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**200 – 393 PORTAGE AVE  
WINNIPEG, MANITOBA  
R3B 3H6**

**TEL: 204.985.8540**

**FAX: 204.985.8544**



**E-MAIL: [centre@pilc.mb.ca](mailto:centre@pilc.mb.ca)**

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Writer's direct line: (204) 985-8533  
Email: [bwilliams@pilc.mb.ca](mailto:bwilliams@pilc.mb.ca)

The Public Utilities Board of Manitoba  
Attention: Mr. Darren Christle, Executive Director and Board Secretary  
400-330 Portage Avenue  
Winnipeg, MB R3C 0C4

Dear: Mr. Christle

**Re: Revised Coalition Budget**

**Overview**

I am attaching for your consideration a revised budget estimate for the Coalition in this proceeding. As set out in Table 1 which is attached to this letter, we propose to revise the Coalition budget in the following manner:

- reduce the proposed budget for La Capra from approximately \$97,000 (Cdn) to about \$53,000 (Cdn) for a proposed downward revision of \$44,000 on the grounds that written evidence will not be presented;
- eliminate the budget requirement for Mr. Stevens for a proposed downward revision of roughly \$2,000 on the grounds that Mr. Stevens' insight was not requested by Mr. Colton;
- eliminate the proposed budget for Dr. Booth for a proposed downward revision of \$26,700 on the grounds that written evidence will not be presented; and,
- insert a new budget line for the depreciation expert Ms Lee for a proposed increase in the budget of roughly \$26,000 (Cdn) on the grounds that her written evidence is necessary to assist the deliberations in this proceeding.

As the Board will be aware, Coalition member CAC Manitoba prides itself on its ability to bring high quality experts to regulatory proceedings in a cost effective matter. As demonstrated during the NFAT proceeding, CAC Manitoba is capable of presenting a wide range of high quality experts provided there is a robust evidentiary foundation.

To the knowledge of legal counsel for the Coalition, this proceeding marks the first Hydro hearing in more than twenty year involving Coalition members in which they have chosen not to bring expert evidence already approved on a preliminary basis by the PUB. Given the unusual nature of this budget revision, we have taken the liberty of providing a detailed explanation of the rationale for the changes in the budget of the Coalition. We also share guidance from other jurisdictions and research which may assist in future filings.

Our letter highlights:

- the intent of the initial budget proposal of the Coalition; and
- the impact on the Coalition budget of the discovery process coupled with Board *Orders 18/15* and *33/15*.

In particular, we note the particular challenges our experts have experienced in their analysis of sustaining capital expenditures given the absence of robust filing requirements and deficiencies in first round information responses. In terms of deficiencies in discovery, we observe the experts retained by the Manitoba Industrial Power Users Group have expressed analogous concerns:

*Manitoba Hydro's information provided in the Application and in response to information requests from participants in this specific proceeding has failed on many key topics to provide the evidence needed to explain adequately the need and justification for the rate increases being requested at this time.<sup>1</sup>*

Our clients understand the challenges they are experiencing in this regulatory proceeding are part of a broader North American experience in which many utilities are just beginning to understand both the opportunity and the need to achieve efficiencies by modernizing their approach to capital asset planning and management. In parallel, some Canadian<sup>2</sup> and US<sup>3</sup> regulators are beginning to ask more of utilities in demonstrating that their expenditures and revenue requirements are “just and reasonable”.

Given market and regulatory evolutions in other jurisdictions, our clients recognize that Manitoba Hydro will need to undergo significant adjustments in modernizing both its capital management and its regulatory filings. For the information of Manitoba Hydro and the Board, our clients have attached two documents which they trust will give insight into both the nature of pre-filed information being sought by some regulators as well as the standard of Asset Health Indices which could form part of the foundation for an informed examination of sustainable capital expenditures:

- Appendix A sets out the Distribution System Plan filing guidelines all Ontario distributors must follow in their OEB rate applications. Sections 5.3 and 5.4 specifically address the details required regarding the asset management process and its link to capital spending; and,
- Appendix B provides a background document for Asset Health Indices and their integration into capital asset management which was developed by Deloitte for the Canadian Electricity Association with the assistance of firms such as Fortis, BC Hydro, Hydro Quebec and Hydro One.

