reasonable rate of return on equity for TQM, gave the various risk premium

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approaches somewhat greater weight." And that, in my submission, is the "good" part, because it gives guidance to the parties appearing before you.

I would respectfully submit to you

that this is the road that you should go further along in the present case. This is the road that is the way to the "gold", which is the right, the fair, and the reasonable rate of return for TQM.

On the evidence that is before you in this case, it is the risk premium technique that the expert witnesses agree is the best. It is, therefore, the risk premium technique that, in my submission, you should use in reaching your result.

Let's look for a minute at the evidence that I am referring to.

Dr. Waters rejects the Comparable Earnings Test, telling you, as he has in the past, that he cannot find any relevance to cost of capital determination for utilities in the accountant's numbers that are used in the Comparable Earnings technique (Ex. C-1-4 p. 63ff; 3T390ff).

Dr. Morin does not like Comparable

Earnings either. He said so in his book. He tells you that he thinks market-based techniques should be given more weight (1T80-81). And he is quite sanguine when the Comparable Earnings Test results make it a "truncatee" (1T109).

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That is what he told me a couple of days ago.

Dr. Morin also says he is "uncomfortable with DCF" (1T87).

Dr. Waters gives you cogent reasons why DCF should not be used today (3T357). That is in his evidence. And he explains to you why he relies on the risk premium technique, to the exclusion of others.

This is not to say that the DCF test will not be used again in the future. It is to say that, as a matter of analysis and judgment of the experts, the DCF technique has less validity at this time. And that is why I say to you that you should not be utilizing the DCF technique.

That leaves us with the risk premium technique. CAPM and Empirical CAPM are simply

derivatives of the Risk Premium methodology. They have their own drawbacks, as was explained to you by Dr. Waters in response to maitre Morel

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yesterday (3T539ff). But they are essentially risk premium techniques.

What you should conclude from this, in my submission, is one thing, and that is that the gold is to be found in the application of the risk premium technique. It is not to be found in an alchemist's brew of every test known to cost of capital analysts.

Dr. Waters is, in my submission, correct to give sole weight to the risk premium technique. Dr. Morin is partially correct when he emphasizes the risk premium technique over DCF, over comparable earnings. And I would submit to you that the Board would be correct to make your decision on the basis of risk premium analysis.

That leads me to the critical differences between the expert witnesses in their application of the risk premium technique. The major difference relates, of course, to the use of arithmetic or geometric means.

This issue first arose in the 1990 case, where it was debated at length. The Board found merit in Dr. Waters' position that geometric means should be used in the context of utility regulation, but the Board was not thoroughly

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convinced, and it said so (RH-2-90 Decision, pp. 14-15).

I think it is worth considering what the Board's attitude was in respect to the geometric and arithmetic means.

At page 14 of the 1990 Decision you said this:

"The risk premium approach as presented during the hearing drew the most attention. The principal topic of discussion centered on whether the market risk premium should be based on arithmetic or geometric mean. While certain of the arguments put forward by CPA's witness have some merit in the context of utility regulation, the Board was not thoroughly convinced in



this case that geometric means should be used. However, the Board notes that TQM's witness who utilized the more theoretically valid arithmetic mean value of the equity risk premium conceded that the market risk premium was at the low end of the range suggested by his analysis, namely six

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percentage points. Further, CPA's witness who used geometric average values for the market risk premium found such premiums to be 5.7 to 5.9 percentage points prior to adjustment. The Board finds that market risk premiums in this order of magnitude are a reasonable point of departure."

And then you said:

"The Board expects that the merits and drawbacks of each of these approaches will be addressed in future toll proceedings. In particular, the Board would expect any analyses presented on this topic to examine the significance of the differential between expected and achieved equity returns in a utility context."

That is precisely what Dr. Waters has done. That is what his Appendix XIII is about.

You will recall the evidence that he gave to you that Appendix XIII was put into his evidence after this Board's Decision came out in the 1990 case, and it has remained there ever since.

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Dr. Waters has done what the Board asked him to do. But in my submission, TQM and Dr. Morin have not done that.

I suggest to you that this issue should be viewed in the light of a legal maxim that is often argued by lawyers and applied by judges interpreting statutes or contracts, and that is the simple maxim that "the general gives way to the specific".

In the case of this issue, application of the arithmetic mean should give way to the specific application, in the utility context, of the geometric mean. There are lots of articles, some on this record; some placed on this record by TQM, as they were on the RH-2-90

record. These articles say: "Use the arithmetic mean for cost of capital determination." (See eg. Exs. B-30, B-31, B-32).

Nobody disputes that that is what the articles say. None of those articles say: "Use the arithmetic mean for cost of capital determination for utilities."

As Dr. Waters told you yesterday, there is no indication that all of these authors even thought about the arithmetic mean or the

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(Yates)

geometric mean in the context of utilities (3T456-472) and, in particular, the risk reduction features of utilities as regulated by this Board.

But Dr. Waters has. He has thought about this. He has given you Appendix XIII of his evidence (Ex. C-1-4), in response to your admonition in the 1990 Decision.

That Appendix makes the point, very clearly, that in a utility context, where the return actually achieved is very close to the expected return, the geometric mean should be used.

The object of the exercise, in my submission to you, is to determine what constant return would have to be achieved in each year to have investment growth equal a particular proportion of the return achieved by the stock market (1T142).

Dr. Morin did not agree with that general proposition as put to him, but he did concur that the geometric mean measures total wealth over time (1T148). He also concurred that one of the reasons to use the arithmetic mean for each time period, in order to achieve the geometric mean over time, was because of the

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expectation of highly varying returns (1T148).

Generally speaking, returns can vary highly. Specifically speaking, specifically in the utility context, returns vary minimally.

This concept is shown very clearly in Appendix XIII, where Dr. Waters sets out the arithmetic means and geometric means of various pipelines regulated by this Board. It applies equally to TQM.

By its toll methodology, TQM can expect its actual return to be very close to its authorized return. All its costs go into TransCanada's cost of service as Transmission by Others. Virtually all of its tolls are paid by TCPL's customers (1T42ff).

Historically, it has achieved what has been authorized, after taking into account the disallowance by this Board of certain costs which were incurred by TQM (1T39ff) -- and you will recall my discussion with Mr. Heider and Mr. Laforge about the difference between the line of "Authorized Return" and the line of "Achieved Return" on the exhibit.

The validity of utilization of the geometric mean in the context of the virtual

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certainty of recovery of the utility returns was illustrated by the arithmetic example that I discussed with Dr. Morin (1T150-154). In that example, it was clear that the geometric mean would give the required return over time in conditions of virtual certainty of recovery -- and those are, for all practical purposes, the conditions of utilities regulated by this Board. It follows that the geometric mean should be used to determine a utility's cost of capital.

