

MANITOBA HYDRO

2012/13 & 2013/14 ELECTRIC GENERAL RATE APPLICATION

UNDERTAKING PROVIDED BY: V. WARDEN

Manitoba Hydro Undertaking #44

Manitoba Hydro to inquire with its external auditors and to extent possible, provide copies of recommendations or advice received which show the strong indications made by them with respect to Manitoba Hydro's accounting practices.

Response:

Please refer to the attached email from Tanis L. Petreny, Partner, Ernst & Young, in which Ms. Petreny indicates that MH's changed accounting methodologies for overhead capitalization "is more consistent with the approach most companies employ and those of other utilities." Ms. Petreny also states that MH's former full costing methodology was "at the extreme end of costing methodologies" and that "we fully supported the shift in methodology... and strongly encouraged a change in costing methodology either under CGAAP or definitely upon the adoption of IFRS."

Warden, Vince

From: Tanis.L.Petreny@ca.ey.com
Sent: Tuesday, December 11, 2012 8:28 AM
To: Warden, Vince
Subject: Operating costs

Hi Vince

With respect to your question on operating costs, here are my thoughts:

Under Canadian GAAP, the measurement of cost of PP&E includes costs that are directly attributable to the construction. There was no further discussion of what comprised directly attributable costs and in practice this was a broad category. Companies applied different methodologies to determine directly attributable costs. In MH's situation, the approach captured all attributable costs under a full costing approach.

With the pending adoption of IFRS, companies took a closer look at what directly attributable costs should be included in the cost of an asset. IFRS is far more specific in its definition of directly attributable costs. Under IFRS, the distinction between directly attributable and general overhead costs is at a much lower level such that a full costing methodology as previously employed by MH would not be appropriate.

In preparation for the adoption of IFRS, MH re-evaluated its overhead capitalization methodology. While the accounting policy did not change, the methodology did similar to a change in estimate. As a result of this change in approach, MH's overhead capitalization methodology is more consistent with the approach most companies employ and those of other utilities. I also recall that PUB had noted in one of the Board orders that they felt the capitalization approach was aggressive and therefore the change was also meeting with their expectations.

Throughout our tenure as MH's auditors we assessed the capitalization methodology using a full costing methodology as acceptable but at the extreme end of costing methodologies. We fully supported the shift in the methodology as it is more consistent with what we see in practice and is better harmonized with existing accounting literature (IFRS). With the requirement to adopt IFRS, we did strongly encourage a change in the costing methodology either under CGAAP or definitely upon the adoption of IFRS.

I hope this helps craft your response for the PUB. Let me know if you need anything further or want to discuss any comments. You can call me on my cell at 204 471 7181 if you are unable to catch me in the office.

Regards,
Tanis



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