M A N I T O B A | **Order No. 116/12**

THE PUBLIC UTILITIES BOARD ACT

August 29, 2012

BEFORE: Régis Gosselin, CGA, MBA, Chair
Raymond Lafond, BA, CMA, FCA, Member
Larry Soldier, Member

AN INTERIM MANITOBA HYDRO RATE ORDER
EFFECTIVE SEPTEMBER 1, 2012

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1.0.0 EXECUTIVE SUMMARY

The Public Utilities Board (Board or PUB) by this Order grants approval of a 2.5% interim increase on currently billed rates across all Manitoba Hydro (MH) customer classes effective September 1, 2012. The Board also approves, on an interim basis, rate schedules incorporating a 6.5% rate increase effective September 1, 2012 for the full cost portion of the rate applicable to General Service and Government customers in four remote communities served by diesel generation.

By this interim rate approval in the ongoing current General Rate Application (GRA) proceedings, the Board is protecting the short term financial status of MH. Given the timing of the GRA filing in mid June 2012, and that a new final rate Order will likely not be issued until early 2013, the interim rate increase allows for the timely implementation of the new rate structure and recovery of revenue in the interim period pending the Board's final ruling. This would avoid a larger percentage rate increase at a later date, should MH's application be approved.

If the Board concludes that MH has not met its onus respecting this interim rate request, the previous interim rate granted affected April, 2012, or any of the other rate requests MH has included as part of its' Application, the Board will adjust the rates in its final GRA Order.

2.0.0 LIST OF SHORT FORMS / ABBREVIATIONS

CAC	Consumers Association of Canada (Manitoba) Inc.
City	City of Winnipeg
DSM	Demand-Side Management
GAC	Green Action Centre
GRA	General Rate Application
G.S.	Generating Station
IFRS	International Financial Reporting Standards
MH	Manitoba Hydro
MIPUG	Manitoba Industrial Power Users Group
MKO	Manitoba Keewatinowi Okimakanak Inc.
NFAAT	Needs For and Alternatives To
PHC	Pre-Hearing Conference

3.0.0 PROCEDURAL HISTORY

On June 15, 2012 MH filed its General Rate Application for the test years 2012/13 and 2013/14 seeking to have the Board approve a series of interim rate increases and new final rate increases.

Specifically as to interim rates, MH seeks:

1. Final approval of a 1% interim rate the Board granted in its final GRA Order 5/12 which arose from a 2.9 % interim increase in Board Order 18/10 effective April 1, 2010 and that represented a 1% difference between what MH sought in the previous GRA and the 1.9% increase that the Board allowed. MH has maintained the 1% difference in a deferral account and seeks to add these funds to its revenue as part of its current rate requests.

2. Final approval of a 2% interim rate increase effective April 1, 2012 granted in Board Order 32/12.

3. Approval of a 2.5% interim rate increase effective September 1, 2012.

4. Approval of a 6.5% interim rate increase effective September 1, 2012 for the full cost portion of the rate applicable to General Service and Government customers in four remote communities served by diesel generation. MH also seeks final approval of all existing interim diesel zone Orders as part of the Board's final GRA Order.

Specifically as to new final rates, MH seeks approval for a further 3.5% increase for grid customers effective April 1, 2013 for the MH fiscal year 2013/14.

As part of the GRA proceedings, the Board directed MH to publish notice of the rate application with specific reference to all of the rate increases being sought including the September 1, 2012 interim rate requests. The Board determined that it would receive written submissions of Interveners and any other written submissions of interested persons as to their position on MH's September 1, 2012 interim rate requests. This written submission process was part of the general hearing notice published by MH.

The Board conducted a Pre-Hearing Conference on July 26, 2012 to consider which Interveners should be approved for participation in the GRA public process, to consider the scope of the GRA and to consider the timetable for the orderly exchange of evidence leading to a public oral hearing in late 2012. Intervener status was granted to Manitoba Industrial Power Users Group (MIPUG), Consumers Association of Canada (Manitoba) Inc. (CAC), Green Action Centre (GAC), The City of Winnipeg (City) and Manitoba Keewatinowi Okimakanak (MKO).

Given the timing of the GRA filing in mid-June 2012 and the timetable to complete the full hearing process, it is not anticipated that a final rate Order will be approved by the Board until sometime in 2013.