I would like to make a specific reference to pages 153 and 154 of the transcript. This is part of my discussion with Dr. Morin. It was the end of this discussion. I said to him, beginning on the bottom line of page 153:

"What I am asking you is: What would happen if you gave the 13.75 to an entity that does have certainty of recovery?"

The "13.75", you will recall, was the arithmetic mean in the example which I had been going through with Dr. Morin. The question was:

"What would happen if you gave the 13.75 to an entity that did have certainty of recovery? The result is

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that you would end up with ---"  
And Dr. Morin interjected with this response:

"You would over-compensate. You would over-compensate that company. The company is riskless, and you would over-compensate the company."

When Dr. Morin was re-examined by maitre Leclerc, this topic came up. Maitre Leclerc put this question to Dr. Morin -- and this is at page 338, at line 4 (2T338; see also 3T473-479):

"If an investor were asked to invest in either one of these companies today, sir, and was told he was going to get 10 per cent from both companies, would he be indifferent from one to the other?"

And the answer was:

"No, clearly not. There would be nobody in this room who would select Company B" -- (and Company B, you will recall, is the varying returns company) -- "for a 10 per cent rate of return because the returns are all over the place, whereas Company A has very, very

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stable returns.

The investor in Company B will demand a much higher rate of return because of the gyrations, the fluctuations in year to year rates of return."

My response to that is to say:

Precisely. That is precisely the point. With utilities, there are no meaningful gyrations. The geometric mean is, for utilities -- to use Dr. Morin's phrase -- "the right thing to do".

In his Argument this morning, maitre Leclerc said that Dr. Waters' approach has effectively taken utilities out of the market.

Presumably, this is a reference to the securities market.

Utilities are not taken out of the market. But it should be remembered that the reason for undertaking all of this analysis is to establish a rate of return on TQM's book equity.

Dr. Waters has not introduced the particular context which is relevant here, namely the setting of a rate of return on book equity for a corporation. He is applying the data available from financial markets, in this different context, and has identified the relevant financial markets

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item, which is the geometric mean.

We have to keep in mind what we are trying to do here: We are trying to establish the rate of return on book equity for TQM, and we are going to the financial markets to see what it should be.

The market data shows volatility amongst the corporations in the market, sure; but the context of the application -- what we are seeking to apply this whole analysis to -- is a situation which shows great stability, and that is the returns of utilities regulated by this Board.

I have submitted to you that this arithmetic/geometric mean controversy is the essence of the difference between Dr. Morin and Dr. Waters. I do not intend to spend any more time detailing the differences between the methodologies or analyses of these witnesses, but I do rely on the record that has been developed through the exhibits that have been filed in this proceeding and through the cross-examination over the last three days of evidence.

It is, for example, clear from the record that Dr. Morin has raised the level of his results by switching from using a 10-year period

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to a 15-year period (Ex. C-11-3, C-11-4; 2T251-264). It is clear on the record from Dr. Waters' "confession" -- as you called it, Mr. Priddle -- that his prior use of the arithmetic mean was inadvertent and resulted in a higher risk premium than he otherwise would have recommended (3T550ff). It is clear on the record that Dr. Waters has moved from the quantitative adjustments to his risk premium analysis to qualitative adjustments, in recognition of the disputatious nature of those adjustments and the difficulties of quantification.

That move by Dr. Waters is something that the Board will presumably applaud, in the light of its Westcoast Decision (3T375-378).

On these and other issues, I commend to the Board the evidence of Dr. Waters, and I submit to you that it is both credible and compelling.

I do, however, have a few words to say about business risk and capital structure.

We need to look at business risk in the context of the history of TQM. It was conceived with 25 per cent deemed common equity (1T15). It has had 25 per cent deemed common

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equity since inception (1T15). It has not had any problem raising money on reasonable terms (1T15-16).

Notwithstanding all of this, in 1988 it sought to increase its common equity from 25 to 30 per cent. Dr. Morin came to the Board and told you that he believed that while TQM's short-term risks were relatively unchanged, its longer-term risks had increased, essentially due to deregulation (RH-2-88 Decision, p. 8).

The witness for the Canadian Petroleum Association, as it then was, was Dr. Waters, and he demurred. He said that there had been no change in business risks (p. 8).

The Board agreed with Dr. Waters and rejected the TQM request for an increase in the deemed common equity.

I think it is useful to look at what you said in that context. It appears at pages 8 and 9, and is as follows:

"In reaching its decision in this matter, the Board was guided by the following: Considerations relating to the inherent business risks faced by TQM's utility operations, the need to

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maintain an appropriate balance between the debt and equity elements of the Company's capital structure, and the historical evolution of the Company's capital structure.

The Board finds that neither the Company's short-term nor longer-term business risks have increased since last year. The evidence presented in this proceeding did not convince the Board that an increase in TQM's equity ratio was required for the Company to access capital markets at reasonable terms, nor was the Board persuaded that such an increase would be cost-effective from the perspective of the tollpayer.

With respect to historical

considerations, the Board notes that TQM's approved capital structure for tollmaking purposes has been at its present level since 1983 and that there has been apparent market acceptance of TQM's capital structure. Bond rating agencies do not appear to be overly

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concerned about TQM's capital structure and coverage ratios." (RH-2-88 p.8-9).

And you went on to approve the deemed common equity of 25 per cent.

The "cost effectiveness" comment related to the evidence of TQM that under a 30 per cent equity scenario, the cost of service would be higher than it would be under a 25 per cent common equity scenario.

In 1990, this issue got relatively short shrift. TQM did not ask for an increase in common equity. They did not even say that they would accept one, if the Board gave it to them.

Both Dr. Morin and Dr. Waters indicated that there was little or no change in the business risk of TQM since the previous proceeding. And that was the conclusion that the Board reached (RH-2-90 Decision, p. 8).

In the present case, TQM does not ask for an increase in its common equity ratio, but it does say that it will gladly accept one, if given by the Board (1T17). It relies on the reasons that it advanced in 1988.

You should not give TQM an increase in equity, and you should not do so for the same

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(Yates)

reasons as were set out in 1988 (1T21).

First, there is simply no evidence that an increase in the equity ratio is required to access capital markets at reasonable terms. The only evidence is to the contrary (1T15).

Second, there is clear evidence that such an increase would not be cost-effective from the perspective of the tollpayer. The example that I discussed with Mr. Laforge and Mr. Heider showed a \$1.3 million increase in the cost of service (1T22ff); and the potential reduction in

return on equity that might come with an increased equity ratio was shown to be minimal by comparison (1T52ff).

