MANITOBA PUBLIC UTILITIES BOARD

Re: CENTRA GAS MANITOBA INC.
2005/06 TO 2006/07
GENERAL RATE APPLICATION

Before Board Panel:

Graham Lane - Board Chairman
Monica Girouard - Board Member
Mario Santos - Board Member

HELD AT:

Public Utilities Board
400, 330 Portage Avenue
Winnipeg, Manitoba
June 13th, 2005
Volume VI
Pages 1241 to 1455

APPEARANCES

R.F. Peters		)Board Counsel
Marla Murphy		)Manitoba Hydro
Karen Melnychuk		)Direct Energy Marketing
David Brown	(np)	)Limited/Municipal Gas
Nola Ruzycki		)Energy Saving (Manitoba)
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--- Upon commencing at 9:06 a.m.

THE CHAIRPERSON: Good morning, everyone. I had a good weekend. We're returning to Mr. Saxberg. Ms. Murphy, you have something else for us here.

MS. MARLA MURPHY: I do. Thank you. Just before we begin, we have circulated the consultation results on customer education, which I believe should be Centra Exhibit 21. You'll find some of the material in that, although it's rather thick-looking, should be familiar to the Board. The report is -- attached is some information that's been previously provided.

--- EXHIBIT NO. CENTRA-21: Consultation results on customer education.

THE CHAIRPERSON: Thank you.

Mr. Saxberg...?

VINCE WARDEN, Resumed:
DARREN RAINKIE, Resumed:
WILLIE DERKSEN, Resumed:
DAVID CASE, Resumed:
AZIZ AZIZ, Resumed:

CONTINUED CROSS-EXAMINATION BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Thank you, Mr. Chairman, and good morning to all. I want to go back to the $18.8 million figure. And that calculation of that amount is at Tab 4 of my Book of Material.

(BRIEF PAUSE)

MR. KRIS SAXBERG: Second page in. I understand, Mr. Warden, from your testimony at the last GRA, that the $18.8 million number was a calculation of the incremental impacts for the year 2003/04; is that correct?

MR. VINCE WARDEN: Good morning. Yes, that's correct.

MR. KRIS SAXBERG: And that it was not necessarily representative of each and every other year over the thirty (30) year term?

MR. VINCE WARDEN: There will be some changes over that thirty (30) year term, yes.

MR. KRIS SAXBERG: And one (1) of the changes that occurred to me after we adjourned last week was that because there's a portion of that figure that -- that is relating to amortization of the net write-up of assets, won't there be a reduction in carrying costs as the net write-up of assets is paid down?

MR. VINCE WARDEN: Yes, Mr. Saxberg. I believe we covered that last week at -- in our discussion.

(BRIEF PAUSE)

MR. KRIS SAXBERG: Would you be prepared to -- to take as an undertaking the 2005/06 incremental cost assumed by Manitoba Hydro and the 2006/07 incremental cost assumed by Manitoba Hydro and, for that matter, carrying forward until the expiry of the thirty (30) year period?

MR. VINCE WARDEN: Yes, we can certainly do that. There will not be significant change in the test years but we can -- we can certainly provide that information.

--- UNDERTAKING NO. 21: Centra to provide CAC/MSOS with the 2005/06 incremental cost assumed by Manitoba Hydro and the 2006/07 incremental cost assumed by Manitoba Hydro, carrying forward until the expiry of the thirty (30) year period.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Last week we were discussing this accounting of the acquisition and integration costs in an organization which you referred to as Manitoba Hydro Corporate; you recall that?

MR. VINCE WARDEN: Yes, I do.

MR. KRIS SAXBERG: Can you tell me more about Manitoba Hydro Corporate?

What it -- what it is first of all; is -- is it a separate corporation?

(BRIEF PAUSE)

MR. VINCE WARDEN: Mr. Saxberg, it might be helpful for you to refer to Centra Exhibit Number 12, that was Undertaking Number 6, in which the corporate note -- or the segmented note that is, to Manitoba Hydro's consolidated financial statements was provided.

And you can see, if you have that in front of you, you can see that corporate contains only those costs which have been incurred to acquire Centra Gas. And it was laid out in this way to make it perfectly clear exactly the costs that were being incurred by the corporation for the acquisition and how those costs are being allocated to gas and electricity ratepayers.

So, in direct answer to your question, corporate only includes the -- the acquisition costs associated with Centra Gas.

MR. KRIS SAXBERG: But is there an actual separate corporate entity?

MR. VINCE WARDEN: There's no legal entity and, as you can see from this exhibit, the corporate account is -- is zeroed out at the end of -- at the end of the fiscal year.

MR. KRIS SAXBERG: And when did this presentation of the acquisition and integration costs begin?

MR. VINCE WARDEN: What we're referring to here is the 2003/04 year-end financial statements. The first year we used this was in '02/'03.

MR. KRIS SAXBERG: Now, prior to this particular presentation of the acquisition, all of the costs of the acquisition were pushed down into Centra Gas; were they not?

MR. VINCE WARDEN: Initially, they were, until we received an Order of the Board -- I can confirm the number for you if you like -- but we received an order of the Board that asked us not to do that, and we complied.

MR. KRIS SAXBERG: So, the first year that you complied with that order was 2002/03 and that's the first year that a corporate allocation is -- surfaces?

MR. VINCE WARDEN: Yes, Mr. Saxberg, you're correct. However, we did make the change retroactively so that any push-down that occurred to Centra Gas was -- was removed and all prior years were stated consistent --consistently with '02/'03, with the one (1) exception, that is there was no corporate allocation prior to '02/'03.

MR. KRIS SAXBERG: Well, in determining net income for the year 2001/02, were there not costs associated with the acquisition included in -- in the determination of the net income figure?

MR. VINCE WARDEN: Yes. If you go back to the financial statements -- the published financial statements for '01/'02, you will see the push-down occurred at that time. But, as I explained previously, with the more recent financial statements in '02/'03, '03/'04, those push-down entries were reversed and -- to make the statements comparable with the presentation in '02/'03 and '03/'04.

MR. KRIS SAXBERG: Did you reissue the financial statements?

MR. VINCE WARDEN: As is typical with financial statements, a note is put in the financial statements indicating that the presentation of the current year -- or presentation of previous years has been adjusted to conform with the current fiscal year.

MR. KRIS SAXBERG: Sir, are you telling the Board that net income for 1999 through to the end of 2002, or March 2002, was adjusted to take out the costs relating to the acquisition that were previously in the financial statements?

MR. VINCE WARDEN: Retained earnings were adjusted to reflect the methodology that was adopted in -- in '02/'03.

MR. KRIS SAXBERG: Can you tell me what increase in retained earnings there was then as a result of that change of accounting?

MR. VINCE WARDEN: I can get that number for you, Mr. Saxberg.

MR. KRIS SAXBERG: Thank you.

(BRIEF PAUSE)

THE CHAIRPERSON: Mr Warden, just a point of clarification, because I realize that Mr. Saxberg is referring, of course, to the Centra financial statements themselves.

On a consolidated basis, this retroactive wouldn't have had any impact at all on the consolidated financial statements of Manitoba Hydro, would it?

MR. VINCE WARDEN: That's correct, Mr. Chairman.

(BRIEF PAUSE)

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Mr. Warden, I want to take you back to the approach that Centra was taking at the last General Rate Application. And I have with me excerpts from the transcripts of that proceeding, I'd like to pass them out.

(BRIEF PAUSE)

THE CHAIRPERSON: Mr. Saxberg, just for ease of handling, do you have the exhibit number for this?

Or, Mr. Singh, do you?

(BRIEF PAUSE)

THE CHAIRPERSON: Number 5? Thank you.
MR. KRIS SAXBERG: Thank you, Mr. Chairman.

--- EXHIBIT NO. CAC/MSOS-5: Excerpts from transcripts taking from the last General Rate Application.

(BRIEF PAUSE)

MR. KRIS SAXBERG: And I have another excerpt that I also want to introduce at this period of time, relating to the same material, and I'll hand that out now as well.

(BRIEF PAUSE)

THE CHAIRPERSON: So this one then would be CAC/MSOS Number 6.
MR. KRIS SAXBERG: Thank you, Mr. Chairman.

--- EXHIBIT NO. CAC/MSOS-6: Excerpt relating to the

last General Rate
Application.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: And perhaps I'll attempt to summarize the approach that was being taken by Centra at the last Hearing as follows.

Centra was looking for the return on equity of approximately $15 million and along with that a synergy transfer of $7 million to, number 1, pay for the acquisition and integration costs of approximately 20 million and contribute to a small net income of approximately $3 million.

And, Mr. Warden, that information is best summarized in your answer beginning on page 184. And perhaps you could take a moment and read that response.

(BRIEF PAUSE)

MR. VINCE WARDEN: Yes, Mr. Saxberg, I think what I was saying there was consistent with what we're demonstrating on Undertaking number 4 in your Book of Documents; that is the 18.8 million that's referenced at Tab 4, so essentially $19 million or $20 million.

We were talking, I think at that point in time, about the equal annual amount that was required to amortize the -- the total investment over thirty (30) years.

I think we've agreed that we were talking probably two (2) different numbers. But the 19 million per year essentially that we're referencing at -- in Undertaking 4 and in the consolidated note to the financial statements -- the segmented note that is, is the amount that has to be recovered each and every year.

So, the amount that would do that would be -- assuming there -- there was a rate of return in Centra of 15 million, the 15 million plus an amount of seven (7), obviously 22 million, would be sufficient to cover the total acquisition costs on an annual basis.

MR. KRIS SAXBERG: So, you agree that it was Centra that was suggesting that the return on equity was what was to be used to pay down the acquisition and integration costs?

MR. VINCE WARDEN: Well, Mr. Saxberg, I would have to read this a little bit more the background to our discussion here because we do, as you know, flip between return on equity and cost of service.

