MORNINGSTAR | DBRS

PRESS RELEASE APRIL 20, 2021

# DBRS Morningstar Confirms Énergir Inc. at "A" and R-1 (low) With Stable Trends

UTILITIES & INDEPENDENT POWER

DBRS Limited (DBRS Morningstar) confirmed its Issuer Rating, First Mortgage Bonds (FMB) rating and Senior Secured Notes (the Notes) rating on Énergir Inc. (Énergir or the Company) at "A." DBRS Morningstar also confirmed the Commercial Paper (CP) rating at R-1 (low). All trends are Stable. The FMB, the Notes, and the secured credit facility backstopping the CP program are guaranteed by Énergir, L.P. (the Partnership). The Company is the general partner of the Partnership and serves as its financing entity. The ratings confirmation is based on the stability of Énergir, L.P.'s regulated businesses operating in the Province of Québec (Québec; rated AA (low) with a Stable trend by DBRS Morningstar).

Énergir, L.P.'s business risk assessment was unchanged in 2020. While the ongoing Coronavirus (COVID-19) pandemic negatively affected the Partnership's volumes and throughputs for the year, earnings remained relatively stable, benefitting from revenue decoupling mechanisms in place at Énergir-QDA, the regulated natural gas distributor operating in Québec, and Green Mountain Power Corporation (GMP), the regulated electricity distributor operating in Vermont. As such, DBRS Morningstar expects Énergir, L.P.'s earnings and cash flow to be steady and increase in line with the growing rate base.

The Partnership's key credit metrics weakened in F2020, with the debt-to-capital ratio spiking to 68.6% from 66.4% in F2019. This increase was partly because of continued capital expenditures (capex) at Standard Solar Inc. (Standard Solar), a nonregulated subsidiary focused on solar generation (capex of around $250 million in F2020). Standard Solar was spun-off from Énergir in October 2020, which led to a reduction of around $235 million of debt at Énergir, L.P. and reduced capex funding needs. As such, DBRS Morningstar expects the Partnership's key credit metrics to be stable over the medium term and remain in line with the "A" rating category. A positive rating action for Énergir is unlikely given the regulatory environments and the current key credit metrics of Énergir, L.P. A negative rating action could occur if the metrics weakened to a level no longer commensurate with the "A" rating category.

A description of how DBRS Morningstar considers ESG factors within the DBRS Morningstar analytical framework can be found in the DBRS Morningstar Criteria: Approach to Environmental, Social, and Governance Risk Factors in Credit Ratings at https://www.dbrsmorningstar.com/research/373262.

Notes:
All figures are in Canadian dollars unless otherwise noted.

The principal methodologies are Rating Companies in the Regulated Electric, Natural Gas, and Water Utilities Industry (October 27, 2020, https://www.dbrsmorningstar.com/research/368939), DBRS Morningstar Criteria: Guarantees and Other Forms of Support (January 14, 2021, https://www.dbrsmorningstar.com/research/372344), and DBRS Morningstar Criteria: Commercial Paper Liquidity Support for Nonbank Issuers (March 9, 2021, https://www.dbrsmorningstar.com/research/375001), which can be found on dbrsmorningstar.com under Methodologies & Criteria. Other applicable methodologies include the DBRS Morningstar Criteria: Approach to Environmental, Social, and Governance Risk Factors in Credit Ratings (February 3, 2021, https://

www.dbrsmorningstar.com/research/373262).

For more information regarding rating methodologies and Coronavirus Disease (COVID-19), please see the following DBRS Morningstar press release: https://www.dbrsmorningstar.com/research/357883.

The related regulatory disclosures pursuant to the National Instrument 25-101 Designated Rating Organizations are hereby incorporated by reference and can be found by clicking on the link under Related Documents or by contacting us at info@dbrsmorningstar.com.

The rated entity or its related entities did participate in the rating process for this rating action. DBRS Morningstar had access to the accounts and other relevant internal documents of the rated entity or its related entities in connection with this rating action.

Generally, the conditions that lead to the assignment of a Negative or Positive trend are resolved within a 12-month period. DBRS Morningstar trends and ratings are under regular surveillance.

For more information on this credit or on this industry, visit www.dbrsmorningstar.com or contact us at info@dbrsmorningstar.com.

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## Ratings

### Énergir Inc.

| Date Issued | Debt Rated | Action | Rating | Trend | Attributes |
|---|---|---|---|---|---|
| 20-Apr-21 | Issuer Rating | Confirmed | A | Stb | CA |
| 20-Apr-21 | First Mortgage Bonds | Confirmed | A | Stb | CA |
| 20-Apr-21 | Senior Secured Notes | Confirmed | A | Stb | CA |
| 20-Apr-21 | Commercial Paper | Confirmed | R-1 (low) | Stb | CA |



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# Rating Report
# Énergir Inc.

**DBRS Morningstar**
April 30, 2020

**Contents**




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## Ratings

| Debt | Rating | Rating Action | Trend |
|---|---|---|---|
| Issuer Rating | A | Confirmed | Stable |
| Commercial Paper | R-1 (low) | Confirmed | Stable |
| First Mortgage Bonds[1] | A | Confirmed | Stable |
| Senior Secured Notes[1] | A | Confirmed | Stable |

1 Guaranteed by Énergir, L.P.

## Rating Update

On April 17, 2020, DBRS Limited (DBRS Morningstar) confirmed the Issuer Rating, the First Mortgage Bonds (FMB) rating, and the Senior Secured Notes (the Notes) rating of Énergir Inc. (Énergir or the Company) at "A". DBRS Morningstar also confirmed the Company's the Commercial Paper (CP) rating at R-1 (low). All trends remain Stable. The ratings of Énergir are based on the credit quality of Énergir, L.P. (the Partnership), which guarantees the Company's FMBs, the Notes, and a secured credit facility that supports the CP program. Énergir is the general partner of the Partnership and serves as its financing entity.