Third, there is no evidence that bond rating agencies are, to use the Board's words, "overly concerned" about TQM's capital structure and coverage ratios (RH-2-88, p. 9).

And finally, the Board should conclude that neither the short-term nor the long-term business risks of TQM have increased. Dr. Morin says so himself. He says, and I quote:  
 "Since the last rate of return decision, TQM's overall risk has not changed significantly." (2T160; Ex. B-4

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 (Yates)

p. 17).

He also says, and I am quoting again:

"TQM's risks are in fact slightly below average, relative to the industry."  
 (2T160; Ex. B-4 p. 190).

This compares to his assertion of increased risk in his previous evidence (2T160).

Dr. Waters tells you that there is no change in business risk (3T528ff).

I suppose the question is: Why are we even talking about this? And I suppose it is because of the different tune that was sung by Dr. Morin in his Responses to Information Requests from the Board (IR No. 2, Item 38; Ex. B-8; 2T1644ff). It may also relate to his comments on the restructuring of the economy.

All of the discussion -- and when I say "all of the discussion", I am referring primarily to my cross-examination of Dr. Morin and maitre Leclerc's cross-examination of Dr. Waters. All that discussion leads us back to the same conclusion: the business risks have not changed.

There was a great deal of arm-waving about things like bypass, and negotiated or arbitrated prices in sales contracts, and the

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 CAPP Arg.  
 (Yates)

potential for change in the TQM toll methodology (2T162-178). But that is all it was, it was arm-waving.

Dr. Morin volunteered that this area was not his area of expertise (2T170), revealing no knowledge of potential bypass. Faced with the Board's Decision in RH-3-86 -- which is to say



with the fact that the toll methodology was determined by the Board to have been established and continued in the light of past economic, political and investment decisions (2T177), and with the fact that the Board's primary concern was with fair and equitable allocation of the sunk costs -- faced with those facts, Dr. Morin was forced to fall back on saying that his was a longer-term concern, not a shorter-term concern (2T178).

On the "contracts" question, Dr. Morin effectively acknowledged the benefits of market-sensitive pricing in the enhancement of volumetric takes (2T164-168), and it follows from that, the enhancement of pipeline utilization.

Mr. Leclerc raised with Dr. Waters the spectre of governmental change in Quebec (3T420ff), and asked him about other aspects of

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(Yates)

business risk.

It was, in my submission to you, Dr. Waters who put this all in the proper perspective. He said, essentially, that unless GMi "goes down for the count", the TQM risk is unchanged (3T 534ff). There is no evidence that GMi is going down for the count.

Sure, they sold less gas in 1991 than 1990. But 1990 was the highest number in five years (3T410-411). And the decline was all of seven units out of 189.

This is not "gloom-and-doom" territory. This is not even "cause-for-concern" territory. It certainly is not compelling evidence of increased business risk to TQM. No case has been made to support a conclusion of increased business risk. No case has been made to support increased equity for TQM. The Board should keep the equity ratio at 25.

The conclusion that we come to is this: Dr. Waters says: Use the risk premium method and give TQM 11 1/2 to 11 3/4. And I submit to you that Dr. Waters' evidence should be found by you to be reliable and compelling. It leads you to the "gold".

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(Yates)

Dr. Morin, as of Tuesday, says 13 to 13 1/4. I submit to you that his evidence is alchemy. It does not turn the data into gold,

only lead. You should reject it.

I have one final comment that relates to matters other than rate of return and capital structure. It acknowledges the fact that CAPP has not participated in the written portion of this proceeding. The participation of the Association has been limited to rate of return and capital structure, in reliance on the expertise and diligence of the Board and its Staff in dealing with the other matters.

The only matter which I wish to comment on is the matter raised in a recent letter by the Board, in respect to the disposition of the, I believe it is now, \$780,000-odd in deferral accounts.

CAPP suggests that that amount should be credited to the 1993 TQM cost of service, thereby giving the earliest and most direct benefit to the tollpayers.

Those are my submissions, Mr. Chairman, unless there are questions.

THE CHAIRMAN: Thank you very much,

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Plaidoirie GMi  
(Hebert)

MR. MOREL: Mr. Hebert for GMi is next.

PLAIDOIRIE AU NOM DE GAZ METROPOLITAIN, inc.

Me HEBERT: Monsieur le President, madame, monsieur les membres, contrairement a ce que je vous mentionnais mardi dernier, on m'a libere. Alors, il me fait plaisir d'etre ici ce matin pour livrer les brefs commentaires de Gaz Metropolitain.

Comme a l'habitude, j'ai remis copie de mes notes aux stenographes.

Tel que nous vous le mentionnions lors de notre comparution mardi dernier, nos remarques seront tres breves. En effet, nous n'avons pas participe activement aux audiences et plus particulierement a cette partie de la cause qui traite du taux de rendement et de la structure du capital de la compagnie Gazoduc Trans Quebec & Maritimes. Nous n'avons donc aucun commentaire sur ces deux enjeux.

Il va sans dire, monsieur le President, que l'interet de Gaz Metropolitain dans cette cause est tout de meme evident et connu. Rappelons seulement que TQM transporte une partie importante des approvisionnements gaziers de Gaz Metropolitain a partir du point de livraison

de Saint-Lazare. De plus, les couts du systeme pipelinier de TQM sont integres dans le cout de service de TransCanada PipeLines Ltd., dont Gaz Metropolitain est

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Plaidoirie GMi  
(Hebert)

l'un des expediteurs et payeurs de droits importants. Enfin, Gaz Metropolitain est la seule cliente de TQM au Quebec pour les services de transport et de stockage.

Comme a l'habitude, le dossier tarifaire de TQM a ete analyse par mes collegues chez Gaz Metropolitain et, plus particulierement, par monsieur Bulger.

Suite a l'analyse du dossier, nous avons cru opportun de transmettre une demande de renseignements a Trans Quebec & Maritimes. Il s'agit de la piece C-4-2. Cette demande traite notamment des depenses d'exploitation de TQM qui, avouons-le, constituent une preoccupation tout a fait legitime dans le contexte economique actuel, et surtout dans le contexte of Gaz Metropolitain veut penetrer de nouveaux marches.

A cet egard, nous vous soumettons que les interets de TQM et ceux de Gaz Metropolitain vont dans le meme sens. Nous referons aussi a la maximisation des infrastructures de transport pour TQM et des infrastructures de distribution pour Gaz Metropolitain. Pour ce faire, les couts de transport et de distribution du gaz naturel doivent etre competitifs.