Regardless of -- of that though, I think we have been consistent in stating that we do require this $19 million per year, whether it will be from a return on equity that will generate 15 million plus the $7 million that the amount is still the same.

So, regardless of how we get there it's still the same requirement.

MR. KRIS SAXBERG: And I want to compare that analysis of $22 million needed to pay the 19 million and to contribute to retained earnings with the position that's been taken in this Hearing for rate base rate of return.

Would you agree that your rate base rate of return material indicates that Centra's seeking a return of approximately 13 million, plus 12 million for the corporate allocation, plus an additional 3 million net income?

MR. VINCE WARDEN: Do you have a reference for that, Mr. Saxberg?

MR. KRIS SAXBERG: Well, Schedule 3.0.0, I think.

MR. BOB PETERS: It might be at, Mr. Saxberg, Tab 13 of the brief of documents that I've provided to the witnesses earlier; that might be a place to readily locate it.

MR. KRIS SAXBERG: Thank you, Mr. Peters.

MR. DARREN RAINKIE: Mr. Saxberg, I think you and I discussed this last Wednesday, towards the end of the day and I don't think I agreed with that proposition.

I explained that the corporate allocation, as it was back then, stated that 15.1 million was to pay for hard costs. We weren't -- and that wasn't part of the return that we were looking for.

I guess I was talking about the purpose of the money as to what flag we attached to it, rather it's return or a cost or whatever. So, I think we had this discussion and you asked me if it was double-counting and I indicated that I didn't think it was -- didn't think it was, in my view.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: I'm looking at -- under the heading, Rate Base Rate of Return, for the 2005/06 test year. Line 19 indicates a corporate allocation of 15.1 million. Line 21 indicates a return on equity of close to 12 million.

You see that, Mr. Warden?

MR. VINCE WARDEN: Yes, I do.

MR. KRIS SAXBERG: If I add those two numbers together we're looking at $27 million in total, correct?

MR. VINCE WARDEN: Mr. Saxberg, you can

add them together but realize our application is -- is column number 1, so you should be adding fifteen one forty-one (15141) and the one seven seven nine (1779). And, of course, this has been updated with the 12 million allocation not the fifteen (15).

MR. KRIS SAXBERG: But just focussing on the moment on the rate base rate of return calculations that have been provided, you'll agree that you're asking for an additional 5 million above what you'd asked for and indicated was required at the last hearing?

MR. VINCE WARDEN: Mr. Saxberg, that isn't out application.

MR. KRIS SAXBERG: Do you understand that the Board has asked Centra to prepare a rate base rate of return calculation in order that it can compare the revenue requirement derived using that methodology with the cost of service --

MR. VINCE WARDEN: And that's the sole purpose of Schedule 3.0.0, to make that comparison. But, remember, our application is Column 1, we're not asking for Column 2.

MR. KRIS SAXBERG: I know. But don't you think it's important then that the rate base rate of return revenue requirement calculation be the appropriate one so that you can appropriately measure it against the cost of service revenue requirement?

MR. VINCE WARDEN: I believe that's what Schedule 3.0.0 was doing.

MR. KRIS SAXBERG: Now, you indicated, Mr. Warden, at the last GRA that $3 million a year was an appropriate amount for retained earnings; and I'm looking at CAC Exhibit 6.

(BRIEF PAUSE)

MS. MARLA MURPHY: Could you give us the reference for that?

Is there a page and line number?

MR. KRIS SAXBERG: Sorry, it's CAC Exhibit 5 and it's page 199, the answer beginning on line 8.

MS. MARLA MURPHY: Thank you.

(BRIEF PAUSE)

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: And for the record, Mr. Warden, the answer at line 13 at page 199 indicates that $3 million was the deemed amount for retained earnings at that time; it was deemed to be the appropriate amount for retained earnings?

MR. VINCE WARDEN: Yes, well, Mr. Saxberg, we do present a financial forecast to the Board of Manitoba Hydro/Centra Gas every year, and that forecast takes into account current conditions.

What we're talking about here, I believe, was the forecast prepared in the fall of 2003. And, at that time, I take from the discussion, that there -- there was -- there was a -- sorry, I was corrected on that, it was the fall of 2002. So we've had a couple of forecasts since that time.

So, at that particular time, going back to 2000 -- the fall of 2002, the Board of Manitoba Hydro/Centra Gas determined that in that particular year that we were discussing at that time, the $3 million transfer to retained earnings was -- was adequate.

I indicated in that answer, I believe, that it's prudent to have some transfer to retained earnings and the $3 million, at that time, was deemed to be the right amount.

MR. KRIS SAXBERG: And if I could now refer you to CAC-6 and page 2114, where you indicate, and I'll read it into the record, the Chairman asks, at line 9:

"I understand that completely, Mr.

Warden, but I guess the question that I'm trying to get a handle on is: Have you given any consideration to the kind of retained earnings that you'd like to build up over a period of time inside of Centra?"

And your answer, Mr. Warden, was:

"Well, really, as long as there's -- I should back up and say that the financial targets, as we talked very briefly about this morning, are set at the corporate level. So we -- Manitoba Hydro has a number of subsidiaries and as long as those subs are contributing towards the financial targets of the parent, then we're reasonably happy. So although we haven't set a specific target within Centra or CHES or any of the subsidiaries, as long as they're not negatively impacting the financial targets of the parent company, we have no concern."

Is it still your position that as long as the subs are not negatively impacting the financial targets, that you have no concern?

MR. VINCE WARDEN: No, I think I indicated there, at line 20 of the excerpt that you read, that we were reasonably happy, so we weren't totally happy; I would take from that. At that time we didn't have financial targets for Centra but -- but now we do.

The updated financial forecast does in fact -- or the forecast that we will be presenting in the fall of 2004 will -- 2005, sorry -- going back in time here -- but the -- the updated forecast that we present to the Manitoba Hydro/Centra Board in 2005 will reflect the fact that the Board of Manitoba Hydro has approved financial targets, or Centra Gas, and those were approved in March of 2005.

MR. KRIS SAXBERG: In this Application you're asking for retained earnings of approximately $5 million for the first test year and $14 million for the second test year, correct?

(BRIEF PAUSE)

MR. VINCE WARDEN: Mr. Saxberg, our Application, as referenced on Schedule 3.0.0, had a net income which is a transferred to retained earnings of one million seven seven nine (1,779,000) in '05/'06 and eleven million three-o-eight (11,308,000) in '06/'07.

Now, as you know, we did make some changes to the corporation allocation, which means those numbers that I've just referenced would go up by $3 million in each of those respective years.

MR. KRIS SAXBERG: So, approximately $5 million for the test year 2005/06, correct?

MR. VINCE WARDEN: Well, as I've just explained, it's one million seven seven nine (1,779,000) plus the 3 million, so it's four million seven seven nine (4,779,000) to be precise.

MR. KRIS SAXBERG: And to be precise with respect to the second test year, we're looking at a request for net income of fourteen million three hundred and eight thousand ($14,308,000)?

MR. VINCE WARDEN: Eleven million three o eight (11,308,000) that's in our Application, plus the $3 million we referenced would be fourteen million three-o-eight (14,308,000).

MR. KRIS SAXBERG: And that figure, you'll agree, is higher than what Centra would have been entitled to under rate base rate of return regulation?

MR. VINCE WARDEN: Comparing to the -- again, looking at -- referencing schedule 3.0.0, that amount is simply a transfer from line 19 to line 21, and as you can see the total -- the grand total is still lower than it would have been under rate base rate of return. We're not changing -- changing the total, it's just a shift from one -- one line item to another.

I'm -- I'm talking strictly about the profit component under rate base rate of return, which is a return on equity of $12.6 million for the '06/'07 test year?

MR. VINCE WARDEN: Well, I -- you can certainly do that if you like, but I wanted to point out that the total is still unchanged, and therefore the total under -- under cost of service -- our Application is still lower than it would have been under rate base rate of return.

MR. KRIS SAXBERG: How do you explain to ratepayers that after the 2006 -- after May of 2006, they'll be paying on a year over year basis, a profit to Centra of $14 million a year, until you come before this Board and ask for something else.

MR. VINCE WARDEN: Well, Mr. Saxberg, I think that's where I think you have a bit of a misunderstanding that this -- the profit you call it, going to Centra, is really to the benefit of ratepayers. That is this is not some company that's taking money out of Centra. This is money that's staying in Centra for the benefit of ratepayers. It's their money, it's their retained earnings.

We're only looking to get to a reasonable debt equity ratio of 75:25 over a period of time, whether we get there quicker or -- or in the judgment of this Board if they want to slow down that's fine too. But it's -- it's Centra ratepayers money.

It's not something we're -- that another company located somewhere else over the Province is going to take money out and take it home and spend it elsewhere. It's going to be spent right here. It's going to reduce the financing cost. By having retained earnings we're going to reduce the financing costs that Centra would otherwise incur.

So, there's no big bad corporation here that's taking this money. It is staying right in Centra Gas for the benefit of those ratepayers.

(BRIEF PAUSE)

MR. KRIS SAXBERG: The original Application indicated that your goal was to get to the 75:25 debt equity ratio by 2009/10. And I'm getting that from page -- from Tab 3 of the Application.

Is that the timeframe?

MR. VINCE WARDEN: We're just finding

that reference, Mr. Saxberg.

(BRIEF PAUSE)

MR. VINCE WARDEN: Yes, Mr. Saxberg, Tab 3, page 5 of 7 starting at line 9 on that page, we do reference the fact that with the proposed rate increase of 2 1/2 percent, effective February 1st, 2005 and 2.5 percent effective May the 1st, 2006, together with projected rate increases of 1 percent each second year thereafter, Centra's debt equity ratio is projected to improve from 84:16 at March 31st, 2005 to 75:25 at 2010.