As part of the September 1st interim rate application process the Board considered the initial GRA evidence and further supplementary GRA materials filed by MH along with MH's written submission in support of the interim rate requests. The Board also considered the written submissions of MIPUG, CAC, and GAC and the written reply submission of MH. City and MKO did not participate.

The Board has benefited from the submissions of MH and all participating interveners as to the principles to be reviewed and the merits of a 2.5% September 1, 2012 interim rate increase. No submissions were received respecting the merits of the 6.5% diesel zone increase also to be implemented September 1, 2012 affecting General Service and Government classes.

4.0.0 MANITOBA HYDRO'S SUBMISSIONS

MH seeks interim approval for the proposed rate changes effective September 1, 2012 for the following reasons:

1. The need is urgent to avoid continuing losses on operations as will be evidenced in the Quarterly Report of the Manitoba-Electric Board for the three months ended June 30, 2012, which was to be released on or about August 15, 2012 (a by-election has held up release of the quarterly report);

2. Financial Ratios are deteriorating and are projected to further deteriorate in the test years;

3. It is essential that the financial and credit rating integrity of Manitoba Hydro be maintained;

4. Prices on the export market are not expected to improve substantially in the near term;

5. Costs are being well controlled and cannot be reduced further without negatively impacting the safety, reliability and efficiency of the power system;

6. The aging infrastructure issue will result in higher maintenance and capital costs in the future;

7. There is a separate government-approved process to review Manitoba Hydro's major capital projects; in the meantime, current rates do not include any costs related to capital projects before those projects are placed in service; and,

8. Even with the proposed rate changes, electricity consumers in Manitoba will continue to benefit from the lowest electricity rate structure in Canada.

If MH receives the increases it seeks, it currently projects that net income from electricity operations will be approximately $60 million for the year ended March 31, 2012, which is $79 million less than the net income for the previous year.

Moreover, MH now reports that its financial position has deteriorated significantly since the conclusion of the 2010/11 and 2011/12 GRA proceeding. Projected net income and retained earnings levels will be reduced due to the impact of the continued low prices in the export markets. Further, based on MH's forecast for 2012/13, total export sales volumes are expected to be lower than previously projected due to lower water inflows during the spring of 2012. In fact MH reports that from September 2011 to April 2012 precipitation across MH's watersheds was among the lowest on record over the last 30 years. A projected increase in domestic demand is also expected to reduce total export sales volumes.

For 2013/14, MH reports that its retained earnings will be significantly reduced on a one-time basis for accounting adjustments pertaining to the transition to IFRS.

Without the interim increases, going back to April 2010 in accordance with its rate requests, MH is projecting a net loss of $35 million in 2012/13 and a further net loss of $23 million in 2013/14.

By MH's calculations the rate proposals, if approved, will result in an overall average electricity rate increase of 3.57% for 2012/13 and 3.5% for 2013/14.

MH takes the position that increases at the rate of inflation are insufficient in the current circumstances to maintain a reasonable level of net income and to maintain its financial ratios. MH notes it is concerned about the projected decrease in its interest coverage ratio and the potential impact of the ratio deterioration on the credit rating of both the Province and MH.

With a 2.5% interim increase as of September 1, 2012, MH will recover an additional $20 million for the remainder of 2012/13 and together with the April 1, 2012 interim increase of 2%, granted in Order 32/12, the cumulative increases will lead to similar revenue as if a 3.5% rate increase had been granted on April 1, 2012. MH argues that if these increases are not granted now, greater rate increases may be required in the future to protect against net income reductions and negative credit rating implications. MH seeks, what it calls, these regular modest rate increases to ensure the maintenance of an adequate financial structure. MH argues that taking these steps now will protect it against its inherent operational risks and will promote rate stability in the long run.

MH's capital cost ratio objective is set at 1.2 so that it can recover surplus cash beyond what it needs for day to day operations. MH submits that it plans to continue to use the surplus cash generated to invest in the ongoing pre-building of major capital projects, including Bipole III, Keeyask and Conawapa, as it has been doing and as it did with Wuskwatim, the newest generating station to come into operation for MH. It states that to do so is a better proposition for ratepayers than allowing such funds to idle in a low-interest account.