Toujours dans le contexte economique actuel qui est caracterise par la recession, les problemes de cout de service et de developpement de marche sont en effet exacerbes. Nous notons cependant que les choses

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(Hebert)

vont dans le bon sens. L'amortissement des infrastructures de TQM se traduit par une poursuite de la diminution de ses tarifs. Comme Gaz Metropolitain ne requiert pas de nouvelles capacites presentement, cette tendance devrait se poursuivre, et ce, dans le meilleur interet des consommateurs de gaz naturel au Quebec.

A notre avis, monsieur le President, TQM devra donc continuer de contrIler etroitement ses depenses d'exploitation et de transmission afin que ses tarifs continuent de diminuer pour demeurer justes et raisonnables, tel que le prescrit l'article 62 de la loi sur l'Office national de l'energie.

A cet egard, je note avec satisfaction les remarques que mon confrere maitre Leclerc faisait ce matin a l'effet que TQM entend deployer tous ses efforts pour reduire ses depenses d'exploitation.

Ceci complete les commentaires de Gaz  
Metropolitain, monsieur le President, commentaires que nous  
vous soumettons respectueusement.

Je vous remercie.

LE PRESIDENT: Merci, maitre Hebert.

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APMC Arg.  
(Moreland)

MR. MOREL: Mr. Chairman, it is  
now Ms. Moreland's turn, on behalf of the APMC.

ARGUMENT ON BEHALF OF THE ALBERTA PETROLEUM  
MARKETING COMMISSION:

MS. MORELAND: Thank you,  
Mr. Chairman.

I have not given a copy of my remarks  
to the Reporter but will do so, when I am through,  
with a plea that he attempt to decipher them and  
include the evidentiary references.

Mr. Chairman, the APMC's argument on  
fair return on equity for Trans Quebec & Maritimes  
is going to deal with the question that you,  
Mr. Chairman, put to Dr. Morin on Wednesday. You  
will recall, sir, that you asked him, in "agnostic  
mode": "Why should I believe you? Why should I  
believe anybody?" And in particular: "Why should  
I believe you more than the other side?" (2&331).

The APMC submits that you have been  
given good solid, thoroughly researched and  
considered evidence in this case, and that is the  
evidence of Dr. Waters, and he should be believed.

A comparison of the approaches taken  
by Dr. Waters and Dr. Morin shows you that  
Dr. Waters' systematic, careful approach to

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APMC Arg.  
(Moreland)

generating the right value for return on equity  
for TQM should be the one that you, as a  
regulator, can feel comfortable adopting.

When I say that Dr. Waters' approach  
is the "right" approach, I think it is valuable to  
think about the analogy that he went through  
yesterday while he was being cross-examined.

You will recall that he talked about  
the analogy of NASA attempting to put people on

the Moon 20 years ago (3T389ff).

Dr. Morin tells you that you should feel comfortable with his "multiplicity of tests" approach.

In my submission, Mr. Chairman, this is analogous to feeling comfortable that, if NASA wanted to achieve its objective of getting to the Moon, it would send up a host of spacecrafts, without having performed a very careful analysis about the best way to achieve the objective; that NASA would simply feel comfortable in the belief that, on average, it might hit the target.

Dr. Morin has no difficulty telling you that of the nine tests that he performs, he throws two of them out because he does not like the results. He concludes they won't even hit the

target. In fact, they are not even given an opportunity to hit the target. He does not even get them to the "truncation" stage.

Of the remaining seven tests, he truncates results based on the highest and the lowest of results arising out of each test. In fact, what he does is he truncates the two extreme values for the low point, the high point and the midpoint of the range for each of his tests.

I do not know what Dr. Morin would have you do with that. I do not know what he would have you make of that approach. He shows you 21 values on his final "Summary of Results", and he truncates six of them. The six need not be restricted to only two specific tests. They can, and in fact they do, apply rather haphazardly, I would suggest, to five tests.

The logic of this approach, Mr. Chairman, is puzzling.

So once the truncation process is completed, there are fewer spacecraft left, in Dr. Morin's world, that can potentially hit the target. There is no comfort level or assurance that the analysis which has been undertaken will ensure that the target is reached.

I submit to you that one would have few volunteers for the space program based on Dr. Morin's approach to sending up missiles on the

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APMC Arg.  
(Moreland)

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APMC Arg.  
(Moreland)

chance that they might or might not get where they are going.

There is no sense of confidence about where one might go if the approach is not detailed and methodical. The detailed precise methodical approach is to be preferred in assessing fair return.

I would like to turn to a brief discussion of some of the reasons why I submit to you that Dr. Morin's approach will not get this Board to the objective of setting a fair return for TQM, the first being a discussion of the Comparable Earnings Test.

#### COMPARABLE EARNINGS

As you know, Dr. Waters does not perform a Comparable Earnings analysis, and you know from this appearance and from others that he does not do that because he believes the data are unreliable for establishing what has truly been earned by companies and what should be done with that information in the present context -- that is utility regulation -- even if that data were

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APMC Arg.

(Moreland)

accurate (3T391ff).

Dr. Morin acknowledges that the Comparable Earnings Test is his least preferred of the tests that he in fact gets to the truncation stage (2T201).

It is "not a true measure of opportunity costs", he says; "it ignores capital markets", he says; and "it cannot be adjusted properly for inflation" (2T202).

Dr. Morin has called this test a "dinosaur" in the context of the U.S. regulatory world. He told you that he likes the test more in Canada because of the paucity of other Canadian data.

Notwithstanding that he likes the Comparable Earnings Test better in the Canadian context, he agrees that the criticisms of the Comparable Earnings Test -- that is, that it is driven by accounting data and hence does not accurately depict economic reality -- exist both in the U.S. and in Canada (2T204).

I submit that the Board should be reluctant to place any weight on the Comparable Earnings Test in Canada.

The conceptual drawbacks that

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APMC Arg.  
(Moreland)

Dr. Morin has identified are not ameliorated by telling you that you should rely on the test "because the data are available and there are other data that you might be able to use if you are in the United States".

In any event, having gone through a discussion of the Comparable Earnings Test, Dr. Morin truncates it, or at least I think he truncates it, because he truncates the midpoint value (1T109); he eliminates the Comparable Earnings result.

So even on his own analysis, it does not get very far out of orbit before it gets destroyed by the truncation process.

In my submission, Mr. Chairman, you should reject it -- not because of the truncation process, but because of the admitted weaknesses of the test when the purpose is setting a fair return for the utility.

DCF - GENERAL

I would like to move to a discussion of Dr. Morin's DCF tests. Dr. Morin does three DCF analyses. Again, one of these tests, to continue on the "space" theme, does not even make it off the lift-off pad. It does not even get the

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APMC Arg.  
(Moreland)

opportunity to be truncated after leaving orbit. That test is the DCF energy utilities test, which Dr. Morin excludes because the results, as he says, are unreasonably high (2T208).