I should point out that was based on the assumptions we had at that time. The $3 million change that we referenced on the first day of the proceedings, I believe it was, the first or second day, would mean that we would get there quicker than 2009/10.

MR. KRIS SAXBERG: Thank you for that, Mr. Warden, and that's where I was going. Could you undertake to tell us exactly when the 75:25 debt equity ratio will be achieved under the current proposal?

MR. VINCE WARDEN: Certainly.

MR. KRIS SAXBERG: And could you also do me a favour and include the 12 million as the appropriate corporate allocation going back to 2002 and drawing it forward as a second calculation?

So that if the corporate allocation was 12 million beginning in 2002/03 and carrying forward, how long would we take to achieve the 75:25 debt equity ratio?

MR. VINCE WARDEN: Well, I wonder if you could do me a favour, Mr. Saxberg, and if you'll allow me, if we're going to go retroactive, to take it all the way back to the acquisition date of Centra Gas.

And if we're going to impute that number, we may as well do it right back to the acquisition date?

MR. KRIS SAXBERG: And I don't mind seeing that type of calculation as well. I think that would be helpful.

If you could, in that undertaking, show that -- or demonstrate what amount of costs that were once included in the Centra accounts for accounting purposes relating to the acquisition are removed during those years so that we can see exactly how things originally were stated financially from 1999 to 2002 and then how they were adjusted?

MR. VINCE WARDEN: We are reconstructing the past, Mr. Saxberg, and we'll attempt to do that as best we can.

MR. KRIS SAXBERG: Thank you, Mr. Warden.

--- UNDERTAKING NO. 22: Centra to provide CAC/MSOS information as to when the 75:25 debt equity ratio will be achieved under the current proposal. Include the 12 million as the appropriate corporate allocation going back to acquisition and drawing it forward as a second calculation. Demonstrate what amount of costs that were once included in the Centra accounts for accounting purposes, relating to the acquisition, are removed during those years.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Now, the corporate strategy of Manitoba Hydro, which is Tab 1 of Attachment -- Attachment 3 to the Application, indicates that Manitoba Hydro's strategy and target is to get to a 75:25 debt equity ratio by 2012; and that's on page 7.

Can you confirm that?

MR. VINCE WARDEN: Without referencing

that tab I can confirm that the corporate target is to be achieved by 2012, yes.

MR. KRIS SAXBERG: And included in my book of documents at Tab 1, the very last page, is integrated financial forecast -- second last page, integrated financial forecast of the electric operations.

What year is this IFF for? Is it the most recent?

MR. VINCE WARDEN: Mr. Saxberg, this is your Book of Documents and you can see on -- at the top of what is referenced at the bottom at page 29 that is MH-04. So that would have been prepared in the fall of 2004, November 2004.

However, if you flip the page, you can see that's IFF-03 to that would -- that document referenced as page 39 in your Book of Documents would have been prepared in the fall of 2003.

So, I just wanted to point out that those are, even though they're back to back, they're -- they're prepared in different -- different years.

MR. KRIS SAXBERG: Thank you for that, Mr. Warden. So I'm looking at the document that was prepared in the fall of 2004 relating to the electric operation and it indicates that Manitoba Hydro, the electric side, is not going to get to a 75:25 debt equity ratio until 2014.

Do you see that?

MR. VINCE WARDEN: That is what the forecast shows as at November of 2004, yes.

MR. KRIS SAXBERG: So, I -- I just want to pull these elements together, and -- and why is it that the gas side needs to get to a 75:25 debt equity ratio by -- sooner than 2010 and yet the electric side is on a more leisurely pace to achieve that financial target?

MR. VINCE WARDEN: Well, the -- at the time the gas forecast, the 2003 forecast was put together we didn't have approved financial targets for the gas company. And, as you pointed out in the excerpt we referenced earlier, we were just looking for some contribution towards -- towards the retained earnings of -- of corporate.

If you look at your -- your document, the last page in Tab 1, you can see that the net income that was being projected there was relatively modest. In fact, there was a net loss projected for '03/'04 and '04/'05 and then gradually building up some retained earnings.

So -- and that was with very modest rate increases throughout that period of time. We had a forecast of 2 percent rate increase in '05/'06 and then only 1 percent in '07/'08. So, you can see the rate increases were very, very modest.

And only at that point we were looking for some kind of contribution towards retained earnings, so without a specific financial target.

MR. KRIS SAXBERG: Is it fair to gas ratepayers for them to have to more aggressively achieve the debt equity ratio than -- than it is for the electric ratepayers?

MR. VINCE WARDEN: No. There -- as we indicated in our application 2009/10, with those very modest rate increases, would have the level of 75:25 achieved for gas ratepayers; 2001/12 for electricity ratepayers. And, obviously, with the 2 1/2 percent rate increase projections that we have on MH-04-1, that financial projection prepared in the fall 2004, we don't make it.

So even with 2 1/2 percent rate increases each and every year for electric ratepayers, we would not achieve our target of 75:25 by 2011/12, unless, of course, as we know, the -- the fortunes of the electricity ratepayers very much rise and fall with water conditions. So this -- this is without getting too much into the electricity side of the business, this does assume average water flows in that interim period of time.

Much to the distress of the farmers today, we have much better than average water conditions and if that holds, we will exceed our financial forecast on electricity operations this year.

So, the targets are just that, they're -- they're something that we strive for over time. It's something that I'm sure not only the Manitoba Hydro Board but this Board takes into account when they're considering the conditions of the day and what rate increases should be awarded to the respective utilities.

MR. KRIS SAXBERG: Mr. Warden, at the last Hearing you said that the subs of Manitoba Hydro don't have specific financial targets and as long as they're not negatively impacting the financial targets of the parent company, you have no concern.

Is it still the case that other subs like CHES, which has a new acronym now I believe, but is it still the case that they don't have financial targets other than having to positively contribute towards the parent company's bottom line?

MR. VINCE WARDEN: That's correct. But realize the other subs are -- are very small in comparison to electric gas; the main lines of business of the Corporation. So, the other subs are mainly there to essentially break even and not go into a deficit position.

MR. KRIS SAXBERG: One (1) of the measures that Manitoba Hydro uses to determine appropriate amount of retained earnings is interest coverage, correct?

MR. VINCE WARDEN: Not to determine an appropriate amount of retained earnings at any given time, it's -- interest coverage is more to measure the effectiveness of that current year's net income. So that -- it -- retained earnings is best measured with the debt equity ratio.

MR. KRIS SAXBERG: And the target interest coverage is one point one (1.1), correct?

MR. VINCE WARDEN: Well, again, that's been updated since -- the document you're holding in your hand, Mr. Saxberg. The current interest coverage target is one point two (1.2).

MR. KRIS SAXBERG: You'll agree that the Application before this Board though, results in retained earnings in each of the test years, that is -- that provides for a much higher interest coverage than the one point two (1.2), correct?

(BRIEF PAUSE)

MR. VINCE WARDEN: Sorry, Mr. Saxberg, do you have a reference there?
MR. KRIS SAXBERG: Well, I'm -- I'm looking at Schedule 3.0.0, and I'm again adding back the $3 million to the net income line.

(BRIEF PAUSE)

MR. VINCE WARDEN: Well, rather than do a quick calculation, perhaps we should give you what the interest cover ratio works out to in each of those -- each of the test years.
MR. KRIS SAXBERG: Thank you for that. And could you also, while you're at it, do the capital financing ratio?
MR. VINCE WARDEN: Yes.

--- UNDERTAKING NO. 23: Centra to provide CAC/MSOS with what the interest cover ratio works out to in each of the test years as well as the capital financing ratio.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Now, one (1) reason to have -- one (1) very important reason to have retained earnings is to provide for safety against business risks, correct?

(BRIEF PAUSE)

MR. VINCE WARDEN: Safety against business risk. All right. I'll accept that, yes.

MR. KRIS SAXBERG: And the document which I've included at Tab 2 of my materials, is I'm sure one (1) that you're familiar with?

(BRIEF PAUSE)

MR. VINCE WARDEN: Yes, Mr. Saxberg, actually this is the Corporate Risk Management Report, which we have filed as an undertaking. We've updated the -- the filing of this.

This is, as you can see on the bottom of this document, that's May of 2003. I believe the updated corporate risk management has June of 2004, which has been filed with these proceedings.

MR. KRIS SAXBERG: And again, the main

reason for a build up of equity under the cost of service approach, is to create a financial cushion to absorb in the case of adverse events?

MR. VINCE WARDEN: Yes.

MR. KRIS SAXBERG: And on the electric side of the business, the largest potential adverse effect is drought; is that fair?

(BRIEF PAUSE)

MR. VINCE WARDEN: It's certainly one (1) of the biggest, loss of export markets, a major incident on our system could be larger but with the ones we're familiar with, the ones that we know happen on a regular basis, about once every decade, drought is -- is certainly one (1) of the big risks.

But, not -- I wouldn't say it's the biggest.

MR. KRIS SAXBERG: If I could just get you to turn to page 3 of Tab 2 of my Book of Documents where I see a preliminary ranking of corporate risks as illustrated on the corporate risk map.

The first bullet on this page says:

"Drought is currently the only high consequence, high likelihood occurrence risk."

Do you agree with that?

MR. VINCE WARDEN: That's correct, yes.

MR. KRIS SAXBERG: And you'll agree that drought is -- is not a risk at all for gas ratepayers?

MR. VINCE WARDEN: Sure.

MR. KRIS SAXBERG: And the export market and what's going on there is also something that isn't a risk to Centra Gas?

MR. VINCE WARDEN: Not directly. It may in some indirect way have an impact on gas energy consumers in the province, but -- but not in a direct way.

MR. KRIS SAXBERG: So, the risk on the Centra side of the business that you're concerned mostly about is some catastrophic infrastructure incident?

MR. VINCE WARDEN: Yes, I agree with that.