The Partnership's business risk assessment is supported by its portfolio of regulated utilities, which provides a steady stream of earnings and cash flow. Énergir-QDA, the Partnership's regulated natural gas distribution utility in the Province of Québec (Québec or the Province; rated AA (low) with a Stable trend by DBRS Morningstar), provided 69.6% of EBITDA in F2019. In November 2019, the Régie de l'énergie (the Régie) issued its decision on Phase 2 of Énergir-QDA's F2020 rate case, which included transitioning from cost-of-service (COS) to a three-year ratemaking framework with an indexation formula for operating expenses for F2021 and F2022. The Régie also approved a revenue decoupling mechanism with variances between approved and actual revenues to be recovered or returned to customers. DBRS Morningstar notes that though Énergir-QDA will face greater cost pressure going forward as it will have to maintain operating costs within inflation, this is offset by the increased stability in revenues with the decoupling mechanism reducing volume risk.

The Partnership's financial risk assessment remained reasonable for the last 12 months ended December 31, 2019 (LTM 2020). Although earnings for LTM 2020 weakened, key credit metrics remained supportive of the current rating category. DBRS Morningstar expects earnings for F2020 to remain relatively stable, although the current Coronavirus Disease (COVID-19) pandemic may have a modestly negative impact on F2020. While earnings for Énergir-QDA should remain in line with expectations because of (1) the revenue decoupling mechanism, (2) long-term contracts with industrial customers, and (3) the majority of revenues for F2020 have already been collected in Q1 and Q2, earnings from the Vermont utilities will likely be modestly weaker because of lower demand. DBRS Morningstar expects the Partnership to continue to fund free cash flow deficits from the large capital expenditures program (capex) to expand and renew the network in Québec, and investments by its subsidiaries in renewable projects, through a prudent mix of debt and equity in order to maintain metrics in line with the current ratings. Additionally, while investments in non-regulated activities have increased over the past few years, the Partnership's trust deed restricts interest in nonregulated energy-related activities and non-energy-related activities to 10% of total nonconsolidated assets (8.12% in F2019, up from 4.78% in F2018) and thus it will remain a modest segment. DBRS Morningstar considers a positive rating action for Énergir to be unlikely, given the regulatory environments and the current key credit metrics of the Partnership. A negative rating action could occur if the metrics weakened to a level no longer commensurate with the "A" rating category.

## Financial Information

| Énergir, L.P. | 12 mos. to Dec. 31 | For the year ended September 30 | | | | |
|---|---|---|---|---|---|---|
| | **2019** | **2019** | **2018** | **2017** | **2016** | **2015** |
| Cash flow/Total debt (%)[1] | 14.1 | 15.1 | 17.8 | 16.0 | 16.8 | 16.9 |
| Total debt in capital structure (%)[1, 2] | 66.8 | 66.4 | 65.3 | 64.7 | 66.5 | 65.1 |
| EBIT gross interest coverage (times)[1, 3] | 2.14 | 2.16 | 2.53 | 2.32 | 2.44 | 2.61 |

1 Adjusted for operating leases.
2 Adjusted for accumulated other comprehensive income.
3 Includes distributions received from companies subject to significant influence.

## Issuer Description

Énergir Inc. is a holding company with majority ownership of Énergir, L.P., which owns and operates natural gas distribution in Québec and natural gas and electricity distribution in Vermont as well as having financial interests in transmission, storage, gas, and other underground systems enterprises. Énergir, L.P. is 71% owned by Énergir Inc.

## Rating Considerations

### Strengths

*1. Supportive regulation in Québec*

The regulatory framework in Québec is viewed as supportive, reflecting the following factors: (A) full recovery of gas supply costs through an automatic monthly adjustment mechanism, (B) rate stabilization accounts to mitigate revenue fluctuations due to the weather, (C) reasonable authorized ROE and capital structure ratio, and (D) a revenue decoupling mechanism.

*2. Reasonable financial profile*

The Partnership's consolidated financial profile has remained reasonable for the current ratings, including cash flow-to-debt ratio of 14.1% and an EBIT-interest coverage ratio of 2.14 times (x) for LTM F2020. Although the consolidated debt-to-capital ratio of 66.8% was relatively weak for the current ratings, the non-consolidated ratios remained consistent with the "A" rating category (cash flow-to-debt ratio of 16.3%, debt-to-capital ratio of 55.3% and EBIT interest coverage ratio of 1.73x).

*3. Cash flow diversification*

The Partnership benefits from a large base of regulated utility assets, including: (A) gas distribution in Québec; (B) U.S. natural gas and electricity distribution in Vermont through Green Mountain Power Corporation (GMP) and Vermont Gas Systems, Inc. (VGS); (C) U.S. electricity transmission in Vermont through majority ownership in Vermont Electric Power Company, Inc. and Vermont Transco LLC (Transco); (D) financial interest in three natural gas transportation enterprises, namely Trans Québec & Maritimes Pipeline Inc. (TQM; rated A (low) with a Stable trend by DBRS Morningstar), Portland Natural Gas Transmission System (PNGTS), and Champion Pipe Line Corporation Limited (Champion); and (E) financial interests in wind power projects.

**Challenges**

*1. Higher risks associated with volume and energy cost in Vermont electricity distribution*

There is a higher level of volume risk associated with regulated operations in Vermont than in Québec as there is no rate stabilization mechanism for the Partnership's electricity distribution subsidiaries in Vermont to mitigate against volume delivery fluctuations due to the weather.