On the expense side, MH states that Operations Maintenance and Administrative (OM&A) increases due to inflation plus the incremental new annual operating costs of Wuskwatim are offset partially by other productivity improvements and costs savings measures. International Financial Reporting Standards (IFRS) also impacts the expense side of MH's operating statement, requiring MH to move capitalized expenses to current OM&A for 2012/13.

Thereafter, MH projects OM&A to rise at the rate of inflation except for the years where significant operating expenses are added as the major generation and transmission projects of the future are brought into service.

As for the debt/equity ratio, MH projects that high levels of capital investment in major new generation and transmission projects combined with reduced net export revenues will result in a projected deterioration of the equity ratio to 12% by 2021/22. MH is predicting recovery of the debt/equity ratio to 75/25 by 2030/31.

Although MH argues that urgency is not a specific requirement to vest jurisdiction in the Board for approval of interim rates, MH submits that in fact there is an urgent need to avoid losses in operations at present and which supports its interim rate request under the current circumstances based on current projections. MH submits that the rates, if granted, will maintain the financial position of the Utility in the short term while allowing the full review of the total GRA rate request to proceed as planned.

No submissions were made by the Interveners, and no detailed explanation was provided by MH with respect to the diesel rate interim increase for General Service and Government accounts for September 1, 2012. MH has submitted that it wished to bring General Service and Government accounts to the same level of rate increases as at September 1st. MH submits that it is in line with the overall 6.5% previously granted to grid customers, which includes existing interim rate increases and inclusive of the requested 2.5% interim rate increase for September 1, 2012.

5.0.0 INTERVENER SUBMISSIONS

5.1.0 Manitoba Industrial Power Users Group (MIPUG)

MIPUG opposes the interim rate increase of 2.5% effective September 1, 2012. MIPUG makes no submission with respect to the 6.5% interim increase for certain diesel customers also to be effective September 1, 2012. MIPUG submits that in Manitoba, the legislature has prescribed an urgency test to be applied when the Board is considering granting an interim Order. Alternatively, special circumstances must exist for the Board to exercise its jurisdiction. MIPUG submits that the reasoning of the Supreme Court of Canada in *Bell Canada v. Canada (Canadian Radio-Television and Telecommunications Commission)*, [1989] 1 S.C.R. 1722, is instructive, in that the reasons of the SCC identify, in a similar situation, a broad discretion to grant interim rates but with the limitation being the need to grant temporary relief where financially serious consequences are shown and where the duration of the regulatory proceedings and associated delay in the final rate Order will further negatively impact the Utility's urgent situation.

MIPUG has cited a number of specific provisions of *The Public Utilities Board Act* (PUB Act) which it says leads to an interpretation that urgency or special circumstances are the basis upon which the Board may consider the granting of interim Orders. Even if the matter is considered urgent, argues MIPUG, the interim application puts the Board in the position of setting rates before it is fully informed. MIPUG offers the example that if the Board ultimately wishes to set differential rates between rate classes upon the conclusion of the GRA or upon the conclusion of a subsequent separate cost of service hearing process, it will be more complicated to perform the change in rate allocations if an interim across the Board rate increase is granted for September 1, 2012.

MIPUG submits that if the Board is prepared to consider an interim increase at this time, certain factors as to quantum and need for the increase, as extracted from a 2005 ruling of the Alberta Utility Commission, are useful guideposts.

MIPUG submits that the specific circumstances of this interim rate increase application do not support the requested increase. The Board rejected a 3.5% interim rate increase for a new interim rate effective April 1, 2012 and granted only 2% in Order 32/12. MIPUG submits that the current request amounts to, in effect, a review and vary application from that Order and as such is without merit. MIPUG submits that on inspection of Manitoba Hydro IFF 11-2, an improved net income is forecast compared to MH IFF 11-1, the financial forecast filed as part of Manitoba Hydro's application for an interim rate increase effective April 1, 2012.

MIPUG also comments that the cumulative rate increases will be 4.55% by the end of the fiscal year 2012 if 2.5% is granted September 1st, which is higher than the 3.5% increase initially sought as of April 1, 2012. MIPUG further states that this will also result in a higher base rate from which any April 1, 2013 increases will be calculated.

MIPUG cites a lack of urgency for an immediate response to the financial position of MH and notes that there will be little delay from the September 1st requested rate increase date to the start of the GRA hearing and then ultimately to the expected Board final rate

Order after the GRA hearing. MIPUG submits that the additional revenue to be generated as a result of this interim rate increase will have little impact on MH's retained earnings.