MR. KRIS SAXBERG: Has anything like that happened in the history of Centra Gas?

MR. VINCE WARDEN: Well, there was a fairly major explosion on Portage Avenue some years back that caused significant damage; fortunately no loss of life at that time. But in other jurisdictions there certainly have been -- have been incidents more serious than that one.

MR. KRIS SAXBERG: Would the financial consequences of that accident be covered by insurance?

MR. VINCE WARDEN: Yes, we -- we do have insurance up to a certain maximum and that particular one was -- was primarily covered by insurance.

MR. KRIS SAXBERG: I think I could move on if you'd agree with me that the -- there are greater business risks on the electric side of the business than there are on the gas side because you're involved in generation primarily?

MR. VINCE WARDEN: The unknown is always, of course, what causes me to -- would cause me to pause there. These days who knows what's out there that might happen that, shudder to think, put's ratepayers or customers of Centra Gas without service.

We're doing everything possible, of course, to make sure that doesn't happen. But that's the risk we face in this world and if, you know, we were to lose supply in the middle of winter, is it more serious to electricity versus gas ratepayers?

Well, I think we can all be the judge of that.

MR. KRIS SAXBERG: But, having a financial cushion in the form of retained earnings wouldn't, in any way, help you to avoid losing supply?

MR. VINCE WARDEN: But, retained earnings are there for the financial risk and there is the hard reality is that if there was a major incident it has to be funded somehow.

MR. KRIS SAXBERG: But with respect to supply of gas, that's a risk that can be mitigated by having in place an appropriate portfolio, gas supply portfolio?

MR. VINCE WARDEN: Well, we can't duplicate everything, Mr. Saxberg.

MR. DARREN RAINKIE: Mr. Saxberg, are you suggesting that if there isn't a pipeline coming from Western Canada that we can somehow physically move the gas from Michigan storage back to Manitoba because that isn't the case.

MR. KRIS SAXBERG: And I hear what you're saying, but if there was a -- an incident involving transmission pipeline or -- and that that would impact your ability to supply customers with gas; that's what you're saying.

MR. DARREN RAINKIE: That's correct. No gas, no revenue.

MR. KRIS SAXBERG: But in terms of there being a limited supply or one of your -- or your supplier of gas, Nexen, not being able to supply you with gas, the fact that you have significant retained earnings wouldn't do anything to mitigate that circumstances?

MR. VINCE WARDEN: That's really not a circumstance we're concerned about.

(BRIEF PAUSE)

MR. KRIS SAXBERG: So, it's fair to say that the risks on the electric side are different than the risks on the gas side?

MR. VINCE WARDEN: Certainly different.

MR. KRIS SAXBERG: And yet that to you doesn't translate to a requirement to have a different debt equity ratio?

MR. VINCE WARDEN: No.

MR. KRIS SAXBERG: Mr. Rainkie, are you familiar with the stand-alone principle?

MR. DARREN RAINKIE: In what context, Mr. Saxberg?

MR. KRIS SAXBERG: In -- in the context of -- of determining interaria (phonetic) debt equity ratios.

MR. DARREN RAINKIE: Yes. I think I understand what you're talking about.

MR. KRIS SAXBERG: And do I have it right that the stand-alone principle provides those who use the services and facilities of a utility should pay rates that reflect the costs of providing those services and facilities independent of the other activities of the utility's owners?

MR. DARREN RAINKIE: I think generally that's the application of the rate base rate of return methodology, but that's drawing, as I said the other day, a box around Centra Gas Manitoba Inc., which is just simply a legal shell.

The fact of the matter is the integrations of gas and -- of Centra and Manitoba Hydro are integrated and have been integrated for some time. So, you know, we can talk about the regulatory construct and how it's been applied in -- in the past but in getting -- I want to take you back to the realities of the world that we have right now, and it certainly is an integrated utility.

(BRIEF PAUSE)

MR. KRIS SAXBERG: Mr. Rainkie, you'll agree that West Coast carried debt in order to fund the approximate level of 40 percent equity in Centra Gas?

MR. DARREN RAINKIE: I don't know that

for sure. I -- I assume they -- they did. But in that point -- at that point Centra was a stand-alone company; it had its own debt, it had its own capital structure. So, I think the -- whatever happened at the holding company level, if you will, was irrelevant. It's not the same situation as we have here.

MR. KRIS SAXBERG: So, the primary reason why you're saying that -- that you should look to the owner in determining a debt equity ratio in this case is that Centra is integrated, fully integrated into Manitoba Hydro?

MR. DARREN RAINKIE: Yes. The provincial debt guarantee come from the ownership of Manitoba Hydro. So, I'm saying that you can't have the benefits of that ownership without the costs; it's only fair, Mr. Saxberg.

MR. KRIS SAXBERG: So, Centra Gas, in your view, isn't a stand-alone entity, it's -- it's intricately caught up in the financial performance of the parent company?

MR. VINCE WARDEN: We'd rather say the financial structure of the parent company, rather than the financial performance of the parent company, Mr. Saxberg.

MR. KRIS SAXBERG: So, why does it matter then that Centra would have to have its own independent debt equity ratio if it isn't stand-alone?

Why -- why shouldn't we just be doing as you indicated in the prior Hearing, and that is providing a positive contribution to the retained earnings of the parent company?

MR. VINCE WARDEN: As a matter of fact, we were requested by this Board to look at specific financial targets to -- for Centra Gas, and that's what we've done. It's only prudent that those financial targets mirror -- and it was always the intent of Manitoba Hydro that they would mirror, to some extent, the financial targets of -- of the parent.

(BRIEF PAUSE)

MR. KRIS SAXBERG: Is there a precedent at all that you're relying on with respect to the treatment of share capital to determine debt/equity ratios in this case?

MR. VINCE WARDEN: Mr. Saxberg, I -- I indicated there is no precedent for what occurred when Manitoba Hydro acquired Centra Gas. That was a first time event in corporate history that we could find, that a Crown owned utility acquired an investor owned utility of any significance.

MR. KRIS SAXBERG: I want to turn now briefly to the topic of synergies. Is Centra Gas/Manitoba Hydro continuing to attempt to achieve greater synergies?

MR. VINCE WARDEN: Yes, we're always striving to achieve every last dollar of synergy that we can achieve, so, yes, we are.

MR. KRIS SAXBERG: And your current estimate though, is that there are -- there has been achieved, on a cumulative basis, $16 million worth of synergies?

MR. VINCE WARDEN: Yes, that's the number as at -- that we derived as at March 31st, 2005.

MR. KRIS SAXBERG: And there's no evidence in this Proceeding, of other avenues to achieve synergies?

MR. VINCE WARDEN: Well, I think we talked about -- I believe we talked about the implementation of Banner, that is the column billing system in -- starting in November of 2005, for which there will be further synergies.

MR. KRIS SAXBERG: On the gas side or on the electric side?

MR. VINCE WARDEN: Both gas and electric.

MR. KRIS SAXBERG: Is that something that you've undertaken to quantify?

MR. VINCE WARDEN: I don't believe we've undertaken to quantify. We've talked about, in the past at least, we've talked about synergy savings in the range of $1 million in total.

MR. KRIS SAXBERG: And in the past, that estimate of synergy savings, flowing from the one (1) bill initiative, was included in the $16 million calculation?

MR. VINCE WARDEN: Do you have a reference for that, Mr. Saxberg?

(BRIEF PAUSE)

THE CHAIRPERSON: Mr. Warden, weren't the synergies that were developed related to actual accomplishment, rather than projected future benefits?

MR. VINCE WARDEN: Yes, the 16 million was actually achieved as at March 31st, 2005. So whatever we achieve beyond that with the one (1) bill, will be incremental.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Okay. And can you undertake then to provide us with the amount of additional synergies that you expect, as a result of the one (1) bill becoming operational?

MR. VINCE WARDEN: Yes, we can do that.

--- UNDERTAKING NO. 24: Centra to provide CAC/MSOS the amount of additional synergies that are expected as a result of the one (1) bill becoming operational.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Now, at the Integration Hearing, which led to Board Order 208/02, Centra presented evidence of the synergies achieved, correct?

MR. WILLIE DERKSEN: Yes, sir, we did.

MR. KRIS SAXBERG: And the Board at that time disallowed some of those synergies, did it not?

MR. WILLIE DERKSEN: I think disallowed is -- it's a different context. They viewed that for the purposes of rate setting we shouldn't include certain cost savings that had been achieved. It's hard to disallow the fact that cost reductions occur.

MR. KRIS SAXBERG: So is it fair to say, whereas Centra was saying to the Board, we've achieved

$15.3 million of synergies, the Board said it is only going to acknowledge ten point three (10.3) worth of synergies?

MR. WILLIE DERKSEN: That was our interpretation of the Order, yes.

MR. KRIS SAXBERG: So, what has happened since then, so with respect to the achievement of those -- those disallowed synergies?

MR. WILLIE DERKSEN: Are you asking me for specific details of -- of what's transpired in the operations?

MR. KRIS SAXBERG: If -- if you turn to Tab 10 of my book of documents, second page in there's a listing of the three (3) types of synergies that weren't allowed by the Board; do you see that?

MR. WILLIE DERKSEN: Yes, I have that.

MR. KRIS SAXBERG: So I guess the question becomes, did Manitoba Hydro achieve ERP savings related to the sixteen (16) vacancies in the amount of $1 million, subsequent to the Board's decision in Board Order 208/02?

MR. WILLIE DERKSEN: I mean, certainly Manitoba Hydro achieved those savings but I'm not sure what your question is, should they be allowed or not allowed, or did they achieve them?

MR. KRIS SAXBERG: Well, there were -- there was a forecast of savings associated with fifty-seven (57) positions which hadn't been implemented at the time of Board Order 208; correct?

MR. WILLIE DERKSEN: Yes, that's correct.