*2. Industrial customers are sensitive to economic conditions*

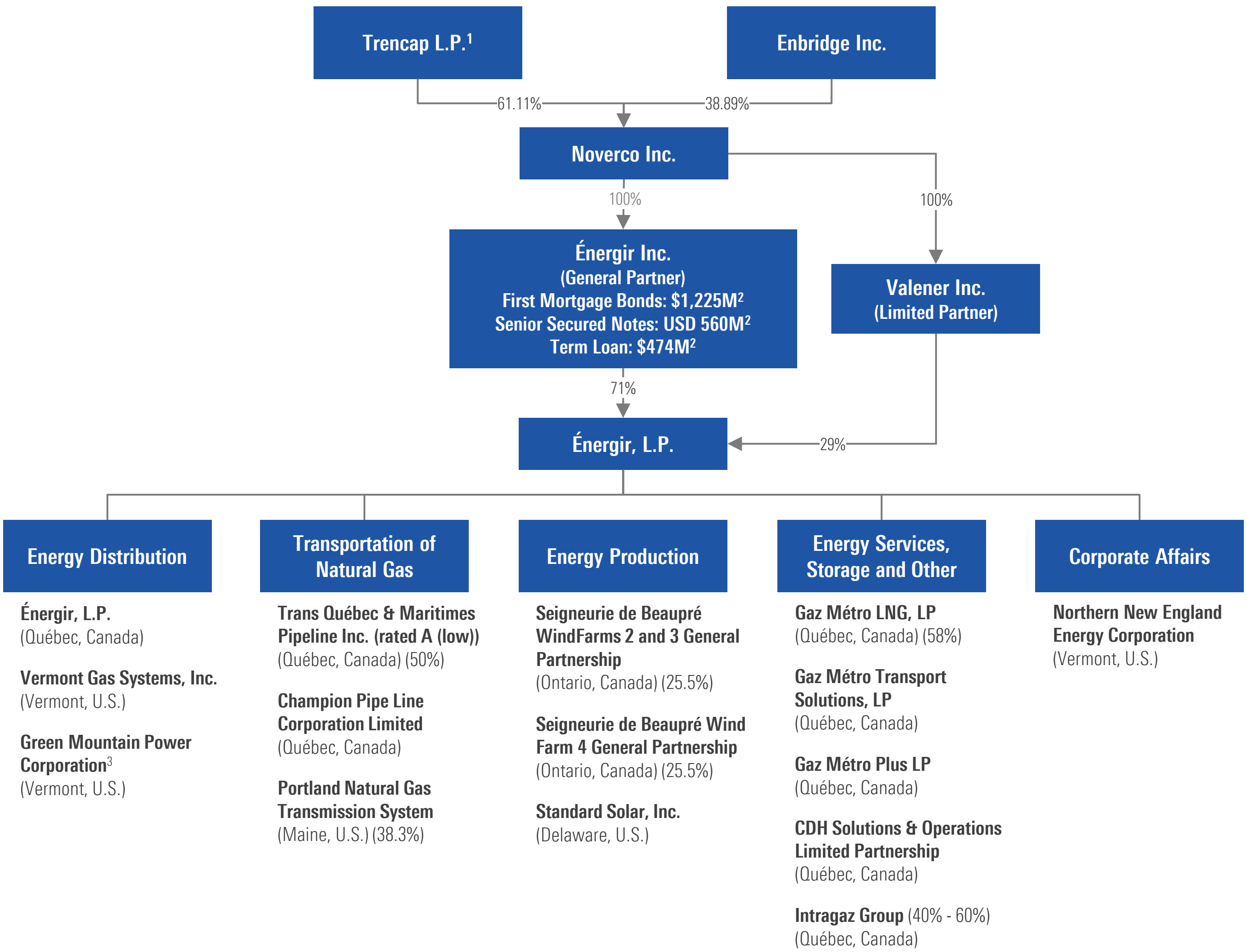
In Québec, approximately 60% of natural gas distribution is consumed by industrial customers, whose consumption is highly sensitive to economic conditions. A significant reduction in demand from these customers could affect the Partnership's distribution revenues; however, this risk is mitigated by firm service contracts of more than one year with many of these customers providing guaranteed payment of a significant portion of distribution services, regardless of their levels of consumption. Firm service contracts account for more than 80% of all industrial volume consumption, which provides the Partnership with sufficient time to reallocate its revenue requirement among customer classes if necessary. Additionally, with the introduction of a revenue decoupling mechanism for F2020, revenues should be even more stable going forward as volume risk will be significantly reduced.

*3. Risk associated with inaccurate cost projection*

A shortfall between earned net income and allowed net income may arise if the actual cost for the Partnership to provide its regulated services is higher than the projected cost. If the difference between actual and projected costs is significant, there could be a material negative impact on the Partnership's credit metrics; however, given the long operating history of this utility, DBRS Morningstar believes that the probability of a materially inaccurate cost projection is low.

## Organizational Chart

### Simplified Organizational Chart




1 The general partner of Trencap is Caisse de dépôt et placement du Québec, which, as a limited partner of Trencap, holds 64.74% of its units. The other limited partners are Fonds de solidarité des travailleurs du Québec (F.T.Q.) (19.10%), British Columbia Investment Management Corporation (14.66%), and the Régime de retraite de l'Université du Québec (1.50%).
2 FMBs, Senior Secured Notes, and the term loan at Énergir Inc. are guaranteed by Énergir, L.P. Balances are as at December 31, 2019.
3 Significant ownership interest in Vermont Transco LLC (direct and indirect totaling 75.7%) and Vermont Electric Power Company, Inc. (38.8% direct).
Source: Énergir Inc. 2019 Annual Information Form.

- Énergir Inc. is the financing vehicle for Énergir, L.P., with funds raised by the Company loaned to the Partnership on similar terms and conditions.
  - Given the mirror-like structure of the financing, the only substantive difference between the two entities is the $892.8 million of subordinated debt at Énergir (intercompany debt from Noverco, Inc., not shown in the above chart).

  - Failure to pay interest or principal on the subordinated debt would not cause either acceleration of that debt or a cross default to senior debt. Consequently, the subordinated debt is treated as equity by DBRS Morningstar.
- The trust deeds stipulate that all of the Partnership's interest in nonregulated energy-related activities and non-energy-related activities must not be more than 10% of its total nonconsolidated assets (8.12% as at September 30, 2019). As for non-energy-related activities, the Partnership's interest in such activities may not exceed 5% of its total nonconsolidated assets (none as at September 30, 2019).