On its review of MH's filings, MIPUG identifies what it submits is a one - year effect on net income based on MH's projections for 2012/13. The main reason for negative net income in 2012/13, says MIPUG, is an anomalously high one-time depreciation expense forecast for 2012/13.

MIPUG submits that in all scenarios provided by the Utility, Manitoba Hydro's capital coverage ratio remains above 1.0. This means that the corporation remains cash positive on an operating basis and is borrowing solely for major new capital projects.

MIPUG submits that interim increases lead to uncertainty for ratepayers regarding final rates, which is a detriment to ratepayers in the balancing of factors before the Board to be considered in setting the Utility's rates. MIPUG concludes that MH has failed to demonstrate a real case of urgency or a net benefit to its customers and therefore the interim rates should not be approved

5.2.0 Consumers Association of Canada (CAC)

CAC also opposes the request for the 2.5% interim rate increase by MH. CAC does not specifically address the 6.5% interim diesel rate increase.

In addressing the Board's jurisdiction to consider interim rates and with reference to the *Bell Canada* case, PUB interim rate Order 18/10, and a rate-making academic reference, CAC advances a number of principles which ought to be taken into account by the Board. CAC suggests that the Board should avoid a rush to judgment before the GRA record is complete. While CAC acknowledges that the Board has regulatory discretion to set interim rates, it submits that the Board should do so only if it finds that the current rate is not just and reasonable while at the same time concluding that it is not possible at this time for the Board to make a final rate Order.

Further factors identified by CAC that may support a decision on interim rate-making include the potential for an anticipated lengthy delay in the regulatory proceeding and the necessity for a rate increase to allay the prospect of financial instability or serious apprehended financial difficulties which are found to exist and which would be further affected by delay in the full GRA proceedings.

CAC also reminded the Board of the principles enunciated in PUB Order 5/12 arising from the last MH GRA process regarding the ultimate determination of final rates for the test years under review. CAC urged that the Board use interim rates with caution and only in circumstances of extraordinary contingency or delay. Further, CAC submits that it has consistently taken the position that MH should not budget for a loss in net income.

With respect to the merits of the current specific interim rate increase, CAC noted that the rate increase leads to a 4.5% overall interim rate for 2012/13, which is greater than the 3.5% increase previously sought by Manitoba Hydro, and has the added effect of increasing the base rate entering the 2013/14 test year, thereby inflating the value of the proposed 3.5% increase for that fiscal year.

CAC questions the support for MH's allegation as to the imminent risk of financial ratio impacts, and notes that MH has not filed any specific current proof of the alleged risk.

CAC notes an increase in capital spending shown in IFF 11-2 v. IFF 10-2, which evidence it says does not match MH's assertion that it is aggressively working at capital expenditures management to meet only the needs of a safe, reliable and efficient service. Higher capital spending will lead to higher debt and interest costs, impacting the debt-to-equity ratio and interest coverage ratio of MH.

CAC submits that Board Order 32/12 disposed of an interim rate increase request with a similar percentage and the matter should not be re-visited at this time. Specifically, CAC argues that the GRA is on-going and that MH will have the opportunity to have its rate requests considered in a full hearing without inordinate delay. CAC submits that the urgency at this time is not at a level which warrants the interim rate to be granted.

CAC notes that transparency in the rate-setting process must be a priority for the Board, and states that any rate increase should occur after a full hearing that will better assist consumers in understanding the factors driving the rate increase.

With respect to MH's statement that its current projects showed a $75M decrease in net income compared to 2010/11, CAC states that when net income is compared not to the actual net income in that fiscal year, but rather to MH's projections set out in IFF10-2, then the current-year projected net income is only $10M less than what was projected in IFF 10-2, indicating that MH had already anticipated most of the reduction in income when it filed that forecast.

CAC also observes that MH's table of OM&A expenditures analysis as part of its July 2012 submission in support of the interim increase excludes costs associated with the new Wuskwatim generating station and increases arising from IFRS accounting changes. MH projects estimated revenue requirement impact with Wuskwatim in 2012/13 to be $106 million and $117 million in 2013/14.