MR. KRIS SAXBERG: Did the projected integration action of fifty-seven (57) positions becoming no longer required; did that integration action occur?

MR. WILLIE DERKSEN: There were a number of underlying integration actions that have occurred subsequent to that period of time. Some of them are as planned and some of them new opportunities.

We have not intended -- or we have not tracked them in absolute detail but in the 16 million there are some general savings that are not specific; if that's what you're referring to.

MR. KRIS SAXBERG: The $16 million estimate of synergies achieved comes from the $15.3 million figure which is then inflated to current year conditions?

MR. WILLIE DERKSEN: Yes, that's correct.

MR. KRIS SAXBERG: So to the extent that the disallowed synergies were not achieved after Board Order 208, the $16 million figure may be too high?

MR. WILLIE DERKSEN: Too high for what?

MR. KRIS SAXBERG: Too high of an estimate of the actual synergies achieved?

MR. WILLIE DERKSEN: Well, I think, you know, our position is and what's actually happened is that the budgets have been reduced by this $16 million so that's a matter of fact.

What has occurred is a number of underlying actions since this point in time. And so if the Board were to say, unless you have specific examples to support the $16 million, the specific new actions and they said any general ones were not eligible for this statement, then the $16 million would be over-stated.

MR. KRIS SAXBERG: Now, when you say that budgets are adjusted so that synergies, whether or not they've been achieved by integration action, are incorporated into the -- into the calculations; what happens if the performance is such that you go over budget, you haven't then achieved the synergies?

MR. WILLIE DERKSEN: Well, there may be other reasons, Mr. Saxberg. In order to track these things in an absolute sense, what are the synergy savings, we'd have to second guess every one of our actions that we'd taken in every department that was related.

So, if, for example, in my position and I have a department of about fifteen (15) or twenty (20) persons and if I replaced one (1) of those persons now I'd have to, given that that's the right thing to do, I'd have to think, going back to a pre-acquisition time to say, Okay, what would I have done under Manitoba Hydro and what would I have done under Centra and would I not have replaced that person, or what were those actions.

And so you can see that getting down to that level of detail and trying to track them six (6) years from now is just something that is very difficult to do.

MR. KRIS SAXBERG: And I appreciate that. But for the year 2003/04 the forecasted budget was the costs in Centra were going to be 49.3 million, correct?

MR. WILLIE DERKSEN: Yes, that's what we forecasted.

MR. KRIS SAXBERG: And so within that forecasted budget you're saying that the -- you would have included synergies in the amount of -- of Centra's deemed portion of synergies?

MR. WILLIE DERKSEN: There were certainly synergies in that forty-nine point three (49.3), yes.

MR. KRIS SAXBERG: But, as the universe unfolded, you didn't achieve costs of forty-nine point three (49.3), did you?

MR. WILLIE DERKSEN: That's correct.

MR. KRIS SAXBERG: And so to the extent that you had reduced the budgets to show synergies, synergies weren't achieved because you didn't -- you didn't meet your budget, you exceeded it by more than $3 million?

MR. WILLIE DERKSEN: Well, they weren't achieved in Centra, that's right. They manifested themselves in Manitoba Hydro instead of in Centra. But the amount of synergies that we projected I believe were achieved.

(BRIEF PAUSE)

MR. KRIS SAXBERG: Is the calculation of synergies achieved going to be affected as a result of the construction of the new office building?

MR. WILLIE DERKSEN: One (1) of the original integration plans was a common premises. And so the new office building will result in that underlying action of -- of achieving common premises.

If we are still required to do synergy saving calculations at that point in time, it would be appropriate to include savings related to the -- to the office building, yes.

MR. KRIS SAXBERG: I'm more concerned about the costs associated with the office building construction. Is it your view that if West -- West Coast still owned Centra Gas, that they would have built an office building downtown?

MR. WILLIE DERKSEN: Now, that's very difficult for me to say what West Coast would or wouldn't have done. I -- I really can't answer that question.

MR. KRIS SAXBERG: Is it --

MR. WILLIE DERKSEN: If you -- you recall though, there was some land purchased at Sutherland Avenue because Centra understood that consolidating its operations in one (1) location would be beneficial to -- to its own operations as well.

MR. KRIS SAXBERG: Is it Centra's intention to collect in rates from gas ratepayers a contribution to pay for the construction of the office building?

MR. VINCE WARDEN: Mr. Saxberg, Centra will pay its fair share of all costs incurred by the Corporation. The determination of whether or not it was a good thing to build an office building downtown was something that was made by the parent company. And bringing employees together will certainly be a benefit.

We have, in the overall justification for the building, looked at what some of those savings will be. And those savings, by having people working in a common facility, will be shared. So Centra ratepayers, in answer -- answer to your question, Centra ratepayers will share in the benefits of being in one (1) location.

MR. KRIS SAXBERG: But as you sit here today you can't tell us that those benefits are greater than the incremental costs associated with the construction of the office building?

MR. VINCE WARDEN: There is an assumption of productivity savings that go into the cost analysis for the new building. And those productivity savings indicate that there will be benefits to all ratepayers.

MR. KRIS SAXBERG: The -- the cost of the building, is it fair to say, will flow through the allocation system?

MR. VINCE WARDEN: Yes. There will be a space allocation to the -- both the gas and electricity ratepayers, yes.

(BRIEF PAUSE)

MR. KRIS SAXBERG: Do you agree that it's important that the measure of synergies in Centra Gas not be overstated?

(BRIEF PAUSE)

MR. VINCE WARDEN: Well, as Mr. Derksen explained, the synergies were -- the estimate of synergies in Centra were part of what determined what the operating maintenance administrative costs would be in Centra.

We have not, as I indicated early on, have -- have not been achieving those synergies within Centra as quickly as we originally forecast. And that's the reason why we've reduced the corporate allocation by $3 million, and transferred that in effect -- in effect transferred that portion of that allocation over to electricity ratepayers.

MR. KRIS SAXBERG: And in this Application you want Centra ratepayers to pay $12 million, in order to get $7 million worth of synergy benefits?

MR. VINCE WARDEN: No, that's not a correct interpretation at all, Mr. Saxberg. We're -- we're looking at -- I refer you back to our rebuttal evidence, the -- the total benefit to -- to Centra ratepayers in '04/'05. Sorry, that was '05/'06.

Page 14 of our rebuttal evidence, the minimum benefit that Centra ratepayers have -- have achieved at that point is with including at that point, the corporate allocation of 15 million, the minimum benefit is -- is nine (9).

(BRIEF PAUSE)

MR. KRIS SAXBERG: What is the number of quantifiable financial benefits on an item by item basis, in Centra Gas?

I know you've said synergies are 7 million. What are the other quantifiable financial benefits?

MR. WILLIE DERKSEN: Well, the other benefits include the reduction in the income tax that otherwise would have been paid, and a -- an amount of return on equity that isn't going to out of Province shareholders.

MR. KRIS SAXBERG: And those are the three (3) items, and I think we agreed that the taxes, foregone taxes are approximately $4 million, correct?

MR. WILLIE DERKSEN: For '05/'06, that's correct.

MR. KRIS SAXBERG: And for 2006/07 test year, you're asking for a net income of $14 million, which is higher than the return on equity would have been under rate base rate of return.

MR. WILLIE DERKSEN: Well, I don't know that we know what it would have been under rate base rate of return, because the schedule that we've -- we haven't prepared that schedule yet, but we were discussing, you know, what equity ratio would West Coast have had.

What rate of return would it have applied for. And what would -- what would be the other changes in the operation since 1999, that would have occurred. So, we don't have -- we can't solidly say that it would have been only fourteen (14).

MR. KRIS SAXBERG: How did we go from asking for a return on equity of approximately 14/15 million, plus $7 million in synergy transfers as being enough to fund the acquisition and produce a comfortable contribution to retained earnings, to what we have before us today, which is a return of approximately 14 million, whether it be net income or as return on equity, along with a $12 million synergy transfer, along with a additional 3 million in net income?

MR. VINCE WARDEN: Mr. Saxberg, rather than be selective as you're doing, I think we do have to take you back to Schedule 3.0.0, so we can compare side by side, what were -- we are asking for in this -- in this Application, compared to what it would have been under rate base rate of return.

So I keep coming back to the fact that it is, no matter how you dissect the numbers, it is lower. Our Application is lower than it would have been under the alternative of rate base rate of return.

MR. KRIS SAXBERG: If the corporate allocation is removed from the calculation under rate base rate of return, you'll agree that the revenue requirement for rate base rate of return is lower than it is under your cost of service submission?

MR. VINCE WARDEN: But you can't do that though, of course, because you'd have to adjust all the other items correspondingly. So that would be an incorrect calculation.

MR. KRIS SAXBERG: Why do you have to adjust the other items if you're removing the corporate allocation?

MR. VINCE WARDEN: Well, I think you -- I take you back to our rebuttal evidence, page 14 of our rebuttal evidence. And just looking at one (1) item, for example, in '05/'06 the operating maintenance and administration number that we've held constant for both cost of service and rate base rate of return in Schedule 3.0.0 is, in fact, under the absent acquisition scenario is $62.2 million.

So that's the changes that would have to be made to make those -- if we were going to remove the corporate allocation line, we'd have to make those adjustments as well.

MR. KRIS SAXBERG: The comparison that I'm trying to make is between Centra's Application under rate base rate of return versus Centra's Application under cost of service, rather than what would have happened absent acquisition?

MR. VINCE WARDEN: Good, then I refer you to Schedule 3.0.0; that's your best source of information for making that comparison.

MR. KRIS SAXBERG: And if I could draw your attention to PUB-131; were you asked to remove the corporate allocation from rate base rate of return?

I have -- I've copied that IR response and I think it might be helpful for it to be on the record as a separate exhibit, so I'll hand it out.