**Consolidated Earnings and Outlook**

| **Énergir, L.P.** | 12 mos. to Dec. 31 | For the year ended September 30 | | | | |
|---|---|---|---|---|---|---|
| (CAD millions where applicable) | **2019** | **2019** | **2018** | **2017** | **2016** | **2015** |
| Net revenues | 1,134 | 1,134 | 1,119 | 1,094 | 1,075 | 1004 |
| EBITDA[1] | 575 | 584 | 623 | 583 | 598 | 540 |
| EBIT[2] | 215 | 224 | 274 | 259 | 273 | 261 |
| Gross interest expense | 166 | 167 | 159 | 156 | 158 | 147 |
| Net operating earnings after tax[2] | 11 | 36 | 96 | 78 | 103 | 80 |
| Equity earnings | 152 | 151 | 137 | 129 | 124 | 119 |
| Net income before non-recurring items | 201 | 211 | 235 | 228 | 225 | 194 |
| Reported net income | 230 | 256 | 216 | 241 | 278 | 181 |
| Return on equity | 9.9% | 10.7% | 12.1% | 12.4% | 13.0% | 12.1% |
| | | | | | | |
| **Segmented Reported EBITDA**[2] | | | | | | |
| Énergir - QDA | n/a | 335 | 315 | 329 | 316 | 305 |
| VGS and GMP | n/a | 146 | 195 | 164 | 193 | 169 |
| Natural Gas Transportation | n/a | 2 | 2 | 2 | 2 | 2 |
| Energy Production | n/a | (15) | (10) | (4) | (1) | (1) |
| Energy Services, Storage and Other | n/a | 13 | 18 | 12 | 6 | 6 |
| **Subtotal** | **n/a** | **481** | **520** | **503** | **515** | **480** |
| Corporate and Other | n/a | (15) | (11) | (15) | (11) | (8) |
| **Total EBITDA** | **n/a** | **467** | **508** | **487** | **505** | **472** |
| | | | | | | |
| Regulated rate base[3] | 2,196 | 2,157 | 2,118 | 2,044 | 1,956 | 1,940 |
| Deemed common equity[3] | 38.5% | 38.5% | 38.5% | 38.5% | 38.5% | 38.5% |
| Allowed ROE[3] | 8.90% | 8.90% | 8.90% | 8.90% | 8.90% | 8.90% |

1 Adjusted for operating leases.
2 Excludes earnings from equity investments.
3 For Énergir-QDA only.

### F2019 Summary

- The vast majority of the Partnership's EBITDA and earnings are generated by low-risk regulated utilities and pipelines supported by long-term contracts.
- EBITDA and EBIT decreased in F2019 largely because of the U.S. tax reform that reduced collections from customers.

- Net income before nonrecurring items also decreased because of higher interest expense from the increased debt load.
    - The difference between reported net income includes USD 30 million of reimbursement to the customers of VGS and GMP from the U.S. tax reform.

**F2020 Summary and Outlook**

- Earnings for LTM 2020 decreased modestly because of (1) lower overearnings compared to the same period in F2019 for Énergir-QDA, (2) lower allowed ROE and equity for GMP, and (3) lower liquified natural gas deliveries.
- DBRS Morningstar had expected earnings for F2020 to be relatively stable, reflecting the regulated nature of most of the Partnership's operations.
    - Earnings for Énergir-QDA are expected to be even more steady going forward following the approval of a revenue decoupling mechanism, with any overearnings or shortfalls in revenues to be returned or collected from customers and reducing volatility from weather.
    - Earnings for GMP should benefit from a higher rate base but these will be partly offset by a lower allowed ROE and deemed equity.
- DBRS Morningstar notes the current coronavirus pandemic may lead to a modest decrease in earnings for the Partnership.
    - Earnings for Énergir-QDA should remain largely in line with expectations because the revenue decoupling mechanism will be in place, there are long-term contracts with industrial customers, and the majority of revenues were collected in Q1 and Q2 of the fiscal year.
    - Earnings from GMP and VGS will likely be modestly lower because of expected lower demand.

**Consolidated Financial Profile**

| **Énergir, L.P.** | 12 mos. to Dec. 31 | For the year ended September 30 | | | | |
|---|---|---|---|---|---|---|
| (CAD millions where applicable) | **2019** | **2019** | **2018** | **2017** | **2016** | **2015** |
| Net income before nonrecurring items | 201 | 211 | 235 | 228 | 225 | 194 |
| Depreciation & amortization | 380 | 380 | 373 | 327 | 327 | 284 |
| Distributions received | 139 | 135 | 126 | 102 | 112 | 122 |
| Equity earnings | (152) | (151) | (137) | (129) | (124) | (119) |
| Deferred income taxes and other | 9 | 20 | 56 | 39 | 50 | 53 |
| **Cash flow from operations** | **577** | **596** | **653** | **567** | **590** | **534** |
| Distributions to partners | (216) | (216) | (216) | (204) | (197) | (187) |
| Capital expenditures | (710) | (618) | (459) | (573) | (691) | (742) |
| **Gross free cash flow** | **(348)** | **(238)** | **(22)** | **(210)** | **(298)** | **(394)** |
| Change in working capital | 10 | (1) | (20) | 13 | 18 | 29 |
| Change in regulatory assets | 79 | 82 | (9) | (20) | (79) | (39) |
| **Net free cash flow** | **(259)** | **(157)** | **(51)** | **(217)** | **(359)** | **(405)** |
| Acquisitions & long-term investments | (22) | (39) | (85) | (8) | (56) | (41) |
| Net change in equity | 50 | 38 | 15 | 140 | 15 | 282 |
| Net change in debt | 249 | 231 | 61 | 135 | 382 | 139 |
| Other investing and financing | (14) | (10) | 5 | (1) | (1) | 12 |

| | | | | | | |
|---|---|---|---|---|---|---|
| **Change in cash** | **3** | **63** | **(55)** | **49** | **(19)** | **(14)** |
| | | | | | | |
| Total debt | 4,093 | 3,948 | 3,659 | 3,526 | 3,497 | 3,147 |
| Cash flow/Total debt (%)[1] | 14.1 | 15.1 | 17.8 | 16.0 | 16.8 | 16.9 |
| Total debt in capital structure (%)[1, 2] | 66.8 | 66.4 | 65.3 | 64.7 | 66.5 | 65.1 |
| EBIT gross interest coverage (times)[1, 3] | 2.14 | 2.16 | 2.53 | 2.32 | 2.44 | 2.61 |
| Dividend payout ratio (%) | 107.6 | 102.3 | 92.2 | 89.4 | 87.7 | 95.9 |
| | | | | | | |
| **Non-consolidated metrics** | | | | | | |
| Cash flow/Total debt (%)[1] | 16.3 | 18.1 | 18.7 | 17.7 | 16.6 | 17.1 |
| Total debt in capital structure (%)[1, 2] | 55.3 | 54.7 | 55.1 | 54.9 | 56.7 | 55.1 |
| EBIT gross interest coverage (times)[1, 3] | 1.73 | 1.80 | 2.07 | 2.31 | 2.11 | 2.37 |

1 Adjusted for operating leases.
2 Adjusted for accumulated other comprehensive income.
3 Includes distributions received from companies subject to significant influence.