In addition, we have provided a link to a small excerpt from the OEB filing of Power Stream relating to its consolidated system plan (section 5.3.3). While by no means the gold standard, the section should assist Manitoba Hydro in understanding the type of description of the asset management and prioritization process which might be expected in a modern regulatory filing:

[http://www.powerstream.ca/ContentMgr/attachments/G-2-1\\_ConsolidatedDistributionSystemPlan\(Chapter5FilingRequirements\).pdf](http://www.powerstream.ca/ContentMgr/attachments/G-2-1_ConsolidatedDistributionSystemPlan(Chapter5FilingRequirements).pdf)

We trust these documents will assist in future filings and proceedings.

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<sup>1</sup>Bowman, PFT, p. 4.

<sup>2</sup>Deloitte, Asset Health Indices, A utility industry necessity, p. 3.

<sup>3</sup>Audrey Zibelman, Chair of NYPSC quoted in *Utilities Profit Recipe: Spend More*, the Wall Street Journal, April 20, 2015.

### **The Intent of the Original Budget Proposal of the Coalition**

Prior to the filing of its initial budget proposal<sup>4</sup> and the particularization of its estimates,<sup>5</sup> the Coalition engaged in a lengthy series of meetings with other intervenors to identify issue priorities. It also met with Hydro, PUB advisors and intervenors in an effort to refine the issues list.<sup>6</sup> In commenting upon the Coalition application, the PUB noted that:

*The Consumer Coalition advised that it intends to examine the reliability of Manitoba Hydro's forecasts, the impact of projected costs, the utility's revenue requirement, and what would constitute just and reasonable rates. In particular, the Consumer Coalition proposed to examine consumer impacts and take the lead intervenor role on issues relating to financial targets, financial risk management and interest rate forecasting, and the testing of Manitoba Hydro's prioritization of expenditures on sustaining capital assets.<sup>7</sup>*

A significant element of the Coalition plan to test the merits of Hydro's case involved cross examination led by counsel from the Public Interest Law Centre and supported by Mr. Harper. In terms of evidence, the original plan of the Coalition was to:

- i) test the prudence of hydro expenditures and reliability of forecasts in three major areas:
  - a) sustaining capital expenditures through the retention of the La Capra firm by the Coalition;
  - b) interest rate and debt cost forecast through the analysis of Mr. John McCormick; and,
  - c) depreciation forecast through a witness retained by Manitoba Industrial Power Users Group.<sup>8</sup>
- ii) provide insight into risk management, the appropriateness of Manitoba Hydro's financial targets and their implications on its affordable access to debt through the collaborative analysis of Mr. McCormick and Dr. Booth;<sup>9</sup>
- iii) support the Green Action Centre in presenting insight into Manitoba specific energy poverty issues and a menu of options to address the energy poverty issue with Mr. Stevens providing

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<sup>4</sup>Intervenor Application Form including Attachment A *Preliminary Overview of the Proposed Intervention of the Consumer Coalition*.

<sup>5</sup> Coalition letter of February 6, 2015 responding to the PUB request for more particulars on estimates.

<sup>6</sup> CAC Manitoba and Winnipeg Harvest have worked closely with MIPUG in the past in identifying hearing priorities related to O, M and A and capital expenditures. CAC Manitoba also has worked closely with the Green Action Centre on issues related to energy efficiencies. These were in effect natural collaborations in which intervenors identified areas where they had substantial common ground and sought to efficiently divide case responsibility. The PUB directed focus on collaborations in the current proceeding was more ambitious given: i) the increased number of intervenors, ii) the potential conflict in positions among the intervenors; and, iii) the intent of designating a lead intervenor on an issue.