--- EXHIBIT NO. CAC/MSOS-7: Information Request PUB-131.

THE CHAIRPERSON: Mr. Saxberg, would this be a good point to have a break?

MR. KRIS SAXBERG: Yes.

THE CHAIRPERSON: Okay, thank you, sir. We'll have our break now. And this would be Exhibit Number 7?

MR. KRIS SAXBERG: Yes, thank you, sir.

--- Upon recessing at 10:26 a.m.
--- Upon resuming at 10:54 a.m.

THE CHAIRPERSON: Ms. Murphy, you have a couple more undertakings to supply?

MS. MARLA MURPHY: Yes, I do, Mr. Chairman. Thank you. We have filed with the Board Secretary, and I believe they've been circulated throughout the room, the response to Undertaking Number 15, which was at transcript page 1018, which was the statistics on the number of line hits where customers failed to call before digging.

And I believe that should be Centra Exhibit Number 22.

THE CHAIRPERSON: Thank you.

--- EXHIBIT NO. CENTRA-22: Response to Undertaking Number 15, at transcript page 1018, which was the statistics on the number of

line hits where customers
failed to call before
digging.

MS. MARLA MURPHY: We also have Undertaking Number 22 from transcript page 1225, which was Mr. Rainkie's recalculation of the 2005/06 no-harm calculation assuming a 38 percent equity ratio. And I believe that should be Centra Exhibit Number 23.

--- EXHIBIT NO. CENTRA-23: Response to undertaking Number 22, from transcript page 1225, which was Mr. Rainkie's recalculation of the 2005/06 no-harm calculation assuming a 38 percent equity ratio.

MS. MARLA MURPHY: We also have the response to Undertaking Number 23, taken from transcript page 1226, which was the calculation comparing Centra's application for 2006/07 to the absent acquisition scenario or the no-harm calculation, as it's been referred to.

And I might also indicate that Mr. Derksen is prepared to speak to an undertaking that was taken at page 1131 of the transcript. I have that as Exhibit Centra -- or, sorry, Undertaking Number 20, which is to advise if Centra takes issue with the calculation made by Mr. Matwichuk on page 11 of his evidence. And Mr. Derksen is prepared to speak to that now if you'd like.

THE CHAIRPERSON: Okay. Well, with respect to Undertaking Number 23, I think that's number 24; correct?

MS. MARLA MURPHY: Thank you. Yes. I'm sorry.

--- EXHIBIT NO. CENTRA-24: Response to Undertaking Number 23, from transcript page 1226, which was the calculation comparing Centra's application for 2006/07 to the absent acquisition scenario or the no-harm calculation.

THE CHAIRPERSON: Mr. Derksen...?

MR. WILLIE DERKSEN: Yes. Thank you. I was asked to indicate whether we agree with the position taken by Mr. Matwichuk with respect to the calculation of eliminating the premium, which is contained on page 11 of his evidence.

And, although I don't accept the premiss, because since Centra received benefits associated with the acquisition and the write-up, they should share in the costs. I do accept that the calculation is a reasonable one given the way that Mr. Matwichuk looks at it.

MS. MARLA MURPHY: I might also indicate, Mr. Chairman, that in filing Undertaking Number 23 Mr. Warden had a comment to make with respect of it. And perhaps he could speak to that now, so that it's on the record along with the filing.

THE CHAIRPERSON: Good. Mr. Warden...?

MR. VINCE WARDEN: Yes, thank you, Mr. Chairman. The Undertaking Number 23, except number 24, does provide the comparison to Centra's filing with the absent acquisition.

And you can see with that comparison there's -- there's virtually no difference between the two (2). And I did want to point out however, that the -- the reason that occurs is that with the $3 million change we made, the same revenue requirement -- because we're not changing our Application, the same revenue requirement results in higher net income than we -- we really had envisioned with our Application, instead of the fourteen million four forty-nine (14,449,000) that's in the test year.

Our Application is for eleven (11) -- eleven three-o-eight (11,308,000) sorry. So, that $3 million perhaps somewhat misrepresents that comparison.

That does -- and we will be filing this as an undertaking we took this morning, does result because of the change in the corporate allocation number down, that $3 million, in each and every year, starting in 2004/05, a difference of $9 million, or the actual in two (2) test years.

It does result in a -- in a higher debt or at least a better debt equity ratio than we have in the consolidated operations of Manitoba Hydro. Again, we will be filing this later, but it looks like we end up with something like 80:20 in 2006/07, because of that $12 million shift from electric operations to gas operations, to the benefit of gas ratepayers.

So, the -- the retained earnings do end up being $9 million higher than we had proposed with our original Application.

I did want to point that out because it looks a little -- a little misleading perhaps, with the undertaking that was filed in -- in Exhibit number 24.

THE CHAIRPERSON: Thank you, Mr. Warden.
Mr. Saxberg...?

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Just to follow-up on that then, Mr. Warden.

Is that -- is Centra prepared to withdraw the request for the additional $3 million in -- in net income and for the '06/'07 test year and go back to the original proposal of an $11 million net income?

MR. VINCE WARDEN: Well, I think the Board should be aware of the implications of us doing that. We indicated that our -- that our Application, the way we had filed our Application was for an approximately 2 1/2 percent rate increase in each of those years to yield additional revenue.

We weren't really targeting a bottom line net income for those years, so the additional revenue that was requested in each of those years is the same as our Application.

But that additional revenue, because of the circumstance I just described, does result in higher net income than we would otherwise have received absent that change in the allocation.

MR. KRIS SAXBERG: You'd agree that what

we see in Centra Exhibit 24 then, is the revenue requirement requested, being virtually identical to the situation absent acquisition?

MR. VINCE WARDEN: Yes, I -- I just pointed that out. I do want to re-emphasize though, that those -- the net income that's indicated on here goes directly into retained earnings for the benefit of Centra ratepayers. It does not leave the Province; it's Centra ratepayers money, so to speak.

MR. KRIS SAXBERG: But, you'd agree that Centra 24 shows that we're peri -- perilously close to Centra ratepayers having been harmed as a result of the transaction then?

MR. VINCE WARDEN: Mr. Saxberg, I don't like using those words, 'perilously close to harm'. There's no harm to -- to Centra ratepayers.

Again, this is their money. If this Board chooses, that retained earnings should be built up more slowly, the debt equity ratio should be built up more slowly; that's certainly the prerogative of the Board and in my position I would, as long as the debt equity ratio reaches that 75:25 at some point, I'm happy.

MR. KRIS SAXBERG: In the proceeding leading to Board Order 146/99, the acquisition hearing, Hydro testified that rates for both gas and electricity customers would be lower than they would otherwise be if the transaction was not completed; do you agree with that?

MR. VINCE WARDEN: Oh, absolutely, I agree with that and I still say that.

MR. KRIS SAXBERG: But Centra Exhibit 24 shows that they're not lower for the 2006/07 test year. Rates won't be lower than they would be as a result of the transaction; in fact they're the same?

MR. VINCE WARDEN: Well, remember we're looking at one (1) test year. We would have to look at what would have transpired in those intervening years. Remember, we have only had a -- before the 2.5 percent interim rate increase granted February 1st, 2005, we've only had a .4 percent rate increase to Centra customers.

And we can all speculate what might have happened under previous ownership, but I think we're fairly safe in saying that rates would have been higher than -- than that.

MR. KRIS SAXBERG: I'm glad you used that word 'speculate' because the baseline calculation, the absent acquisition calculation is riddled with speculation as to what West Coast would have done, correct?

MR. VINCE WARDEN: Well, we've certainly

admitted there's assumptions. That's all we can do. We can make the best assumptions that we can and I guess that's your job to challenge those assumptions.

MR. KRIS SAXBERG: But you'll agree with me that there is a margin of error associated with the calculation, the absent acquisition calculation?

MR. VINCE WARDEN: Well, we've -- we've chosen purposely to err on the size -- side of conservatism; that is we've stated repeatedly that we think that the absent acquisition probably is -- is understated in terms of the costs that would have been incurred under those circumstances.

MR. DARREN RAINKIE: I would also indicate, Mr. Saxberg, that when I look at the application and I take the two (2) test years into consideration, we're $9.2 million lower than what otherwise would have happened. And I think that's a fairly good cushion on about $142 million non-gas costs.

MR. KRIS SAXBERG: But, that's only going to be the case for nine (9) months?

MR. DARREN RAINKIE: For nine (9) months, sir?

MR. KRIS SAXBERG: Well, until May 1st, 2006?

MR. DARREN RAINKIE: But, sir, as Mr.

Warden just indicated, if you go back to 1999 I think you can assume that the calculation of 2005/06 is probably indicative. So if you take five (5) or six (6) years at $9 million, I think we've -- you know, we got -- we're $45 million to the good.

I mean, you can parse one (1) test year, if you want, but I'm going to look at this whole Application as a total and that's going to be the basis of my opinion.

MR. KRIS SAXBERG: The margin of error, you'll agree though, is greater than two hundred and thirty-two thousand dollars ($232,000)?

MR. VINCE WARDEN: Again, we're being conservative though, so the margin of error, to use your words is -- that number would be greater benefit to Centra ratepayers than we've indicated here.

MR. KRIS SAXBERG: On -- getting back to the document that we marked as an exhibit prior to the recess Centra -- or, sorry, CAC Exhibit Number 7, have you had a chance to review that answer to interrogatory during the break?

MR. DARREN RAINKIE: Yes, sir, we're familiar with it.

MR. KRIS SAXBERG: And you'll agree that it's stating that if the corporate allocation is removed from the revenue requirement calculation under rate base rate of return, then the revenue requirement for rate base rate of return is less than under cost of service?

MR. DARREN RAINKIE: Yes, if we do that mechanical calculation, sir. That's not our position, we simply did in this Information Request, what was asked of us to remove the 15.1 million.