He is left with his industrial and his telco DCF tests.

The DCF telco test is based on a sample of regulated telephone utilities.

Dr. Morin agreed, when we were discussing this the other day, that the DCF test for telcos suffers from circularity. Obviously, the returns are returns based on awards made by regulators and, hence, contain the implicit assumption that returns will be continued, on average, over time (2T227).

This Board indicated, in the last TQM case, RH-2-90, that it placed little weight on the utility DCF tests performed by Dr. Morin then, in

part because of the circularity problem he agreed exists with that (RH-2-90 Decision, p. 15).

He suggested in this case that he heeded your advice and that he, therefore, excluded the energy DCF results this time as part of his recommendation.

But in fact Mr. Chairman, Dr. Morin

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APMC Arg.  
(Moreland)

did not really exclude the energy utility DCF results because of circularity concerns; he excluded them because he did not like the results. The results were unreasonable (2T253).

The conceptual difficulty of circularity of utility DCF exists for his DCF telcos, and the DCF sample he has used in the past has only been deleted because of the result, not the circularity.

DCF GROWTH RATES

In respect to the growth rates that Dr. Morin employs in his DCF analysis, Mr. Yates told you that he has used a 15-year growth rate to measure the DCF model in this proceeding.

He used a 10-year growth rate in RH-2-90; and he has told that he uses a 5-year or a 10-year growth rate in developing his DCF evidence in U.S. proceedings.

As indicated in Exhibit C-11-4, which was the comparison of the 15-year and 10-year growth rates ending in 1991, one can see that the 15-year growth rates are all higher than the 10-year rates for each of Dr. Morin's DCF samples.

Even after the revision to his

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APMC Arg.  
(Moreland)

industrial sample and a recalculation of growth rates for the most current earnings and dividends per share data, rather than his historical reliance on FRI growth rate computations, the 10-year rates are still lower than the 15-year rates (2T258ff).

As Madame Cote-Verhaaf noted, and as Dr. Morin agreed, when one computes growth rates including the period prior to 1981-1982, the inflation rates existing in those early years have a dramatic effect on those (2T318).



I submit the effect is dramatic. It is evidenced by Exhibit C-11-4, and the use of a 15-year growth rate should simply be rejected.

Dr. Waters' approach of weighting 5-, 8- and 10-year growth rates, in my submission, is to be preferred, as it provides balance, and the rates generated by that approach bear significant relation to today's investor expectations regarding prospective inflation. They do not give weight to historical growth, which was driven by the very high inflation represented by the 15-year rates, which exceed investors' current expectations as to future inflation.

DCF QUARTERLY MODEL

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APMC Arg.  
(Moreland)

The next issue in respect of Dr. Morin's DCF test is the use of a quarterly model.

As you heard, Dr. Morin uses a quarterly DCF compounding model, which has the effect of increasing his DCF results by approximately 20 to 30 basis points over the results that would obtain if he used an annual model (2T266).

Dr. Morin says that that is a "mismatch" between return on equity calculated quarterly and a rate base construct which assumes accumulation of earnings on an annual basis (2T275).

He is right. He is perfectly right. That is why the quarterly model does not fit TQM's circumstances.

This is a matter which Dr. Waters analyzes -- and you can find that in Appendix VIII to his Evidence.

The use of a quarterly DCF model and an average annual rate base would result in an over-allowance.

The CRTC has told Dr. Morin that, in its view, it wants experts using a quarterly DCF

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(Moreland)

model to make an adjustment to their results to reflect the use of an average annual rate base

(2T270 and 274).

Dr. Morin agreed that he will adjust his DCF model the next time he gives evidence before the CRTC, if that is the wish of the CRTC (2T276).

I submit that the NEB, too, should reject Dr. Morin's quarterly model and should similarly direct expert witnesses relying on the quarterly DCF model -- and, parenthetically, apparently Dr. Morin is aware of no other witnesses who appear before this Board who use that model (2T276) -- that they should be directed to adjust the model to reflect the existence of annual average rate base.  
CAPM/ECAPM

Moving to the CAPM and ECAPM which Dr. Morin uses: As Mr. Yates told you, the CAPM and the ECAPM are variations on the equity risk premium theme. Dr. Waters summed up these two tests very well by saying that the tests tell you something, but they do not tell you everything (3T543).

Dr. Waters told you that the CAPM and

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APMC Arg.  
(Moreland)

ECAPM models suffer, to the extent that not all practitioners, or academics for that matter, concur that beta is the sole and complete indicator of the risk of securities for which a risk payment is expected by investors (3T541). In fact you will recall that Dr. Waters uses five measures of relative risk in his analysis. He does not just use beta.

Moreover, the Arbitrage Pricing Model, of which Dr. Morin spoke, identifies several factors -- not just one; not just beta -- which in total describe the risk characteristics of a security.

I would like to focus for a moment on the adjustments that Dr. Morin makes to the CAPM model to give us the ECAPM model (3T540).

First, he makes an adjustment to the beta because he is of the view that the CAPM model produces a downward-biased estimate of equity costs for companies with betas -- that is, relative risk values -- of less than 1.00 (Ex. B-4 p. 35).

He agreed with Mr. Yates the other day that if one observed that beta values for

low-risk utilities did not regress toward the mean

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APMC Arg.  
(Moreland)

in subsequent periods, it would be inappropriate to adjust beta values (1T140).

As Dr. Waters said, the beta adjustment to the CAPM model exists because one says that the initial, the original assessment of "beta" under the CAPM, as the indicator of risk, is not enough, because the relation of outcomes of securities and beta values do not necessarily coincide with what you expected. So you have to adjust the beta (3T542). You adjust the beta for "drift" because you have measured the relative risk imprecisely in the first place because you have used beta values, which cannot tell you everything you need to know about risk (3T543).

The ECAPM, I suggest to you, is best described as "a patch upon a patch". You are correcting for something that you got wrong in the first place, or that you measured imprecisely in the first place.

If one is careful (as Dr. Waters is) in establishing the relative risk of utilities through a number of approaches, you can observe that utilities do have a systematically lower risk which does not drift toward that of the market portfolio. They are truly low risk (3T512).

0651

APMC Arg.  
(Moreland)

I commend to you, Mr. Chairman, Dr. Waters' Response to TQM's Information Request No. 4(b) (Ex. C-1-5) for a discussion of the estimate of beta values in the context of low-risk companies that have been identified as low-risk companies on other criteria.

After adjusting for beta, an adjustment which produces a higher cost of capital for utilities (2T281) -- that is, as soon as you adjust the beta, you wind up with a higher cost of capital -- Dr. Morin then uses the equation that you find at page 35 of his Evidence, which again results in a further increase in the cost of capital estimate.

