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Undertaking # 3

MPI to advise at what percentile level was Basic total equity exhausted in the simulations.

RESPONSE:

The Corporation applied the full amount of management action corresponding to the following table. Excluding the applied for 4.3% rate increase in 2017/18, the assumed management action totals a 6.0% Rate Stabilization Reserve (RSR) rebuilding fee over three years, with a 6.0% rate change over two years. On a compounded basis this represents a total rate increase from 2018/19 to 2020/21 of 12.46%.

	2016/17	2017/18	2018/19	2019/20	2020/21
Rate Changes	0.0%	4.3%	0.0%	3.0%	3.0%
Add’l RSR Rebuilding Fee	0.0%	0.0%	2.0%	2.0%	2.0%

With management action, one of the 5,000 4-year scenarios will deplete, to zero, the Basic Total Equity corresponding to an MCT ratio of 70%.

With management action, none of the 5,000 4-year scenarios will deplete, to zero, the Basic Total Equity corresponding to an MCT ratio of either 80% or 90%.

The analysis requested in this undertaking appears to be testing probability of total capital depletion from a near fully funded RSR (at 70%, 80%, or 90% of MCT). That analysis, dealing with total depletion, is more relevant to the lower RSR threshold. The lower RSR threshold is set to a level appropriate to maintain the satisfactory financial condition of Basic as determined by the DCAT at a certain threshold (i.e. 1-in-40 as defined by the PUB).

MPI respectfully suggests that, when looking at the upper RSR target, the analysis in this undertaking is not the most pertinent inquiry. MPI views that the relevant capital depletion scenario to consider in this exercise is the depletion of capital down to the

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lower RSR threshold (not zero), which triggers a rebuilding fee, and contributes to rate volatility. The scenario MPI seeks to avoid is a rebate to customers in a given year, bringing capital down to 100%, followed by a significant depletion of capital in the ensuing year(s) to require a rebuilding fee to meet the minimum threshold.

The probability of this depletion should be considered absent management action, as an RSR rebuilding fee would not be sought when capital levels are above the minimum threshold. MPI has calculated that the four year scenario that depletes total equity from $411 million (100% MCT) to $159 million is a 1-in-49 year scenario. That scenario is significantly more likely than a total depletion of capital, and also more germane to the purpose of the upper RSR threshold.

Indeed, MPI has recently experienced losses that required approximately $150 million in capital transfers to maintain Basic Total Equity at the minimum threshold. MPI elaborates on these financial losses in response to CAC (MPI) 1-113, where it provided evidence to demonstrate the plausibility of the adverse scenarios through the Dynamic Capital Adequacy Test (DCAT) report. Ultimately, the adverse scenarios that could deplete between $150 to $250 million are, in MPI's view, plausible and have to some extent been experienced in the recent past.