I -- I suppose we could have put a disclaimer or a paragraph in there but we thought it wasn't -- it wasn't appropriate, but we -- we did what was asked of us, sir. And that's the -- that's the mechanical calculation.

MR. KRIS SAXBERG: I just want to look at the benefits on the hydro side, on the electric side for a moment. Under rate base rate of return methodology, there would be a return on equity amount of approximately $12 million for the '05/'06 test year, correct?

MR. DARREN RAINKIE: That's correct. But as we explained the other day, that money does not get paid out in a dividend to the electric side of the business. That -- that money would stay in the retained earnings of -- of Centra for the benefit of gas customers.

So, you know, I'm a little dicey on using these terms,'return'. To me, 'return' means after you've covered all your expenses and you have a certain amount of money, that's there and that's available for distribution to the shareholders. And that is, of course, the private company context.

But I think, as Mr. Warden indicated several times in the record that week, the policy position of Manitoba Hydro is different. So just -- I'm just -- when we use that -- that term, 'return', I think we should look at the purpose for which the money is going to, not label it with a certain label and -- and then say, Well, it's good, bad or indifferent.

MR. KRIS SAXBERG: And there's $9 million of synergies in the electric side of the organization as well; correct?

MR. WILLIE DERKSEN: In that order, yes.

MR. KRIS SAXBERG: So if I add the return of approximately 12 million to the $9 million of synergies, then together that amount exceeds the $19 million, estimated $19 million in annual costs associated with the acquisition and integration, and even leaves a margin of $2 million for retained earnings; does it not?

MR. VINCE WARDEN: Mr. Saxberg, as Mr. Rainkie attempted to explain just a -- a moment ago, that 'return', as you called, is not being pulled out of Centra. So it's not going over to Hydro. It's remaining in Centra for the benefit of Centra ratepayers.

MR. KRIS SAXBERG: But that's not what's -- that's not what happened in the last three (3) years. The entire amount of the return plus was transferred as a credit to Manitoba Hydro Corporation.

MR. VINCE WARDEN: No. No, Mr. Saxberg. It was not.

MR. KRIS SAXBERG: Well, your Exhibit 12, does it not show that there is a charge in 2003 and in '04 of $15 million to Centra, and a credit of that same amount to Manitoba Hydro Corporate?

MR. VINCE WARDEN: Mr. Saxberg, as I explained earlier, all this is doing is indicating how those acquisition costs are being allocated between electricity and gas ratepayers. There -- there's no transfer of monies. There -- there is an allocation from corporate to gas, to electricity ratepayers, and that's cleared out at the end of the year.

That was done solely to facilitate this discussion we're having right now, so that it could be very, very clear what was happening, that there's no benefit to electricity ratepayers from this transaction other than the synergies that we -- we talked about earlier.

MR. KRIS SAXBERG: But for the corporate

allocation, net income would have been $15 million higher in Centra Gas in those years?

MR. VINCE WARDEN: Well, it's clear that in those years, again referring to our Exhibit Number 12, net income in 2002/03 was insufficient to cover the corporate allocation. Likewise, in '03/'04 it was insufficient to cover the corporate allocation. And, therefore, there was a -- a net reduction in retained earnings in both of those years.

MR. KRIS SAXBERG: So, in effect, the return on equity portion was taken out of Centra through the application of the corporate allocation?

MR. VINCE WARDEN: Well, we can go around and around on this, Mr. Saxberg, but I -- I'm telling you there was nothing taken out of Centra. There was an allocation to Centra of the fair share of the costs of acquisition.

MR. KRIS SAXBERG: And at the end of the day it means that the return on equity awarded by the Board didn't go to the bottom line and didn't impact net income.

MR. VINCE WARDEN: Well, the net income in Centra was insufficient -- I'm repeating myself it seems, but was insufficient to cover off the total costs of the allocation each of those years.

MR. KRIS SAXBERG: And you'd agree that at any time Manitoba Hydro can take the return on equity out of Centra Gas, and without seeking approval of the Board.

MR. VINCE WARDEN: It's never crossed my mind to take that money out as it would be the wrong thing to do. We're not -- we're not here to take money out of Centra.

MR. KRIS SAXBERG: Or to render further corporate allocations which have the same effect as taking the return out of the organization.

MR. VINCE WARDEN: The corporate allocation is the amount required to recover the costs of the acquisition, apportioned fairly between electricity and gas ratepayers.

MR. KRIS SAXBERG: When the corporate allocation was determined to be 12 million, rather than the 15 million in prior years. That was done fairly recently in the context of -- of a review of financial statements?

MR. VINCE WARDEN: Yes, it was done in conjunction with the year end process at Manitoba Hydro.

MR. KRIS SAXBERG: Was there a document that was submitted to the Board of Directors to support the reduction of the $15 million allocation to a $12 million allocation?

MR. VINCE WARDEN: To the Board of Directors of Manitoba Hydro, no.

MR. KRIS SAXBERG: Or the Board of Directors of Centra Gas?

MR. VINCE WARDEN: No.

MR. KRIS SAXBERG: And so -- so was there any submission made to the Board with respect to why the corporate allocation should be adjusted from 15 million down to 12 million?

MR. VINCE WARDEN: Yes, the -- there was a discussion of this at the Audit Committee of the Board, and they fully understand why this was done. The financial -- year end financial statements have not been presented to the -- to the Board of Manitoba Hydro yet, that takes place next week on June 23rd. And on the recommendation of the Audit Committee, I'm sure they'll have no difficulty with that.

MR. KRIS SAXBERG: Does the Audit Committee have a -- a written submission that it's going to be presented to the Board?

MR. VINCE WARDEN: They do not.

MR. KRIS SAXBERG: Did the Audit Committee receive a written submission before making its decision?

MR. VINCE WARDEN: They did not.

MR. KRIS SAXBERG: Centra Exhibit 16, is the graph referencing actual O&M Costs, comparing those to CPI and customer growth. Perhaps you could turn that up?

MR. VINCE WARDEN: Yes, we have it here.

MR. KRIS SAXBERG: Could you undertake to provide the Excel spreadsheet that shows all of the data points for this graph?

MR. VINCE WARDEN: Yes, we can do that.

MR. KRIS SAXBERG: And would you also include information concerning the underlying CPI determinations, and their source, and the calculation of the customer growth assumptions?

MR. VINCE WARDEN: Sure, we can do that as well.

--- UNDERTAKING NO. 25: Centra to provide CAC/MSOS Excel spreadsheet that shows all of the data points for the graph, as well as information concerning the underlying CPI determinations, their source, and the calculation of customer growth assumptions.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Now, Mr. Derksen, you had indicated on Wednesday, that there was an implied productivity assumption built into Centra Exhibit 16. Do you recall that?

MR. WILLIE DERKSEN: Yes, I recall that.

MR. KRIS SAXBERG: And I think you said it's because wage -- actual wage increases are above CPI?

MR. WILLIE DERKSEN: Yes, that's correct.

MR. KRIS SAXBERG: And actual wage increases are 3.88 percent; does that sound right?

MR. WILLIE DERKSEN: I believe that's the number, I'd have to check to confirm it.

MR. KRIS SAXBERG: Why is it the case that -- that wage increases are -- are higher than -- than CPI? And ought they be?

MR. VINCE WARDEN: We have a -- a progression system at Manitoba Hydro whereby people start at the bottom of a range -- I think it's very typical of most organizations, start at the bottom of a range and work there way through to the top.

So, people -- to the extent that people are still working their way through that range as they gain experience in the Company, they're more valued, of course, with that experience. They're paid more in addition to the annual general increases that are awarded to all employees.

So those things, together -- together with some what we call merit increases, results in the composite increase of 3.8; if that's the number.

MR. KRIS SAXBERG: Now, with respect to 1998 actual costs, Mr. Derksen, you explained that there were some adjustments made to account for a new accounting treatment -- or differences in accounting treatment between West Coast and Manitoba Hydro?

MR. WILLIE DERKSEN: Yes.

MR. KRIS SAXBERG: Were those same adjustments made for the years 1993 through 1997?

(BRIEF PAUSE)

MR. WILLIE DERKSEN: Yes, the major adjustment was the reclassification of payroll tax and that's been done in every one of the years.

MR. KRIS SAXBERG: But, was the transportation depreciation adjustment made?

MR. WILLIE DERKSEN: Effectively it was. I -- my understanding is because these numbers here were based upon the audited financial statements of Centra and the audited financial statements reclassify the transportation depreciation away from O&A expense.

MR. KRIS SAXBERG: Was the adjustment for overhead methodology made?

MR. WILLIE DERKSEN: I believe there was no adjustment for overhead methodology made in these.

MR. KRIS SAXBERG: And the impact of that would be then to reduce the -- the reporting of actual costs for those years by -- by what amount; is it close to half a million dollars?

MR. WILLIE DERKSEN: I believe that's correct, yes.

MR. KRIS SAXBERG: So, we should be seeing actual costs underneath the CPI customer growth lines for those years 1993 to 1997 then if that adjustment was made?

(BRIEF PAUSE)

MR. WILLIE DERKSEN: Well, I think if we stated in 1993 for both lines, the lines and the bars are at the same point, you'd see the same basic information. It's just the gap in the years following 1998 would be a minor amount smaller than it is.

MR. KRIS SAXBERG: So Centra under West Coast was able to keep its actual costs below CPI and customer growth increases?

MR. WILLIE DERKSEN: Well, this graph shows that it's virtually identical to those sorts of things.

And as I've indicated, the period up to 1998 there was a period of time where little of no wage increases were being given to employees and as well, subsequent to that point in time, there have been some substantial cost increases related to bad debts, related to pension expense and other items.

So, I think, you know, that was then and this is now.

MR. KRIS SAXBERG: And you'd agree that the actual O&M set by the Board, during this period 1993 to 1998, was lower than the actual costs?