### F2019 Summary

- Key credit metrics for the Partnership weakened modestly in F2019 because of the lower earnings and cash flow along with a higher debt load. However, the metrics remain supportive of the "A" rating.
    - The Partnership's nonconsolidated debt-to-capital ratio of 54.7% was in line with the regulatory capital structure of 46% equity (including 7.50% of preferred shares).
- Cash flow from operations decreased, tracking the lower earnings for the year.
- Capex increased significantly because of investments made by Standard Solar Inc. (Standard Solar) and GMP in solar power projects.
- The Partnership distributed over 90% of net income to its limited partners. Under the Partnership Agreement, Énergir, L.P. will not distribute any less than 85% of its net income before nonrecurring items to its partners, except under extraordinary circumstances.
- The Partnership funded its net free cash flow deficit mainly through debt issuances.

### F2020 Summary and Outlook

- Although key credit metrics for the Partnership weakened in LTM 2020, tracking the lower earnings and cash flow for the period, they continue to be in line with the current ratings.
- The Partnership has forecast capex of around $700 million for F2020 ($197 million spent in Q1 2020), with the increase largely for Énergir-QDA to extend the existing network and for replacement of equipment at the liquefaction, storage, and regasification plant.
- DBRS Morningstar expects the Partnership's key credit metrics to remain relatively stable in F2020.

## Liquidity

**Credit Facility (non-consolidated)**

| (CAD millions) - As at December 31, 2019 | Maturity | Committed | Draw/CP Backstop | Letters of Credit | Available |
|---|---|---|---|---|---|
| Secured Term Loan | March 2024 | 800.0 | 473.1 | 28.1 | **298.8** |

- Énergir has a $800 million secured term loan facility maturing in March 2024 that supports the Company's CP program.
  - Énergir has an investment policy in place such that CP maturities will not exceed an aggregate amount of $35 million for two consecutive business days to ensure that the $50 million swingline facility, which is available under its credit facility, maintains adequate liquidity to backstop the CP program.
  - The debt issued under the term loan facility is guaranteed by the Partnership.

### Long-Term Debt

- The following is a table of the Partnership's debt maturities on a consolidated basis:

**Consolidated Debt Maturities**

| As at December 31, 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | Thereafter | Total |
|---|---|---|---|---|---|---|---|
| Énergir | 100 | 150 | 169 | 0 | 473 | 1,534 | **2,426** |
| NNEEC | 0 | 0 | 65 | 0 | 0 | 65 | **130** |
| VGS | 1 | 1 | 1 | 1 | 1 | 149 | **154** |
| GMP | 13 | 41 | 164 | 1 | 23 | 936 | **1,178** |
| Other | 1 | 1 | 1 | 2 | 12 | 90 | **109** |
| **Subtotal** | **115** | **193** | **400** | **4** | **509** | **2,774** | **3,995** |
| Financial costs | | | | | | | (16) |
| **Total** | | | | | | | **3,979** |

- The debt maturity schedule is reasonably spread out with minimal refinancing risk over the next five years.

### Covenants and Restrictions

- The Partnership's long-term trust deeds and other agreements contain covenants that restrict its issuance of any long-term debt if such issuance would result in its long-term debt-to-total capitalization ratio exceeding 65% and its long-term debt interest coverage ratio being less than 1.5x (both on a non-consolidated basis).
- If the Partnership's long-term debt-to-capitalization ratio exceeds 75% (on a non-consolidated basis), it will not make a distribution to its partners.
- As of September 30, 2019, the Partnership's non-consolidated long-term debt-to-total capitalization ratio and the non-consolidated long-term debt interest ratio were 52.9% and 3.71x, respectively.
- The Partnership's interests in nonregulated energy-related activities and non-energy-related activities must not be more than 10% of its total nonconsolidated assets (8.12% at September 30, 2019), and its interest in such activities may not exceed 5% of its total nonconsolidated assets. As at December 31, 2019, the Partnership had no interest in such activities.

**Description of Operations**

The Partnership's main business segments are described below.

**1. Energy Distribution (84.8% of reported adjusted F2019 net income, excluding Corporate Affairs)**

- The Partnership's regulated natural gas distribution utility in Québec, Énergir-QDA (46.3% of reported adjusted F2019 net income, excluding Corporate Affairs), delivers 97% of the province's natural gas consumed and serves more than 207,000 customers.
- GMP is the largest electricity distributor in Vermont, serving more than 265,000 customers. GMP generates, transports, distributes, purchases and sells electricity as well as providing electric network construction services in Vermont. GMP also transports electricity in New Hampshire and generates relatively small amounts of electricity in New York, Maine, and Connecticut.
- VGS is the sole gas distributor in Vermont, serving more than 50,000 customers and provides other energy-related services, including increased energy efficiency by renovating natural gas equipment.

**2. Natural Gas Transportation (14.5% of reported adjusted F2019 net income, excluding Corporate Affairs)**

- TQM (50% owned) operates a gas pipeline in Québec that connects upstream with TransCanada PipeLines Limited (TCPL; rated A (low) with a Stable trend by DBRS Morningstar) and downstream with PNGTS and the Énergir-QDA system.
- Champion operates two gas pipelines that cross the Ontario-Québec border to supply the Partnership's distribution system in Northwestern Québec.
- PNGTS's pipeline (38% owned) originates at the Québec border and extends to the suburbs of Boston.