<sup>7</sup> PUB Order 18/15, p. 6.

<sup>8</sup> The Coalition noted that "In the event MIPUG chooses to call an expert witness on issues related to depreciation including the proposed approach to ELG and ASL, CAC Manitoba and Winnipeg Harvest will support MIPUG as may be requested." Attachment A to the Intervenor Application of the Coalition, p. 9.

Manitoba focused assistance to Mr. Colton. The intent was to initiate a robust collaborative outside the hearing process;

iv) assist the MKO in bringing information forward relating to energy efficiency and Northern issues; and,

v) bring forward the ratepayer perspective through consumer panels in collaboration with the MMF and perhaps other policy communities.

Subject to the provision of a satisfactory budget, *Board Order 18/15* approved expenditures on La Capra and Dr. Booth and rejected expenditures for Mr. McCormick and the ratepayer panel. Based upon our review, the *Order* appears to be silent on a budget for Mr. Stevens.

### **Explanation for the Proposed Budget Revision for La Capra**

#### **a) What a robust process might look like**

As the PUB will be aware, there are three parallel trends in North American utility regulation:

- some utilities are identifying material opportunities to cost effectively manage capital expenditures by moving away from *ad hoc* asset management and moving towards an evidence based decision making culture through a more robust link between improved operational management, better data analysis and rigorous budget prioritization;<sup>10</sup>
- there is considerable debate in the North American electrical industry related to allegations that the industry is “gold plating” capital expenditures for reasons that are not entirely related to issues of reliability, performance and the cost effective mitigation of risk;<sup>11</sup> and,
- some North American regulators are requiring improved analysis in support of accelerated corporate capital expenditures.

As noted by Deloitte in analysis prepared for the Canadian Electrical Association:

*In some Canadian provinces, regulators are demanding detailed analysis and justification for budgets being submitted by utilities. They are requiring information about asset health and condition, as well as long term views about necessary maintenance activities and system*

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<sup>9</sup>In its February 6, 2015 letter, the Coalition noted that “As recognized by other regulators, Mr. McCormick has successfully appeared in panels with experts such as Dr. Booth without material duplication.” The budget proposals for both Dr. Booth and Mr. McCormick expressly contemplated interaction between the witnesses. The proposed questions for Dr. Booth expressly considered interaction with Mr. McCormick: “Taking into account the evidence of Mr. McCormick relating to the reliability of interest rate forecasts in the current IFF, what are the implications, if any, for your previous conclusions regarding Manitoba Hydro’s reasonable access to affordable debt.” Attachment A to the intervenor application also makes reference to the potential of a joint presentation of the witnesses.

<sup>10</sup>According to Deloitte, one utility observed savings of up to 20% on their O&M costs as a result of better planning. Another reduced breakdown maintenance costs by 21% over a six year period. Deloitte, *Asset Health Indices, A utility industry necessity*, p. 23.

<sup>11</sup>See for example: *Utilities Profit Recipe: Spend More*, the Wall Street Journal, April 20, 2015. While some question the motives of industry players, others reject the allegation of “gold plating”.

*reliability.*<sup>12</sup>

Parallel trends in certain US jurisdictions were well characterized by the New York Public Services Commission:

*From now on, utilities must prove that their spending will make an electric system cleaner, more efficient or stronger. Business as usual has become unaffordable.*<sup>13</sup>

Deloitte also has noted that while steps are being made in Canada toward modernized management including a more robust analysis of data:

*there is a large variation in the maturity of AHI's for Canadian Utilities. While some are relatively advanced and well into the Predictive level, others are working at developing the basic steps required at the Reactive level. This is a reflection of the different scales of utilities (asset values ranging from \$100M to over \$55B) and different regulatory issues faced across the country. In addition, there is a general trend to lower maturity as you move across the model elements. In particular, a large number of utilities have Proactive Data Management, but lower maturity of Analysis and AHI consistency. This is to be expected, as strong Data Management is the first step towards enabling greater sophistication of analysis.*<sup>14</sup>