The second adjustment -- that is, the weighting found at the equation on page 35 of his Evidence -- is ad hoc and, I would suggest, is best described as "a patch upon a patch upon a patch". We have adjusted three times.

QUALITATIVE ADJUSTMENT

I would like to move to a brief discussion of the "qualitative" versus "quantitative" adjustments that Dr. Waters has made in this case.

As you know, and as you have heard

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APMC Arg.  
(Moreland)

from maitre Leclerc, and briefly from Mr. Yates this morning, Dr. Waters has not in this case made a quantitative adjustment for the purchasing power risk premium or the shortfall between investors' anticipated and achieved returns when he performs his equity risk premium.

He has told you that why that is so is because the specific adjustments have become disputatious and controversial in the past, and he prefers to now deal with them in a qualitative sense, tending to emphasis the lower end of his range (Ex. C-1-4; 3T353).

He has arrived at this conclusion on the basis that the Board's interests will be best served by dealing with these issues in a qualitative, rather than a quantitative, sense.

I suggest to you, Mr. Chairman, that you have to be mindful of the fact that return on equity analysis is not static; that it must constantly be augmented and refined to produce the most fruitful approach and result (3T560).

It was also suggested, both through cross-examination and in argument this morning, that Dr. Waters makes two adjustments for risk when he, firstly, utilizes the geometric mean --

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APMC Arg.  
(Moreland)

and I will not repeat what Mr. Yates had to say about that this morning -- and, secondly, selects a relative risk value.

The geometric mean is used because the arithmetic mean of the market risk premium would give the utility cumulative returns in excess of the intended values.

Mr. Yates talked about that at some length.

The choice of the geometric mean is not based on the relative risk value of securities of the utility in question; rather, it is based on the observed and the predictable stability of the

rate of return on rate base outcomes for utilities regulated by this Board. That is the essence of what Mr. Yates told you.

The second adjustment -- being the selection of a relative risk value -- is a completely separate issue. That issue is driven by the proportion of the market index value that the Board wishes the utility to achieve.

Mr. Chairman, there is simply no "double dipping" for risk. There are two separate issues. And Dr. Waters is not "tampering with the machine", as maitre Leclerc suggested

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APMC Arg.  
(Moreland)

this morning.

Finally, in response to two brief comments that maitre Leclerc made this morning with respect to Dr. Waters' adjustments made without empirical support, he suggested that Dr. Waters 50 basis point "cushion" was made without any empirical support.

I would commend to you Dr. Waters' discussion with maitre Leclerc at page 373 of yesterday's transcript. It is worth reading a very brief portion of this into the record, because I am at a loss as to how maitre Leclerc has determined that Dr. Waters makes this adjustment without empirical support.

What he says at page 373, and following is:

"Q I take it, sir, that these adjustments are judgments on your part and not empirical computations?

A I think that is fair -- oh, the 50 basis points is not. That is an empirical computation. That is based on my examination of the volatility of long-term interest rates over the past seven or eight years."

0655  
APMC Arg.  
(Moreland)

That sounds empirical to me.

"What I do is I look at monthly data and see to what extent actual values of long-term interest rates deviate in subsequent months from the value that prevailed at the beginning of the year.

I am looking at the extent to which

long-term bond investors could have been wrong in their forecasts of interest rates for the full year, and then I have taken, I believe, one standard deviation from the mean value ---"

Again, that sounds fairly empirical.

"-- and that is approximately 50 basis points."

And Dr. Waters concludes the answer by saying:

"So, the 50 basis points is empirically determined."

The second adjustment that maitre Leclerc suggested was made without empirical support is the adjustment in respect to the DCF analysis, the 60 to 80 basis points.

I would just ask that the Board

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APMC Arg.  
(Moreland)

review transcript 355 of yesterday through to line 17 of transcript 356, and there you will see that there is a discussion of the empirical basis for that as well.

CONCLUSION

In conclusion, Mr. Chairman, I submit to you that if you do want to reach your target of setting a fair rate of return for TQM, you should rely on the careful, comprehensive analysis undertaken by Dr. Waters and the recommendations that arise from that analysis.

You should not rely on the "many spacecraft" approach of Dr. Morin, hoping that one of them will get you where you want to go.

I commend to you the comments made by Drs. Waters and Morin in response to the question that Mr. Priddle asked each of the witnesses this week. That question was whether or not, in the view of the witnesses, regulators should divulge their "recipes" or give the witnesses some idea of what it is that the regulators found persuasive, or not.

Dr. Morin said, in essence: If I were you, I would not divulge anything in 'the black box' (2T324); Dr. Waters said: Yes, I would

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APMC Arg.  
(Moreland)

find that kind of information helpful.

He wanted, as he termed it, "full, true disclosure" of the process (3T559). He told you that a "dialogue" would give you more useful results and responses in the future, without

unduly restricting your ability to change, due to changed circumstances which you saw as relevant (3T560).

The "full, plain, true disclosure" advocated by Dr. Waters is indicative to me of an analyst who wants all of the relevant data at hand, including what you, the adjudicator, find relevant, and why, so he can go away and fine-tune, evaluate, and constantly re-evaluate the best possible way to hit the target.

The "black box" approach gives absolutely no additional data to the "NASA scientists" so they can reduce the number of ships sent up with little but the fond hope that one of them might make it.

Subject to any questions, Mr. Chairman, those are my remarks.

THE CHAIRMAN: We do not have any questions, Ms. Moreland. Thank you very much.

MS. MORELAND: Thank you.

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Plaidoirie - PGQ  
(Robitaille)

LE PRESIDENT: Maitre Robitaille.

PLAIDOIRIE AU NOM DU PROCUREUR GENERAL DU QUEBEC:

Me ROBITAILLE: Bonjour, monsieur le President, madame et monsieur les membres.

Nous avons remis au service de traduction et de stenographie le texte de notre plaidoirie. Nous ne repeterons pas les references aux pieces, mais nous aimerions cependant qu'elles soient reproduites dans la transcription.

Me ROBITAILLE: Le 28 aout 1992, Gazoduc Trans Quebec & Maritimes Inc. (Gazoduc TQM ou TQM) a demande a l'Office national de l'energie (l'Office ou ONE), aux termes de la Partie IV de sa loi constitutive, de lui delivrer entre autres certaines ordonnances concernant les droits.

Dans sa demande (piece B-1), Gazoduc TQM a propose que l'Office suive une procedure semblable a celle utilisee au cours de la derniere audience concernant les droits exigibles par TQM. L'Office a donc decide, dans son ordonnance d'audience (piece A-1) de proceder par voie de memoires pour toutes les questions a l'exception de celles portant sur le taux de rendement.