5.3.0 Green Action Centre (GAC)

GAC confirmed that in its final submission in the previous GRA process, it supported MH's requests to finalize the April 1, 2010 interim rate of 2.9%, the April 1, 2011 rate of 2% up to the final Board rate Order, and a further 0.9% increase for the balance of 2011/12. GAC recommended at that time that the Board consider a 3.5% interim increase for April 1, 2012 to be reviewed as required at the next GRA.

By GAC's calculations, a 2.5% increase on September 1, 2012 will yield a cumulative 3.57% overall increase for 2012/13 when added to an increase of 2% effective April 1, 2012. GAC agrees that in totality all of the interim increases represent a 4.5% increase to base, being 1% higher than the 3.5% previously requested by MH.

GAC submits that MH has demonstrated a prima facie case reinforcing the Utility's need to effectively restore the rate levels it previously sought in the past GRA and as previously recommended by GAC.

GAC further stated that at the Pre-Hearing Conference in this process, it remarked on the structural dilemma facing the Board as to its role in considering major capital expenditures. GAC takes the position that the Board must determine the prudency of expenditures that contribute to the revenue requirement of MH and yet the Board has no jurisdiction to approve major capital expenditures. GAC notes that its support for the current September 1, 2012 interim increase does not equate to its support of MH's preferred development plan. Other options need to be publicly reviewed.

GAC identified MH's request for a 6.5% September 1, 2012 increase with respect to certain diesel customers, but was not in a position to make specific submissions as to that aspect of the rate relief.

GAC noted that Wuskwatim G.S. was coming on-line with negative net income, and expressed its concern that if Wuskwatim G.S. was indicative of new northern generation, then MH's net income might be expected to worsen rather than improve as Keeyask G.S. and Conawapa G.S. come into operation.

GAC also commented on Demand-Side Management (DSM), indicating that in the Christensen Associates report on Cost of Service, DSM was identified as part of a least-cost package of meeting domestic energy and capacity requirements, while MH's Power Resource Plan treated DSM as a component of dependable resources to serve both domestic and export load. GAC wondered whether this suggests an intention to measure the cost-effectiveness of DSM differently than the cost-effectiveness of new northern generation.

Ultimately, GAC supports MH's request for an interim rate increase. GAC submits that resource development is part of MH's mandate, and that this mandate drives large costs affecting MH's financial targets. While the Board should review the reasonableness of such costs, rates should provide adequate revenue to support all reasonable costs including resource planning and development costs.

Nonetheless, GAC does not support a segmented rates process leading to a “stop and start” pattern of rate applications based on large fluctuations in net export revenue. It is important, submits GAC, to look at revenue requirements in the contents of a longer run trajectory as a general guiding principle.

6.0.0 MANITOBA HYDRO’S REPLY

In reply to the Intervener submissions, MH submits that the Board has broad jurisdiction as to when and in what circumstances it approves interim rates. The ultimate appropriate consideration, submits MH, is meeting the public interest which it characterizes based on Manitoba Court of Appeal precedent as the balancing of the interests of the Utility’s ratepayers and the financial health of the Utility.

MH argues that MIPUG’s suggested interpretation of *The PUB Act* is incorrect, stating that there is no legislative language requiring a finding of urgency or special circumstances for the granting of an interim rate and no sound basis to conclude, in reference to other sections of *The PUB Act*, that urgency is necessarily implied. The *Bell Canada* case is not binding, argues MH, since it does not deal with *The PUB Act* and regulation of MH and since the issue decided by the Supreme Court of Canada (SCC) was not the jurisdiction to grant interim Orders but rather the issue of the CRTC’s jurisdiction to revisit an interim Order and issue a credit to Bell Canada’s customers under the appropriate governing legislation in that case.

MH notes that both MIPUG and CAC made the same submissions on the law relating to interim Orders in a hearing leading to the interim rate granted to MH by Board Order 18/10 (the Board notes the proper reference is to Order 40/11) within the last GRA process. MH states that in Order 40/11, the Board unequivocally found that urgency is not a requirement for the exercise of its power to grant an interim rate.

MH further notes that a final rate Order in the current GRA is not expected until 2013, and that it would not be in the best interest of ratepayers to absorb the full rate increase in the Spring of 2013. A modest further interim increase of 2.5% at September 1, 2012 will reduce the rate impact when the time comes, submits MH. Ratepayers will therefore benefit in the long run.