**3. Electricity Production (-1.7% of reported adjusted F2019 net income, excluding Corporate Affairs)**

- This segment consists of non-regulated energy production activities related to Wind Farms 2, 3, and 4 as well as Standard Solar activities.
- Wind Farms 2 and 3 are an equal-share joint venture (JV) of Boralex Inc. and Beaupré Éole General Partnership. Beaupré Éole General Partnership is 51% owned by the Partnership and the remaining 49% is owned by Valener. As a result, the Partnership owns 25.5% of the equity interest in Wind Farms 2 and 3. The JV's core business includes owning and operating wind farms with an installed capacity of 272 megawatts (MW). All electricity generated is sold to Hydro-Québec (rated A (high)/R-1 (middle) with Stable trends by DBRS Morningstar) under an agreement that expires in 2033.
- Wind Farm 4 is an equal-share JV of Boralex and Beaupré Éole 4. Beaupré Éole 4 is 51% owned by Énergir, L.P. and the remaining 49% is owned by Valener. As a result, Énergir, L.P. owns 25.5% of the equity interest. Wind Farm 4 owns and operates a wind farm with an installed capacity of 68 MW. All electricity generated is sold to Hydro-Québec under an agreement that expires in 2034.
- The Partnership acquired Standard Solar in April 2017. Standard Solar develops and owns solar power systems, the power from which is sold to customers under long-term power-purchase agreements. It also provides contractor and operating services.

**4. Energy Services, Storage and Other (2.4% of reported adjusted F2019 net income, excluding Corporate Affairs)**

- Through subsidiaries, the Partnership (A) sells natural gas as fuel for transportation; (B) develops liquefied natural gas marketing and production activities to market compressed natural gas; (C) offers natural-gas-powered appliance sales, leases, and maintenance services; and (D) operates the Montréal Thermal Plant that supplies heat and air conditioning to the downtown area. The activities related to energy services are not regulated.
- The Partnership owns an indirect interest in Intragaz Ltd., whose main activity is underground natural gas storage and is regulated on a COS basis by the Régie.

## Regulation

**1. Énergir-QDA – Regulated by the Régie**

- DBRS Morningstar considers the regulatory framework in Québec as supportive:
  - Natural gas supply costs are fully passed on to customers through an automatic monthly adjustment mechanism;
  - All transportation costs charged by TCPL are included in the costs of Énergir-QDA and are reflected in its transportation rates;
  - Énergir-QDA is allowed to recover the cost of providing its service and to earn a reasonable rate of return on its rate base; and
  - Énergir-QDA has been subject to the Cap and Trade System regulation effective January 1, 2015. The compliance cost is fully passed onto ratepayers.

- The following table summarizes the key regulatory parameters for Énergir-QDA:

| Énergir-QDA | F2020 | F2019 | F2018 | F2017 |
|---|---|---|---|---|
| Average rate base (CAD millions) | 2,196 | 2,157 | 2,118 | 2,044 |
| Deemed equity (including 7.5% of preferred shares) (%) | 46 | 46 | 46 | 46 |
| Authorized ROE (on common equity) (%) | 8.90 | 8.90 | 8.90 | 8.90 |

- In March 2019, the Régie approved Phase I of Énergir-QDA's F2020 rate case.
  - Énergir-QDA had submitted a proposal that would ease the regulatory process by introducing multi-year treatments of certain rate-setting parameters.
  - The Régie approved operating expenses for F2020 to F2022 to be subject to an indexation formula comprising a price index (75% provincial hourly wages and earnings index, 25% provincial consumer price index) and customer growth, adjusted by a discount factor of 0.75.
  - The Régie also renewed the authorized ROE of 8.9% for F2020.
- In November 2019, the Régie issued its decisions on Phase 2 of the F2020 rate case.
  - The Régie renewed the authorized ROE of 8.9% for F2020 to F2022 and rate base of $2,195.8 million for F2020 for a total revenue requirement of $790.9 million.
  - The decision led to a 14.6% decrease in rates for customers through (1) reimbursement of balances in regulatory deferral accounts, (2) return of overearnings from previous years, and (3) lower TCPL rates.

- The Régie also approved a revenue decoupling mechanism, with all variances between approved and actual revenues to be returned or collected from customers. DBRS Morningstar expects the revenue decoupling mechanism to provide more stable revenues for Énergir-QDA, reducing volume risk.
- The earnings sharing mechanism was also updated, with over- and under-earnings shared 75% to Énergir-QDA and 25% to customers for the first 50 basis points (bps), and 50%:50% beyond the first 50 bps.

**2. Vermont Distribution Utilities – Regulated by Vermont Public Utilities Commission (VPUC)**

- GMP and VGS are regulated by the VPUC.
  - Electricity prices for GMP are adjusted annually using a rate-adjustment mechanism.
  - Natural gas prices for VGS are adjusted quarterly using a rate-adjustment mechanism.
- The following table summarizes the key regulatory parameters for the two Vermont utility subsidiaries:

| | F2020 | | | F2019 | | | F2018 | | |
|---|---|---|---|---|---|---|---|---|---|
| | **Deemed equity (%)** | **Authorized ROE (%)** | **Average rate base (USD)** | **Deemed equity (%)** | **Authorized ROE (%)** | **Average rate base (USD)** | **Deemed equity (%)** | **Authorized ROE (%)** | **Average rate base (USD)** |
| **GMP** | 49.5 | 9.06 | 1,622 million | 49.9 | 9.30 | 1,558 million | 48.6 | 9.10 | 1,433 million |
| **VGS** | 50 | 9.20 | 265 million | 50 | 8.50 | 255 million | 50 | 8.50 | 248 million |

*GMP*

- Effective October 1, 2012, Green Mountain and Central Vermont Public Service Corporation merged to form GMP.
  - As part of the merger agreement, GMP agreed to the following savings-sharing plan during the first ten years following the close of the merger: (1) flow through to ratepayers via rates credits of USD 2.5 million, USD 5.0 million, and USD 8.0 million in 2013, 2014, and 2015, respectively; (2) 50% of total savings from 2016 to 2020 (USD 15.6 million in 2016, USD 16.9 million in 2017, and estimated USD 18.2 million in 2018, USD 14 million in 2019, and USD 14.5 million in 2020); and (3) all savings in 2021 and 2022.
  - GMP is required to file a savings guarantee plan with the VPUC by December 31, 2022, to compensate ratepayers if the total merger saving is less than USD 144 million during the ten-year period. GMP expects to realize sufficient synergies to reach the USD 144 million objective.
- In April 2018, GMP filed its COS proposal for January 1, 2019, to September 30, 2019, to align GMP's rate period with its fiscal year.
  - In December 2018, the VPUC approved an overall rate increase of 5.43% based on an authorized ROE of 9.30% and deemed equity of 49.85% for the period; however, the rate increase will be more than fully offset by the impact of reimbursements to customers of the regulatory liabilities related to the December 2017 U.S. Tax Reform legislation, thereby resulting in an overall decrease of 0.90%.
- In June 2018, GMP filed a proposal to adopt a new multi-year regulation plan.