Dans ce contexte, notre plaidoirie portera sur le taux de rendement demande par Gazoduc TQM.

Gazoduc TQM propose de continuer la pratique

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Plaidoirie - PGQ  
(Robitaille)

etablie dans les audiences anterieures en soumettant des taux de rendement pour deux annees-temoins, 1993 et 1994. Le taux de rendement accorde pour les quatre dernieres annees a ete de 13,75 pour cent (Schedule 58.A, piece B-19).

Monsieur Roger Morin a recommande a TQM un taux de rendement sur l'avoir ordinaire entre 13 pour cent et 13,25 pour cent respectivement pour 1993 et 1994 (Tr. Vol. 1, page 75) afin de conserver son integrite financiere et son pouvoir d'attirer du capital. Son taux de rendement est calcule en fonction de la moyenne de sept methodes d'evaluation standards (piece B-4, p. 49).

Pour sa part, monsieur Waters demontre dans sa preuve ecrite (piece C-1-4) et dans son temoignage verbal (Tr. Vol. 3) que le taux de rendement demande par Gazoduc TQM est trop eleve et que celui-ci devrait plutit s'etablir entre 11,50 et 11,75 pour cent (piece C-1-4, page 2).

Le Quebec considere que plusieurs elements du dossier confirment le bien-fonde de cette conclusion. Nous allons traiter de ceux qui nous apparaissent particulierement pertinents.

1 - LE TAUX DE RENDEMENT OBTENU PAR D'AUTRES SOCIETES INDUSTRIELLES

Selon la preuve ecrite de monsieur Waters

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Plaidoirie - PGQ  
(Robitaille)

(piece C-1-4, tableau 7), la moyenne des taux de rendement obtenue par 208 compagnies est de 7,6 pour cent et 3,7 pour cent en 1990 et 1991 respectivement. Par contre, le taux de rendement obtenu par TQM a ete de 11,23 pour cent et 11,17 pour cent pour la meme periode (Schedule 58.A, piece B-19).

Gazoduc TQM a donc beneficie d'un taux de rendement superieur a la moyenne de 3,63 pour cent en 1990 et de 7,47 pour cent en 1991. Un tel ecart justifierait, a notre avis, une reevaluation du taux de rendement demande pour les deux prochaines annees.

2 - LA BAISSSE DES TAUX D'INTERET

Tel qu'il appert de la preuve ecrite de monsieur Waters (C-1-4, page 5), le taux des obligations a long terme du gouvernement du Canada de 10 ans et plus a baisse de 1,61 points de pourcentage entre la mi-decembre 1990, lors de la derniere audience de TQM, et la mi-octobre



1992. Par contre, le nouveau taux de rendement demande de 13,25 pour cent par Gazoduc TQM n'a baisse que de 0,50 point de pourcentage par rapport au taux accorde dans la cause RH-2-90, soit 13,75 pour cent.

A notre avis, cette baisse des taux d'interet est un facteur important a considerer lors de l'etablissement du taux de rendement accorde a Gazoduc TQM.

3 - LE RENDEMENT ACCORDE A D'AUTRES SOCIETES REGLEMENTEES

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(Robitaille)

Le tableau 16 (piece C-1-4) de la preuve ecrite de monsieur Waters enumere les taux de rendement accordes a plusieurs entreprises d'utilite publique dont certaines oeuvrent dans le domaine du transport par pipeline.

Nous soumettons que le nouveau taux de rendement sur l'avoir ordinaire demande par TQM est de loin superieur aux rendements accordes recemment. En effet, en 1992 l'ONE a fixe a 12,50 pour cent le taux de rendement applicable aux trois compagnies suivantes: Interprovincial Pipe Line, Trans Mountain Pipe Line et Westcoast Energy Inc.

Le Quebec croit que cet ecart de, 75 point de pourcentage entre le taux demande par TQM et ceux accordes recemment, soit 13,25 pour cent moins 12,50 pour cent, est un facteur important a considerer lors de la decision de l'Office.

4 - INTEGRITE FINANCIERE DE TQM

En reponse a la demande de renseignements numero 1 de l'Office (piece B-9, question 9), Gazoduc TQM admet que le risque corporatif de l'entreprise est considere comme etant de "categorie faible". Par contre, son risque financier est plus eleve, creant ainsi un risque total superieur a la moyenne des compagnies de services publics. Ces differents risques se quantifient

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(Robitaille)

par la cote de credit de B++.

En reponse a la demande de renseignements numero 2 de l'Office (piece B-18, question 50B), Gazoduc TQM mentionne qu'elle a ete en mesure de se financer a des conditions adequates.

De plus, l'agence de credit DBRS considere que les benefices degages de TQM sont acceptables pour sa cote de credit (piece B-18, question 45).

Compte tenu de ce qui precede, le Quebec estime qu'un taux de rendement inferieur au taux demande n'affecterait pas l'integrite financiere de cette societe.

CONCLUSION

Le Quebec croit que le taux de rendement demande, soit 13 a 13,25 pour cent, est exagere vu le contexte economique prevu pour 1993.

Le Gouvernement du Quebec suggere donc a l'Office d'approuver un taux de rendement de 11,75 pour cent sur l'avoir ordinaire pour les annees 1993 et 1994, base sur un ratio de 25 pour cent d'avoir ordinaire.

Ceci complete notre plaidoirie, monsieur le President.

Merci de votre attention.

LE PRESIDENT: Merci beaucoup, maitre Robitaille.

Maitre Leclerc...?

0663  
Plaidoirie - PGQ  
(Robitaille)

Me LECLERC: Est-ce que je pourrais avoir environ dix minutes, monsieur le President, pour preparer la replique?

LE PRESIDENT: Certainement.

--- Recess/Pause

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Rebuttal - TQM  
(Leclerc)

--- Upon Resuming

MR. CHAIRMAN: Mr. Leclerc, please.

MR. LECLERC: Mr. Chairman, in reply to the arguments of my colleagues, the first comment I would like to make is that I find it regrettable that, instead of addressing the real issues, they would have chosen to make comparisons between baseball, spaceships, and the like.

Mr. Yates reproaches the fact that Dr. Morin would have updated his information to the very last minute.

That is what I gather from his comments, sir.

You must remember that Dr. Morin's Evidence was prepared back in May, the end of May and the beginning of June of this year, and it was more likely that he would have had to have made these changes, and it was preferable that these changes be made before the hearing of the evidence, as opposed to making them in advance.

On the other hand, Dr. Waters himself made an update at the very last minute, but yet

totally disregards it.

Mr. Yates stressed the fact that Dr. Morin appears to have completely discarded his

0665  
Rebuttal - TQM  
(Leclerc)

DCF analysis as being "unreliable" and "too low". And I suggest to you, sir, that Dr. Waters does, for all intents and purposes, the same thing.