MH rejects MIPUG's view of the current interim rate request as a review and vary application. The Board, it notes, has jurisdiction to consider the request and procedural limitations as suggested by MIPUG have not been imposed by the legislature.

MH notes that MIPUG was incorrect when it submitted that MH was not forecasting a net income loss or cash shortage. MH restated that without the September 1st increase, it will return zero net income under current projections and further that without the 1% reinstatement respecting the deferred 1% rate pending from Order 5/12, it projects a $35 million dollar loss. MH also notes that MIPUG incorrectly referenced that there has been an improvement in MH's financial position as between IFF 11-1 submitted to this Board in March 2012 with respect to the April 1, 2012 interim rate request and IFF 11-2, which is the most recent financial forecast. In fact, the improvement relates to recovery of the 1% rollback from PUB Order 5/12 and not an improvement in the finances of MH as a result of its operations. In reply to the submission of CAC, MH states that CAC should support MH's position, since CAC asserts it is not in the best interest of ratepayers to allow the Utility to incur a net loss on operations.

MH reiterated that the Utility's financial ratios are a significant concern with potential immediate impact. MH highlights the fact that a capital coverage ratio of 1.0 is below MH's target of 1.2, and does not provide any cash support against adverse and variable risks.

In response to the submission of GAC, MH strongly disagrees that the Board has the responsibility for reviewing the reasonableness of MH's resource development costs. MH cited existing case law from the Manitoba Court of Appeal to support its position. The Board notes that the Court of Appeal has yet to render a decision on the jurisdiction of the Board to subpoena and consider MH's new export contracts, which matter also arose in the last GRA. In the context of the pending decision, the Court of Appeal may address this jurisdictional issue.

MH challenges MIPUG's analysis regarding the increase in the depreciation expense in 2012/13, stating that an increase in 2012/13 is primarily due to Wuskwatim G.S. coming into service, while a decrease in 2013/14 is caused by the implementation of IFRS. MH also specifically challenges CAC's characterization of MH's financial projections and capital spending.

7.0.0 BOARD FINDINGS

As it has found previously, the Board confirms that it has jurisdiction to approve interim rates for MH. The Board has also determined that this is an appropriate case to exercise the jurisdiction and to award an interim increase, pending final determination of all of the rate relief requested by MH at the conclusion of the GRA hearing.

MIPUG and CAC made the same submissions to this Board respecting the regulatory guidance to be found in the Supreme Court of Canada's reasons in *CRTC v Bell Canada* [1989] 1 S.C.R. 1722, when theses Interveners opposed an interim increase in the last GRA process. The Board addressed this in Order 40/11 finding that urgency was not a necessary condition to establish jurisdiction. The Board finds the *Bell Canada* ruling instructive as to what it may consider in determining an interim rate application, but accepts the submission of MH that the *Bell Canada* decision does not bind the Board.

The Board restates the conclusion that urgency is not required to establish its jurisdiction. By any terminology, however, MH's current financial situation is of significant or major concern, is problematic and warrants intervention.

Having considered the filings and submissions, the Board finds that MH has established, on a *prima facie* basis, justification and support for an interim 2.5% rate increase based on rate schedules incorporating the increase on currently billed rates across all rate classes, effective September 1, 2012 for grid customers and a 6.5% interim increase on the full-cost portion of the rate applicable to General Service and Government customers in the Diesel Zone also effective September 1, 2012. For the reasons provided herein, it is in the interest of ratepayers and the Utility to grant these increases and the Board finds that on the current available information these interim rates are reasonable and are required to meet MH's immediate financial needs.

Since Order 5/12 issued in the last GRA proceeding, certain of the anticipated and unfavorable operating conditions facing MH have come to pass and MH clearly has future challenges remaining arising from its identified operational risk factors as well as the Utility's ongoing plan to build new generation and transmission in advance of domestic need premised on profitable, international export sales.

The Board was well aware of the pending operating and financial risks facing MH at the conclusion of the last GRA process and as identified by the Board in Order 5/12. MH now reports that a number of these operational limitations have resulted in projected net losses for 2012/13 and 2013/14 if the interim increases are not granted.