Recognizing that modern asset management involves balancing risk, performance and budget to create a capital plan, an operations plan and a maintenance plan, the intent of the Coalition in this proceeding was to examine the prudence and necessity of Hydro's proposed sustaining capital expenditures by considering:

- how the overall budget was determined;
- the basis for prioritization between business units;
- evidence relating to the condition of assets and how the determination of asset health was undertaken,<sup>15</sup> and,
- the prioritization process within business units.

The Coalition is aware that a robust examination of sustaining capital expenditures often involves:

#### Understanding the process and its practical application

- pre-filed evidence consistent with modern planning expectations sufficient to provide insight into

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<sup>12</sup>Deloitte, Asset Health Indices, A utility industry necessity, p. 3.

<sup>13</sup>Audrey Zibelman, Chair of NYPSC quoted in *Utilities Profit Recipe: Spend More*, the Wall Street Journal, April 20, 2015. The Coalition would add that strong performance data would be a check on a management philosophy of replacing assets simply because they are "old".

<sup>14</sup>Deloitte, Asset Health Indices, A utility industry necessity, p. 14. Based on the acknowledgements in the Deloitte Report, Manitoba Hydro does not appear to have participated in the study. Deloitte, p. 25.

<sup>15</sup>For example, see Deloitte. An Asset Health Index can be defined as a way of measuring the overall health of an asset; a list of data parameters for an asset that feed into a calculated health rating; a way of comparing different assets and asset classes in a consistent manner; an output of Big Data and asset analytics; an input, or building block, to a broader asset management process. Deloitte, p. 5. An AHI should help to address a number of the following questions: Which assets should be replaced vs. repaired? When should assets be replaced? What trends are evident in each asset class? What trends are visible across the asset portfolio? Can predictions be made on future asset failures? Can maintenance activities be optimized to reduce overall expenditures? Deloitte, p. 6

the planning and prioritization process, the data sets and modelling tools employed and the tradeoffs between maintenance and refurbishment as compared to new capital expenditures;<sup>16</sup>

- first round information requests aimed at better understand the application of the process and its implications for the merits of expenditures; and,
- post filing access to the planning models employed by the corporation along with a technical workshop to better understand model application.

Better understanding of specific decisions, consideration of options and questions of clarification

- through model analysis and second round information requests.

**b) The gap between a robust process, the Hydro filing and the Hydro disclosure**

As set out in Appendix C, the ability of Coalition experts to form an opinion on the merits of the application were hindered by the quality of original filing, the denial of access to Hydro models,<sup>17</sup> the choice by Manitoba Hydro not to offer a workshop to explain its models<sup>18</sup> and profound deficiencies in its first round information responses.

At the close of the first round information request process and contrary to their experience in other Canadian and US jurisdictions, Coalition experts were unable to develop a robust understanding of critical aspects of the Hydro asset management process, its application or the merits of its spending decisions. At a stage when they would normally be undertaking the critical draft of their evidence, the disclosure available to Coalition experts was below what they would expect from a robust, initial application, meaningful responses to first round discovery requests or an opportunity to explore modeling during a workshop.

An imperfect but more responsive series of second round information answers<sup>19</sup> left Coalition witnesses somewhat better informed but at a much later stage in the procedural schedule. For example, the response to Coalition II-53 d), the Manitoba Hydro 2012 Asset Condition Assessment by Kinectrics, Inc., would be one that Coalition experts would expect to be filed as part of the originating application due to its relevance to transmission projects under the sustaining capital expenditures.