    - In May 2019, the VPUC approved a three-year regulation plan for GMP for F2020 to F2022, effective October 1, 2019.
    - Under the three-year plan, base rates are based on a three-year forecast of all costs with increases to be smoothed based on the average rate for each fiscal year.
    - Rates will be adjusted annually for power supply costs and revenue forecasts and their corresponding impact on taxes.
    - The allowed ROE will be adjusted annually based on 50% of the change in the 10-year US Treasury bond yield.
    - For F2020, rates will increase by 2.72% based on ROE of 9.06% and deemed equity of 49.5%.

*VGS*

- VGS is subject to an Alternative Regulation Plan for F2019, which includes a natural gas cost quarterly adjustment mechanism.
- In October 2018, the VPUC approved VGS's application for rates effective November 1, 2018.
    - Distribution rates increased by 3.9% based on an average rate base of USD 255.5 million based on an allowed ROE of 8.50% and deemed equity of 50%.
- In October 2019, the VPUC approved VGS's application for rates effective November 1, 2019.
    - Distribution rates increased by 5.0% based on an average rate base of USD 264.7 million, allowed ROE of 9.20%, and deemed equity of 50%.

**3. Vermont Electricity Transmission – Regulated by the Federal Energy Regulatory Commission (FERC)**

- Transco, which is 75.7% indirectly owned by the Partnership, owns transmission assets in Vermont.
- Transco operates under a COS framework regulated by the FERC that allows it to recover all prudently incurred operating costs. Transco is not exposed to any volume or commodity risk.
    - Complaints filed to the FERC about the New England Transmission Owner's allowed ROE led to a reduction in the base ROE.
    - Although the lower ROE will reduce the revenues collected by Transco through the ISO New England Inc. Transmission, Markets, and Services Tariff, the shortfall will be collected through the 1991 Vermont Transmission Agreement with regional electricity distribution companies in Vermont and will not have a negative impact on Transco's earnings and cash flows.
    - Even though this will place more rate pressure on the Vermont distribution utilities and their customers as they will have to contribute a larger portion of the 11.8% weighted-average return allowed for Transco's membership units, DBRS Morningstar does not anticipate changes to the 1991 Agreement.
    - DBRS Morningstar notes that the FERC issued an Order Directing Briefs in October 2018, proposing a methodology to determine the just and reasonable ROE and range. Based on the FERC's preliminary analysis, it has calculated a just and reasonable ROE range of 9.60% to 10.99% with a just and reasonable ROE of 10.41% and a cap of 13.08%.

**4. Pipelines – Regulated by the National Energy Board (NEB) in Canada and by the FERC**

*TQM – Regulated by the NEB*

- In April 2017, TQM (50% owned) reached a multi-year settlement agreement with its interested parties, establishing the mechanisms for determining TQM's annual revenue requirements for 2017–2021.
    - Under this agreement, annual rates are calculated using a formula that includes a fixed-cost component and a component that is fully recoverable from or payable to customers (refer to the TQM report dated December 10, 2019, for more details).

*Champion – Regulated by the NEB*

- Champion (100% owned) operates two natural gas pipelines that cross the Ontario border and supply Énergir's distribution system in northwestern Québec.
- Its activities are regulated by the NEB with tolls based on an annual COS methodology.
    - Champion uses a ROE and capital structure equivalent to those approved by the Régie for Énergir-QDA (the deemed equity component was set at 46% and the authorized ROE was set at 8.90% for F2020).

*PNGTS – Regulated by the FERC*

- PNGTS (38.3% owned) originates at the Québec border and extends to the suburbs in Boston.
- PNGTS is regulated by the FERC on a COS basis.
- To meet growing demand for natural gas in New England, PNGTS will need to raise its network capacity by adding, among other things, a compressor to the Elliot station, for which work is expected to begin in winter 2020. Projected investments will amount to $50 million for TQM and $85 million for PNGTS.

**Assessment of Regulatory Framework**

| Criteria | Score | Analysis |
|---|---|---|
| **1. Deemed Equity** | Excellent<br>**Good**<br>Satisfactory<br>Below Average<br>Poor | Énergir-QDA has a deemed equity thickness of 46% (38.5% in common equity, 7.5% in preferred stock), for F2020 to F2022, unchanged since F2013. |
| **2. Allowed ROE** | Excellent<br>Good<br>**Satisfactory**<br>Below Average<br>Poor | The Régie set the ROE at 8.90% for F2020 to F2022, unchanged since F2013. |
| **3. Energy Cost Recovery** | **Excellent**<br>Good<br>Satisfactory<br>Below Average<br>Poor | There is no natural gas price risk for Énergir-QDA as purchase costs are passed on to ratepayers at rates set by the Régie. Énergir-QDA collects the payments from its customers on a monthly basis. |
| **4. Capital and Operating Cost Recovery** | **Excellent**<br>Good<br>Satisfactory<br>Below Average<br>Poor | Major capital and operating costs are pre-approved by the Régie and recovered through distribution rates. Interim base rate increases have been frequently authorized. Future test periods are fully incorporated for rate-case decisions. Effective F2020, there is a revenue decoupling mechanism which would further reduce volatility in revenues, such as weather, reducing volume risk. DBRS Morningstar considers the inflation factor to be reasonable. |
| **5. COS versus IRM** | Excellent<br>**Good**<br>Satisfactory<br>Below Average<br>Poor | Effective F2020, the Régie approved a three-year regulatory framework. DBRS Morningstar does not expect the change from a COS framework to have a material impact on the financial performance of the Partnership. |
| **6. Political Interference** | Excellent<br>**Good**<br>Satisfactory<br>Below Average<br>Poor | There has been no adverse legislation in the regulated natural gas utility sector in Québec. |
| **7. Stranded Cost Recovery** | Excellent<br>**Good**<br>Satisfactory<br>Below Average<br>Poor | Énergir-QDA has a limited history of stranded costs. |
| **8. Rate Freeze** | **Excellent**<br>Good<br>Satisfactory<br>Below Average<br>Poor | Rates have never been frozen and are not expected to be frozen in the foreseeable future. |