Always unpredictable is the state of MH's hydrologic resources in any year, water being the key ingredient for MH's energy production. Very low precipitation on the watersheds feeding MH's system indicated lower than expected water volumes in spring 2012, as reported by MH to the Board in March 2012. The Board understands that water volumes have increased and are closer to median flows based on the most recent MH supplemental filings.

Projected low export prices continue in the test years, both due to the continued economic reality in the MISO export market region and the low price of natural gas which fuels competitive electricity generation alternatives. MH identifies these as the key factors to its current negative financial position.

MH's partial adoption of IFRS accounting and incorporation of certain applications of the IFRS accounting principles in the test years as part of its regulatory filing are noted but not accepted by the Board at this time for the purposes of this decision. This matter will be considered further in the hearing process.

Further, MH has placed the Wuskwatim Generating Station into service which requires MH to bring certain expenses onto its Operating Statement, adding pressure for increased revenue to meet additional expenses. The low export prices do not appear to fully offset the additional costs.

Finally, MH continues to spend significant amounts on the combined 'pre-building' phases of Keeyask, Conawapa and Bi-Pole III transmission line. Regarding the financing of these projects, less consumer revenue means greater debt financing than planned to fund this stage of these mega-projects, affecting MH's debt/equity ratio.

The Board also recognizes the commentary of GAC, MIPUG and CAC as to the negative income position reported by MH with the impact of the newly operating Wuskwatim GS and the remarks offered as to the continued level of spending and borrowing to maintain MH's Preferred Development Plan. These issues remain for further discussion in the main hearing. The Board finds that new Wuskwatim operating expenses are a material expense impacting MH's current financial projections for the test years and which results in MH coming forward with the interim rate increase request at this time.

MH reports, and the Board accepts for the purpose of this Application, that MH's consolidated financial results for 2011/12, although not yet publicly released, are close to what is projected in IFF 11-2. Further, although it has not released the quarterly report for the three month period ended June 30, 2012, MH reports that it has suffered a substantial net loss on electricity operations in the first quarter of 2012/13.

The Board has real concerns about the deteriorating financial position of MH and the negative turn in the financial ratios that will follow based on the projections filed by MH if the requested interim increases are not granted.

The Board appreciates that MH's revenues and expenses have not been tested and that the GRA process, now underway, will afford the Board and Interveners the opportunity to do so. However, given MH's current circumstances, it is arguable that if MH's case is borne out and the interim increase is not approved, much larger (and therefore less gradual) rate increases than originally planned will be required in 2013/14 since MH will not have recovered these revenues in the upcoming winter heating period while the GRA process unfolds leading to a final rate Order. The Board, as it has previously stated, disapproves of retroactive rate increases.

In accepting the financial projections filed by MH at this time, the Board does not make any binding conclusions as to the particular aspects of the financial details challenged by the Interveners and which have been addressed in detail by MH in its reply submission. It does not appear that there has been a material improvement to MH's net income position since the Board granted the 2% interim increase effective April 1, 2012. Moreover, there was limited time available for the Board to make its ruling leading to the April 1st rate Order. The Board has considered this Application based on all of the subsequent materials provided by MH.

CAC has highlighted the limited evidence currently available to support MH's assertion of curtailment of capital spending on all but essential elements of its operations to meet safe and reliable service standards, and has identified certain issues regarding OM&A expenditures and analysis by MH that should be examined further. MH will be expected to demonstrate the internal savings that the Corporation has realized in an effort to reduce expenses and improve net income. A portion of the quotation from the Moody's

Investors Service Credit opinion, dated February 7, 2011 and cited by MH, is instructive in this respect, noting that a weakening financial profile for MH may require larger rate increases, curtailment of capital spending or other action to ensure that the company continues to be able to independently service its debt.

The GRA hearing process followed by the Board allows for a comprehensive public review of MH's operations and the factors that impact rates. This serves the public interest by allowing for proper consideration by the Board, with the assistance of MH and the Interveners, of the filed Application and the issues and evidence addressing the issues that lead to the setting of just and reasonable rates. However, the process takes time.

By this further interim rate approval effective September 1st, the Board seeks to protect the short term financial status of MH given MH's current filed information and projections. If, after hearing all of the facts and submissions in the GRA process, the facts do not justify the imposition of the rate increases granted, the Board will adjust the rates in the final Order.