Given the absence of robust disclosure of information that by its nature would require analysis and consideration, Coalition experts were not yet able to produce evidence with an opinion on whether Hydro's sustaining capital planning, operation and management process was reasonable. They are unable at this late stage of the hearing to offer an opinion on whether Hydro's proposed expenditures are prudent, necessary, and consistent with the statutory intent.

The Coalition will attempt to address some of the information gaps in Hydro's disclosure through cross examination with the hope that it will be able to form an opinion on the merits of Hydro's proposed

<sup>16</sup>Please see Appendix A. At a very high level this would include: a description of the asset management objectives; an explanation of the ranking of management objectives for the purpose of prioritizing investments; description of the data sets, primary process steps and information flows used by the distributor to identify, select, prioritize and/or pace investments; an understanding of a distributor's asset lifecycle optimization policies and practices to support the regulatory assessment of system renewal investments and decisions to refurbish rather than replace system assets.

<sup>17</sup>Board Order 35/15, p. 9/10.

<sup>18</sup>In a telephone conversation with the Coalition after Board Order 35/15, Manitoba Hydro indicated that it was not prepared to offer a workshop into its models. Among the reasons given were time pressures and the sense that the Coalition should have requested a workshop at the pre-hearing conference.

<sup>19</sup>See Coalition II-53 d) and II 52 a – f.

sustaining capital expenditures by the time of closing argument. Through its submission of this letter and through closing argument, the Coalition will attempt to outline a future process which the PUB might consider in order to robustly consider the merits of future Hydro applications.

### **Explanation of the proposed budget revision related to Mr. Stevens**

As explained in its Inteviewer Application, the Coalition retained Mr. Stevens to assist GAC witness, Mr. Colton, in the identification of appropriate Manitoba data and data gaps relating to vulnerable hydro users including relevant aspects of the social safety net.<sup>20</sup> Ultimately, Mr. Stevens' services were not requested by Mr. Colton.

### **Explanation of the proposed budget revision related to Dr. Booth**

There appears to have been a miscommunication between the Coalition, the PUB and Manitoba Hydro regarding Dr. Booth's participation in this hearing. While the Coalition saw his evidence as an element of a broader panel both the PUB and Hydro saw his evidence as a potential duplication of the areas to be addressed by Mr. McCormick.

As the Board may be aware, in prior Hydro hearings, CAC Manitoba has presented successful witness panels with complementary skills sets on issues related to Manitoba Hydro's reserves and financial targets. These panels have included Mr. Todd and Mr. Harper about 12 years ago and Mr. Matwichuk and Mr. McCormick in 2011. The choice to present witnesses in panels generally reflects a professional judgment that the skill sets of the witnesses are complimentary with one witness often being more focused on big picture issues and the other offering more technical analysis.

While perhaps imperfectly expressed, the intent of the Coalition was to present a panel similar to that which it had presented on prior occasions. As the Coalition noted in its letter of February 6, 2015, Dr. Booth had successfully appeared in panels with Mr. McCormick on prior occasions.<sup>21</sup> The budget proposals for Dr. Booth and Mr. McCormick expressly contemplated interaction between the witnesses with one of the proposed questions to Dr. Booth being:

*Taking into account the evidence of Mr. McCormick relating to the reliability of interest rate forecasts in the current IFF, what are the implications, if any, for your previous conclusions regarding Manitoba Hydro's reasonable access to affordable debt.*

Ultimately, the Board chose to approve Dr. Booth but not Mr. McCormick concluding that his evidence might be better suited for a subsequent GRA "to follow Manitoba Hydro's external review of its financial targets and risk assessment reports that are expected in the fall of 2015."<sup>22</sup>

Given the original intent of the Coalition to address "financial targets, financial risk management and interest rate forecasting" through an integrated panel and the Board's determination that much of that

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<sup>20</sup>Some of the proposed areas of research included: identify Manitoba data on the cost of electricity borne by low income households including an estimate of how many of those households are on income assistance and what proportion of those on income assistance pay for their own electricity vs. have the program pay for the utility and perform a similar analysis for on reserve households.