Mr. Yates reproaches Dr. Morin for using the accounting data, or accounting numbers; the techniques for accounting data or numbers, specifically referring to the Comparable Earnings technique. But yet he fails to indicate that two of the five measures of risk that Dr. Waters relies upon are also based on accounting data. I refer you in that regard to pages 52 and 54 of his Evidence.

I was pleased to see, sir, that in addressing the issue of arithmetic versus geometric average, Mr. Yates would have referred the Board to its findings in the RH-2-90 Decision, where the Board had found that the range which was then discussed was an acceptable departure point.

I would like to remind Mr. Yates and the Board that the 5.7 per cent range which was found acceptable was then the arithmetic average.

Mr. Yates claims that Appendix XIII addresses the question which was asked by the Board, and I submit that that is simply not the case.

0666  
Rebuttal - TQM  
(Leclerc)

What Appendix XIII says is that you should apply the average which would fall from the observation of utilities to the market as a whole.

Again, sir, that is a complete departure from the basis of the Risk Premium technique.

One of the most important aspects of this is that Dr. Waters recognizes that his study is based on the fact that returns appear to be constant. A constant return implies zero risk.

This is contradicted by the position he has taken year after year after year in these proceedings that, in general, utilities have a risk which is 50 per cent that of the market.

How can you reconcile these two situations? It is "double dipping". There is no doubt about that.

With regard to Mr. Yates' comments concerning the historical situation as a justification for the past, he has stressed the fact that since TQM had been able in the past to obtain financing on reasonable terms, that that should be an indication that it can do so in the future.

0667  
Rebuttal - TQM  
(Leclerc)

I would suggest to you, sir, that that has nothing to do with it. What is most important, and what will be the considering factor, the most important factor, will be the conditions that prevail at the time that the Company goes into refinancing. Irrespective of how the Company was viewed in the past -- that may be an element, of course -- it is the conditions that will prevail at the time that will determine whether the cost of capital will be reasonable.

Let me now turn to Mr. Yates' last comment concerning the disposition of the Deferral Account.

I understood him to say that the CAPP supported the position of crediting this amount against TQM's Cost of Service. I was not clear as to whether he meant that as a lump sum payment at the outset, credit at the outset, or that it was to be credited throughout the year.

It is our position that everyone concerned, TQM's and TCPL's tollpayers, would benefit if it were an up-front credit for the full amount.

I was rather amused by the constant references by Ms. Moreland to the situation of

0668  
Rebuttal - TQM  
(Leclerc)

NASA.

I just cannot imagine that NASA would have contemplated sending someone to the moon without backups. It just seems unimaginable.

She, again, says that Dr. Morin dislikes his DCF results and therefore discards them.

I again point to you, sir, that Dr. Waters has, for all intents and purposes, done the same thing.

A lot was said of Dr. Waters' growth rates in the DCF technique. What I find most revealing is that Dr. Morin stresses the need to look at the longer periods. We see that Dr. Waters, in previous evidence, had used five and eight year periods and is now moving towards a longer period.

You must ask yourself: Why? I submit to you that it is because that is one of the fundamental precepts of the techniques. Otherwise, you are changing the technique.

Ms. Moreland made reference to the betas of utilities and the fact that one should not look at adjusted beta, if I understood her correctly.

Whatever the discussion, whatever the views that Ms. Moreland put forth in that regard, sir, if you look at the end as a result of what Dr. Waters has done, he has effectively used an adjusted beta when he states that the relative risk of TQM in respect of the market is .60 per cent.

If that is not an adjusted beta, I do not know what is.

With regard to the "quantitative" versus "qualitative" adjustment, after having hearing my colleagues, sir, we are still faced and remain with our fundamental concern. We just cannot explain how, over two, three, or four years, Dr. Waters has been making such a point of these two adjustments and has quantified them to the level of 300 basis points.

If we were to apply today, using his technique, the same adjustments, if I take the 11 3/4s per cent upper range of his recommendation and I deduct from that the 300 basis points, we would end up with a rate of 8.75 per cent.

Mind you, we recognize that that would have to take into consideration the relative risk, which would bring it back up. But

0669  
Rebuttal - TQM  
(Leclerc)

0670  
Rebuttal - TQM  
(Leclerc)

nonetheless, the order of magnitude of these adjustments would bring us to virtually a risk-free rate, which I submit to you is not reasonable.

In my closing remarks, Mr. Chairman, what I would like to do is draw the Board's attention to the words of Dr. Morin at page 323, the bottom of the page.

A lot was made about the fact that Dr. Morin is suggesting various techniques and indeed the need to do so. I believe the inference was that all of this is useless information.

I would like to read what he said at the bottom of that page, sir, and it is as follows:

"So what I am suggesting to regulators: Do not be dogmatic. Don't paint yourself into a corner. Look at all of the evidence. Make up your own mind. But do not rule out any given technology ---"

I am actually surprised our colleagues would say: "Do not look at any evidence that you may find useful." It is incomprehensible to us.

0671

With those comments, Mr. Chairman, that concludes my remarks.

I would like to extend our thanks to the Board for coming to Montreal, and our gratitude to everyone who participated; and, since we are getting close to that period -- it is probably the first time you will hear this -- our best wishes for the upcoming season.

THE CHAIRMAN: Thank you, Mr. Leclerc.  
--- (A Short Pause/Courte Pause)

Me LECLERC: Monsieur le President, avec votre permission, on m'a fait remarquer que j'ai cite incorrectement un chiffre lorsque je parlais de la position concurrentielle de la Compagnie.

Pour ce qui regarde les salaires, j'ai mentionne le chiffre de 2,2 pour cent alors que j'aurais du dire 3,2 pour cent.

Egalement, lorsque je faisais reference, a la toute fin de la partie traitant du cout de service, j'ai mentionne la piece B-27 plutot que la piece B-28.

Et enfin, je crois avoir suivi la coutume

habituelle devant l'Office d'avoir remis aux stenographes une copie de mes notes et je n'ai donc pas fait référence aux transcriptions et aux pièces justificatives lors de ma plaidoirie. Cependant, je crois comprendre que ces références apparaîtront à la transcription.

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Je vous remercie.

LE PRESIDENT: Merci, maître Leclerc.

Quelqu'un aurait-il des questions?

S'il n'y a rien d'autre, je vais terminer en vous remerciant tous à mon tour de votre participation. Ce fut quatre journées fort intéressantes.

Donc, la partie orale de cette audience est maintenant terminée et la décision de l'Office, évidemment, suivra.

Merci, et bonnes fêtes à tous!

--- L'audience est terminée/The Hearing Closed

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