The Board remains of the view that consumer interests, balanced against the financial viability of the Utility, must always be protected. MH continues to bear the onus of establishing in the full GRA process that all of the rate relief, whether on an interim or final basis, is just and reasonable and that the financial health of the Utility and the interests of its domestic ratepayers are met in the result.

Since no final decision will be made by the Board until after the conclusion of the full GRA process and since the interim rate Orders do not bind the Board as to final rates to be determined, Interveners should use the GRA process to fully test all rate related issues. The increase is only granted to preserve the financial stability of the Utility based on current available information and upon consideration of the submissions made. It is therefore not a preliminary finding on the merits and the Board is not to be taken as having drawn any conclusion as to the ultimate outcome of MH's rate case at this very early stage of the proceeding. As for the adjustment of all rates, and the issues raised by the Interveners respecting the creation of a larger base rate going into 2013/14 arising from a cumulative 4.5% series of increases on 2012/13, all of those matters are capable of variance in accordance with the Board's jurisdiction on final rate approval for MH.

The Board specifically notes that a decision to finalize the following interim rates should be taken after consideration in a full hearing when supporting evidence for the request can be fully tested by the parties:

- 2% interim rate increase granted effective April 1, 2012 in Board Order 32/12
- 1% interim rate increase initially granted in Board Order 18/10 that has been accumulating in a deferral account since the Board issued Order 5/12.

Cost of Service Studies, as an input in the rate structure for MH remains an ongoing matter affecting rate-setting and the Board is mindful of the concerns and issues raised by both MIPUG and GAC that impact rates for the various classes of consumers. Uniform rate increases across all classes could potentially disadvantage certain classes, depending on the other considerations which the Board may take into account in the existing circumstances of the rate request. As directed in Order 98/12, the Board plans to establish a process to consider MH's Cost of Service methodology. The Board is satisfied that there will be options to address costing principles and allocations for the purpose of fixing rates going forward, and does not find that the added complexity is a basis to reject the current interim rate increase across all rate classes.

The Board does not intend this Order to be a signal to MH or any party to the proceeding, or indeed to ratepayers, that it endorses a segmented interim rate process as the desirable method for rate setting for the Utility. Rather, and as submitted by MH, the Board must address an Application that is brought before it within the jurisdiction of the Board and must properly determine if the rate requested is just and reasonable on the information before it, in light of the timing of the larger ongoing GRA process and in addressing the balancing of the factors to meet the public interest for its rate setting mandate for MH.

The Board accepts the principles advanced by GAC, and as previously identified as an objective by MIPUG, that rate reviews and related processes should lead to predictable, stable rates including rate increases where they are found to be reasonable for the benefit of all electricity consumers and for the maintenance of the financial health of the Utility. The Board also recognizes one of the hallmarks of its ongoing responsibilities, as noted by CAC, that the processes employed and final outcomes be as transparent as possible so that consumers can follow the rationale and factors driving rate increases. At this time, the Board finds that the financial predicament of MH is the factor that weighs most heavily in favour of approval of this rate request.

PUB decisions may be appealed in accordance with the provisions of Section 58 of *The Public Utilities Board Act*, or reviewed in accordance with section 36 of the PUB's Rules of Practice and Procedure (Rules). The PUB's Rules may be viewed on the PUB's website at www.pub.gov.mb.ca.

8.0.0 IT IS THEREFORE ORDERED THAT:

1. Manitoba Hydro's request for a 2.5% interim rate increase, effective September 1, 2012, BE AND IS HEREBY APPROVED, on an interim basis for all domestic customer classes;

2. Manitoba Hydro's request for a 6.5% interim rate increase effective September 1, 2012 on the full cost portion of the rate applicable to General Service and Government customers in four remote communities served by Diesel Generation BE AND IS HEREBY APPROVED, on an interim basis.

3. Manitoba Hydro is to file, for Board approval, revised rate schedules and customer bill impacts to reflect the September 1, 2012 interim rate increases.

4. The September 1, 2012 rate increases are granted on an interim basis only and are subject to being reversed, varied or finalized by subsequent Order of this Board.

THE PUBLIC UTILITIES BOARD

"RÉGIS GOSSELIN, CGA, MBA"
Chair

"HOLLIS SINGH"
Secretary

Certified a true copy of Order No. 116/12 issued by The Public Utilities Board

Secretary