

MANITOBA HYDRO
Corporate Risk Management
Middle Office Report
September to December 2008

A. Credit

During the quarter, at the request of PS&O, review and advisory support was provided to the credit function.

B. Short Term Transactions

It was previously reported that complete compliance was unable to be verified on these transactions due to:

- a) Insufficient supporting documentation, and
- b) Relevant sections of Management Control Plan are difficult to assess compliance against

Work was initiated with Power Trading to develop supporting documentation practices for assessing compliance. Progress to date includes:

- A supporting documentation list was provided to Power Trading when entering into short term contracts.
- A subscription to PIRA was obtained. This will be used to review industry pricing data used by Power Trading for decisions. This was necessary since copyright and subscription rules restricted access.
- Notification of signed and available short term contracts has commenced.

The attached summary table outlines a position report for the period that includes total volumes and average price for contracts entered into by Power Trading (Export Power Marketing financial contracts are excluded).

Risks associated with these transactions are primarily price and volume. Applicable policy/control requirements are outlined in Appendix A for reference.

C. Related Merchant Transactions

Transactions reviewed for the period were determined to be compliant.

The attached table summarizes relevant information on the transactions for the period. Applicable policy/control requirements are outlined in Appendix B for reference.

The transactions involve trading energy purchased, not generated by the corporation. The volume of transactions is currently limited by the capacity of the related transmission positions (short and long term).

Risks associated with this activity, include the risk that the energy may not be accepted by the Canadian market, pricing may change in the Canadian market between the time energy is purchased in the day ahead market in U.S. and delivery of the sale into Canadian market at hourly or pre-dispatch price). In addition, a net position other than zero (purchases net of sale) may result in financial exposure. We would consider it to be a pure merchant transaction, which have not been approved at this time.

PS&O is developing revisions to trading risk limits to address recommendations made previously on these transactions. PS&O anticipates presenting the revisions shortly to the Market Committee.

Recommendations made include:

- Management Control Plan set risk parameters and limits related to the arbitrage transactions that are consistent with the EPRMC risk tolerance.
- Define transaction limits (such as the 1000 GWh) for transactions that are purchased to meet system requirements and later considered surplus separate from arbitrage transactions.
- Transaction limits for arbitrage trading include an intended zero net position.
- Defining/clarifying volume limits related to transmission of these trading activities.

Short Term Transactions
(Up to later of 5 months or next March 31st)

	VOLUME ON PEAK (MW) ¹				VOLUME OFF PEAK (MW) ³			
	Sept	Oct	Nov	Dec	Sept	Oct	Nov	Dec
Forecast surplus volume	not available				not available			
Volume Approved for Sale	300	300	300	150	0	0	0	0
Physical Bilateral	0	100	100	100				
Avg Price ²		\$70.00	\$70.00	\$70.00				
Financial Bilateral Swaps	0	0	0	0				
Avg Price ²	-	-	-	-				
Avg Index Price ²	\$41.29	\$38.42	\$40.00	\$54.39				
Remaining Surplus	300	200	200	200	0	0	0	0

¹ 5 X 16

² US dollars

³ weekend and off peak

Note:

Excludes financial contracts entered into by Export Marketing that include the Opportunity Portfolio up to the later of 5 months or the next March 31st.

Short Term Contracts - Related Policy

A. System Energy & Related Products - Management Control Plan¹

"System energy products include physical bilateral contracts, day ahead market and real time market power transactions and related products. The underlying intent for these transactions is the physical delivery of power to or from Manitoba Hydro's system."

Forward sales and purchase contracts, two weeks and longer in duration are formalized in writing in accordance with the applicable Master Agreement. The power trader or marketer negotiates these forwards sales using industry pricing indicators as a guide."

Pricing

- As a minimum, Hydro will require recovery of 110% of its incremental costs in making any short term forward sale commitment. The power trader or marketer uses this information along with industry pricing indicators to negotiate forward contracts.