<sup>21</sup>The Alberta Generic Cost of Capital proceeding - Decision 2004-052 as well as ATCO Gas Decision 2003-72.

<sup>22</sup>Board Order 18/15.

information was better addressed in the context of a future General Rate Application, the question for the Coalition was whether ratepayers would get good value from Dr. Booth's evidence heard in isolation.

Ultimately, after reviewing the quality of information responses coupled with the Board's determination to defer a number of core issues to a later proceeding, the Coalition concluded that better ratepayer value would be achieved by deferring Dr. Booth's expert evidence. After consulting with Dr. Booth and Mr. Harper, a decision was made to test Hydro's evidence in this proceeding through cross examination using some of Dr. Booth's prior writing and other tools.

### **Explanation of the proposed budget revision related to the depreciation witness Ms Lee**

As the Board will be aware, Coalition members and MIPUG have undertaken periodic collaborations on matters of mutual interest in prior proceedings. The Coalition did not originally include a budget proposal for Ms Lee. However, the question of whether Hydro is unreasonably front loading depreciation costs was a core issue for CAC Manitoba in the 2013 GRA and for the Coalition in this proceeding. Attachment A to the Intervenor Application of the Coalition indicated that it would support MIPUG in the development of depreciation evidence if a decision was made to file that evidence.

In terms of the selection of the witness, the Coalition was aware of Ms Lee from her work in a prior Newfoundland proceeding. Ms Lee was originally selected and approached by MIPUG. Over the last couple of weeks, the Coalition became aware that MIPUG was having challenges retaining Ms Lee as a witness due to budget limitations. As the Coalition understands the issue, MIPUG does not have sufficient budget room to enable the preparation of oral evidence from Ms Lee or her appearance as a witness.

The Coalition met with Ms Lee and MIPUG by telephone on April 21, 2015. At that point in time, the Coalition formed the opinion that the evidence of Ms Lee would be of benefit to all ratepayers by clarifying some misunderstandings that might flow from the evidence of Mr. Kennedy and enabling a more vigorous discussion of the policy decisions related to the selection of ELG as compared to the status quo. The Coalition had the opportunity to review the proposed retainer of Ms Lee including the proviso that her evidence be fair, objective and non-partisan and to make suggestions on the proposed scope of her work.

The Coalition undertook a vigorous internal discussion on April 22, 2015 in order to assure itself that the evidence of Ms Lee would assist the PUB deliberations and benefit all consumers rather than any specific class. It also determined that in the event intervenor funding was provided it would be paid to Ms Lee via a direct contractual relationship with the Coalition rather than using MIPUG as a conduit.

Both the Coalition and MIPUG have made it clear to Ms Lee that the current budget does not contain sufficient resources to enable the preparation and presentation of oral evidence and that regulatory sanction has not been given to a Coalition budget related to Ms Lee.

The preliminary budget of Ms Lee is attached as Appendix E. The Coalition proposes that it cover Ms Lee's hourly rate up to the PUB approved maximum of \$223 an hour (Cdn) with MIPUG being responsible for the remainder up to Ms Lee's hourly rate of \$300 (US).



**Conclusion**

The focus of this letter has been on justifying budget revisions by the Coalition and in providing examples which might assist in future regulatory proceedings.

Like the PUB, Hydro and other intervenors, the Coalition is committed to a PUB process that is credible, efficient and effective in providing rigorous analysis. With regard to the current hearing, our client is concerned that certain aspects do not lend themselves either to rigorous analysis or to public confidence in the process.

The Coalition looks forward to an ongoing opportunity to discuss the modernization of regulatory filings and analysis in Manitoba with a goal to improving public confidence and the deliberative process.

Yours truly,

BYRON WILLIAMS  
DIRECTOR

BW/ah

Enclosures