## Balance Sheet - Énergir, L.P.

| (CAD millions) | Dec. 31 | Sep. 30 | Sep. 30 | | Dec. 31 | Sep. 30 | Sep. 30 |
|---|---|---|---|---|---|---|---|
| **Assets** | **2019** | **2019** | **2018** | **Liabilities & Equity** | **2019** | **2019** | **2018** |
| Cash & equivalents | 59 | 96 | 52 | S.T. borrowings | 98 | 114 | 43 |
| Accounts receivable | 372 | 222 | 230 | Current portion L.T.D. | 161 | 117 | 213 |
| Inventories | 1 | 91 | 81 | Accounts payable | 339 | 352 | 317 |
| Other current assets | 289 | 227 | 237 | Other current liabilities | 225 | 213 | 197 |
| **Total current assets** | **721** | **636** | **600** | **Total current liabilities** | **823** | **797** | **770** |
| Net fixed assets | 5,078 | 5,000 | 4,524 | Long-term debt | 3,834 | 3,716 | 3,403 |
| Goodwill & intangibles | 636 | 670 | 765 | Regulatory liabilities | 687 | 684 | 661 |
| Regulatory assets | 591 | 600 | 402 | Other L.T. liabilities | 1,166 | 1,174 | 905 |
| Investments & others | 1,563 | 1,531 | 1,448 | Minority interest | 63 | 73 | 65 |
| | | | | Shareholders' equity | 2,016 | 1,992 | 1,935 |
| **Total assets** | **8,589** | **8,437** | **7,740** | **Total liabilities & SE** | **8,589** | **8,437** | **7,740** |

## Ratios - Énergir, L.P.

| | 12 mos. to Dec. 31 | For the year ended September 30 | | | | |
|---|---|---|---|---|---|---|
| **Balance Sheet & Liquidity & Capital Ratios** | **2019** | **2019** | **2018** | **2017** | **2016** | **2015** |
| Current ratio | 0.88 | 0.80 | 0.78 | 1.09 | 1.01 | 1.05 |
| Total debt in capital structure (%) | 66.3 | 65.6 | 64.7 | 64.4 | 65.9 | 64.5 |
| Total debt in capital structure (%)[1, 2] | 66.8 | 66.4 | 65.3 | 64.7 | 66.5 | 65.1 |
| Cash flow/Total debt(%) | 14.1 | 15.1 | 17.9 | 16.1 | 16.9 | 17.0 |
| Cash flow/Total debt (%)[1] | 14.1 | 15.1 | 17.8 | 16.0 | 16.8 | 16.9 |
| (Cash flow - dividends)/Capex | 0.51 | 0.61 | 0.95 | 0.63 | 0.57 | 0.47 |
| Dividend payout ratio (%) | 107.6 | 102.3 | 92.2 | 89.4 | 87.7 | 95.9 |
| **Coverage Ratios (times)** | | | | | | |
| EBIT gross interest coverage | 1.30 | 1.34 | 1.73 | 1.66 | 1.73 | 1.78 |
| EBIT gross interest coverage[1, 3] | 2.14 | 2.16 | 2.53 | 2.32 | 2.44 | 2.61 |
| EBITDA gross interest coverage | 3.46 | 3.50 | 3.93 | 3.74 | 3.79 | 3.68 |
| Fixed-charge coverage | 1.30 | 1.34 | 1.73 | 1.66 | 1.73 | 1.78 |
| Debt/EBITDA | 7.12 | 6.76 | 5.87 | 6.05 | 5.84 | 5.83 |
| **Profitability Ratios** | | | | | | |
| Return on equity (%) | 9.9 | 10.7 | 12.1 | 12.4 | 13.0 | 20.9 |
| Return on capital (%)[2] | 5.3 | 5.6 | 6.1 | 6.0 | 6.3 | 10.1 |
| EBITDA margin (%) | 21.5 | 21.5 | 24.6 | 23.1 | 23.1 | 7.5 |
| EBIT margin (%) | 8.0 | 8.2 | 10.8 | 10.3 | 10.6 | 12.1 |
| Profit margin (%) | 7.5 | 7.8 | 9.3 | 9.0 | 8.7 | 6.1 |

1 Adjusted for operating leases.
2 Adjusted for accumulated other comprehensive income.
3 Includes distributions received from companies subject to significant influence.

## Rating History

| | Current | 2019 | 2018 | 2017 | 2016 | 2015 |
|---|---|---|---|---|---|---|
| Issuer Rating | A | A | A | A | A | A |
| Commercial Paper | R-1 (low) | R-1 (low) | R-1 (low) | R-1 (low) | R-1 (low) | R-1 (low) |
| First Mortgage Bonds[1] | A | A | A | A | A | A |
| Senior Secured Notes[1] | A | A | A | A | A | A |

1 Guaranteed by Énergir, L.P.

## Previous Actions

- DBRS Confirms Énergir Inc. at "A" and R-1 (low), Stable Trends, April 17, 2020.

## Previous Report

Énergir Inc.: Rating Report, April 29, 2019.

## Related Research

- DBRS Discontinues Rating on Valener Inc., September 27, 2019.
- DBRS Confirms Valener Inc. at Pfd-2 (low), Stable Trend, April 16, 2019.
- DBRS Comments on Proposed Acquisition of Valener Inc. by Noverco Inc., March 28, 2019.

Notes:
All figures are in Canadian dollars unless otherwise noted.

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