Transaction Limits

- No specific limits established in the Management Control Plan for short term physical forward sales.

B. System Financial Products

Put and call options, swaps and bilateral contracts for differences for power or natural gas for the purpose of managing the uncertainty in available generation or load forecast or fuel supplies for Hydro's power supply assets. In addition, these products may be used to enter into favorable forward sales or to minimize exposure to price volatility on power and gas purchases.

Permitted Financial Products

- Put and call options, swaps, and bilateral contracts for differences. Financial Transmission Rights, auction revenue rights, virtual bids and offers and bilateral contracts registered as financial schedules.

Volume Limits

- Cannot exceed the projected underlying physical position.

¹ Approved by the Board of Directors November 22, 2007

C. Approval Authority

Transactions from existing generation or purchase from 15 calendar days up to the later of 5 months or the next March 31st:

Power Sales & Operations Market Committee or Division Manager Power Sales & Operations for volumes for purchase or sale *and*,

Manager, Power Trading or Financial Trading Supervisor for transactions.

D. Confirmation Method

Either orally or through electronic communication or approved electronic platform followed up by written confirmation. The Management Control plan states that written contracts are reviewed, approved, and signed in accordance with the approval authority requirements noted above.

Related Merchant Transactions - Related Policy

A. Merchant Transactions - Management Control Plan

Resale of power purchased from third parties and which either flows over transmission owned or reserved by/for Manitoba Hydro or was purchased for Manitoba Hydro system requirements and has subsequently been deemed surplus.

Transaction Limits

- Maximum net power position of 1000 GWh
- Fixed price to fixed price transactions may be entered into only if there is a positive profit margin
- All other transactions may be entered into only if there is a positive expected value and with a term no more than three days in duration.
- Maximum duration six months

B. Approval Authority

- Merchant Energy Products up to and including 14 calendar days in duration: Manager, Power Trading or Division Manager, Power Sales & Operations
- Merchant Energy Products Day Ahead: Day Ahead Power Trader or Financial Trading Supervisor
- Merchant Energy Products Real Time: Day Ahead Power Trader or Financial Trading Supervisor or Real Time Power Trader or Physical Trading Supervisor

**Middle Office Compliance Report
Related Merchant Transactions
Sept to Dec 2008**

	Sept		Oct		Nov		Dec	
Number Deals	366		418		389		365	
Duration	1 day		1 day		1 day		1 day	
% Total Deals with Losses	5.2%		9.6%		1.3%		15.6%	
	Total MWh	Total Settlement	Total MWh	Total Settlement	Total MWh	Total Settlement	Total MWh	Total Settlement
CDN Market								
Purchases[1]	145,335	5,471,515	147,214	5,860,939	161,530	6,689,358	79,723	3,463,122
Sales	<u>145,355</u>	7,195,948	<u>147,214</u>	6,723,363	<u>161,530</u>	8,577,497	<u>79,723</u>	4,299,070
Net Position	0		0		0		0	
Total Trading Gains/(Losses)[2]		1,724,433		862,424		1,888,139		835,948
Profit Share to Third Party								
Other[3]								
Purchases	1,054	35,539	4,283	240,933	3,949	181,845	13,713	650,539
Sales	1,054	<u>26,049</u>	4,283	<u>233,106</u>	3,949	<u>176,288</u>	13,713	<u>578,689</u>
Total Trading Gains/(Losses)		(9,490)		(7,827)		(5,557)		(71,850)
Profit Share to Third Party								
Transmission & Market Costs[4]								
Net Profit		<u>452,034</u>		<u>66,866</u>		<u>592,359</u>		<u>255,932</u>

Compliant

[1] US dollar purchases converted to CDN at Webtrader monthly rate

[2] Before transmission and market costs

[3] Purchases not accepted by CDN market and sold back into US

[4] Source: Webtrader monthly summary