I put too many actuals in that question I think, so let me just start again.

What you've presented on this chart are the actual costs incurred not the approved Public Utility Board O&M costs?

MR. WILLIE DERKSEN: Yes, these are always the actual costs incurred.

MR. KRIS SAXBERG: If the -- if you had

depicted what was approved and therefore what was recovered in rates, those amounts would be lower than the CPI customer growth increases?

MR. WILLIE DERKSEN: I don't have the numbers in front of me, sir, so I can't validate that.

MR. KRIS SAXBERG: You don't have any contrary evidence to the assertion that the actuals were higher than the approved in each of these years?

MR. WILLIE DERKSEN: I know that it's true in 1998, the actuals were higher than the approved, but I don't have the -- the track from prior to that.

MR. KRIS SAXBERG: Could you undertake to provide that information?

MS. MARLA MURPHY: I might indicate we have already indicated -- undertaken on the record to provide the rates applied for and granted from 1994 which I believe has the information you're looking for.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Thank you for that.

Now, for the year 2003 the actual O&M costs were 53.6 million?

MR. WILLIE DERKSEN: Yes, that's correct.

MR. KRIS SAXBERG: What would they have been if they had matched CPI in customer growth?

MR. WILLIE DERKSEN: According to this schedule, fifty-nine point one (59.1).

MR. KRIS SAXBERG: And that is a -- a difference of approximately 5 million, correct?

MR. WILLIE DERKSEN: Five and a half (5 1/2).

MR. KRIS SAXBERG: Shouldn't we be seeing a deduction of approximately seven (7) million being the synergy reduction?

MR. WILLIE DERKSEN: Well, you would, except that there are those other factors that I've talked about, and that are attached to our rebuttal evidence as well, that show that there are significant cost increases that would have occurred under either Centra or with Manitoba Hydro.

And, I think, as I've said, in 1998 the allowed debt expense was in the order of nine hundred thousand dollars ($900,000), whereas the real expense for that year was something in the order of -- of one point three (1.3) to one point five (1.5), I'm not sure what the exact number was, and it's grown to almost $3 million.

As well, there was increases in pension costs and -- and the change related to replacing the company's customer information system with the Banner system. The customer information system was a capital based system that most of the costs were -- well, first of all, they were fully depreciated, but they were in depreciation and interest, whereas Centra, in acquiring this new system, had transaction fees of about $2 1/2 million flowing through its O&A expense.

So there are a whole number of cost increases that had occurred and would have occurred, that aren't included in a straight CPI plus customer growth graph.

MR. KRIS SAXBERG: Do you agree that Centra Gas should have, as a target, that its O&M does not increase any higher than CPI and customer growth on a year over year basis?

MR. WILLIE DERKSEN: From my perspective, I think that we have to take a look at the costs that are really going to be incurred in order to support the customers and their requirements. And so the target should be based upon the -- the cost expected.

MR. KRIS SAXBERG: Centra Exhibit 16 shows that Centra under West Coast was able to keep track with -- with CPI and customer growth and not -- and to keep its -- its growth in O&M costs below CPI and customer growth; you agree with that?

MR. WILLIE DERKSEN: Well, sir, as I've

said several times, during that period of time the economy of Manitoba was not very -- was not very strong and the costs were being contained artificially, if you like, during that period, because of that factor.

But what this graph is showing is that in spite of that, the costs under West Coast were tracking with CPI and customer growth and the costs subsequent to that time have dropped below that, and I think the trend line is lower than that as well.

MR. KRIS SAXBERG: And what we should see for Centra Gas under Manitoba Hydro ownership is costs on a year over year basis, at least $7 million lower than this CPI customer growth forecast?

MR. WILLIE DERKSEN: Well, I think it's $7 million lower than they otherwise would have been, not lower than the CPI plus customer growth forecast. This is an indicator and it's, you know, it tells a story, but it's not all of the facts that have been presented before this Board.

(BRIEF PAUSE)

MR. KRIS SAXBERG: The last time that the Board reviewed Centra Gas's O&M was at the GRA, leading to Board Order 118/03, correct?

MR. WILLIE DERKSEN: Yes, that's correct.
MR. KRIS SAXBERG: And at that Hearing, the Board was faced with comparing costs advanced by Manitoba Hydro, under a new cost allocation system, with an old methodology of accounting for costs, correct?
MR. WILLIE DERKSEN: Yes.
MR. KRIS SAXBERG: And it wasn't an apples to apples comparison, it was -- it was -- in that instance?
MR. WILLIE DERKSEN: The presentation of the costs were different, that's right.
MR. KRIS SAXBERG: And so what came out of that Hearing was a comment by the Board in its order, stating that the four point (4.) -- the $49.3 million in cost of operations, that had been approved, would, on a go forward base, represent a base line from which future applications could be measured; do you agree with that?
MR. WILLIE DERKSEN: Yes, I read that statement.
MR. KRIS SAXBERG: And do you agree that this Board should be looking at the $49.3 million number for 2003/04, and measuring the test years against it?
MR. WILLIE DERKSEN: Well, no, sir, as I -- as I think we've explained in much of our evidence, that the 2003/04 test year forecasted operating costs

were a transition, and there were some items that were under forecasted as a result of the transition, I think a much better comparison would be the actual costs incurred in 2003/04 and looking forward from that point.

MR. KRIS SAXBERG: The actual costs incurred for '03/'04 were 52.7 million, and that's reflected on CAC/MSOS/CENTRA-15(A)?

MR. WILLIE DERKSEN: Yes.

MR. KRIS SAXBERG: Your budget though, would have provided for costs, total costs in the amount of 49.3 million?

MR. WILLIE DERKSEN: Yes.

MR. KRIS SAXBERG: And in this undertaking, which -- which was circulated on Wednesday, I believe to everyone, sorry, this prior response, CAC-15, you've set out information on why it is the case that you didn't achieve your budget. Is that a fair characterization of the Information Request Response?

MR. WILLIE DERKSEN: Yes.

MR. KRIS SAXBERG: Now, on the very last page, CAC/CENTRA-15(B), page 4 of 4, you're noting that there is a synergy transfer benefit of $3 million included in the forecast; do you see that?

MR. WILLIE DERKSEN: Yes, I see that.

MR. KRIS SAXBERG: Has the synergy

transfer amount, approved by this Board, been embedded in the cost of operations?

MR. WILLIE DERKSEN: The actual cost of operations, the actual cost of operations in order to service the gas utility are being charged to the gas utility. There is no $3 million or any other synergy benefit transfer amount in the actual costs of operations.

What we've done in this schedule is for forecast comparison purposes, recognizing that the $3 million was based upon expected benefits in Centra. We've reclassified it as an operating cost component, but that's only in the forecast.

MR. KRIS SAXBERG: The actual cost of operations is affected by the amount of activity rate charged and the amount of activity rate hours recorded; correct?

MR. WILLIE DERKSEN: Yes.

MR. KRIS SAXBERG: So if you were simply to increase the activity rate without changing the amount of activity hours recorded, you'd increase the cost of operations?

MR. WILLIE DERKSEN: Well, we would but there is a mechanism to ensure that that doesn't happen. And that mechanism calls for the redistribution of any residuals, any over-recoveries, to both gas and electric operations.

So if a department, let's say, had $10 million in operating cost and it had an activity rate designed to recover that $10 million there would be no residual in there. But let's say they -- they raised that activity rate such that they recovered $11 million, that $1 million credit would then be reallocated back to gas and electric operations.

So, that the increase in the activity rate, in and of itself, was not the factor in increasing the operating costs being charged to gas.

MR. KRIS SAXBERG: If I could get you to turn to page 1 of 4 of CAC/CENTRA-15(B)

MR. WILLIE DERKSEN: Yes, sir.

MR. KRIS SAXBERG: The variance between forecast and actual, in connection with certain matters, is -- is fairly significant; you agree with that; for instance Banner system?

MR. WILLIE DERKSEN: Yes.

MR. KRIS SAXBERG: What accounts for the forecast with respect to the Banner system costs being off by 61 percent, being understated by 61 percent in the forecast or budget versus what actually occurred?

MR. WILLIE DERKSEN: Well we do provide a response for that in -- on that page and basically it relates to when there's a major implementation of a system going on, the staff that are normally there to support the ongoing operation of that system refocus their efforts towards the capital project of -- of creating this new enhancement.

And so the forecast assumed that they were going to move ahead into that capital project at an earlier date than actually happened. And so those people that would have moved off of the -- off of the supporting of the operating of -- of that system kept their roles in that support rather than move on -- moving on to the capital project.

Now, what happens in our operations during that period of time is that there's generally a list of things that would -- they would like to have addressed but if you minimize that list so that only the high priority items are addressed by that staff.

MR. KRIS SAXBERG: Is it a matter of poor forecasting or is it -- is it that there are not enough cost control measures in place to ensure that budgets are achieved?

MR. WILLIE DERKSEN: Well, neither of those, sir. The -- the forecast is done ahead of time and it's based upon the best information that they have at that time.

And in -- in this case the circumstances that were forecasted didn't transpire such that the project moved ahead at the -- at the rate expected. So I wouldn't characterize it as either one of those items.

MR. KRIS SAXBERG: On the next page, which is page 2 of 4, I note that donations and grants vary by 69 percent from forecast to actual; do you see that?

MR. WILLIE DERKSEN: Yes, I see that.

MR. KRIS SAXBERG: And I note that the response as to why that occurred -- but wouldn't it be -- it would seem to me that it would be a fairly straightforward matter to stay within budget in terms of what your donations and grants are?

Why shouldn't the Board here say, you know, you shouldn't be entitled to recover anything more than was in the budget when it was within your power to assure that that was the case?

MR. WILLIE DERKSEN: Well, the donations and grants expense that are actually incurred by Manitoba Hydro and Centra are certainly under the authority of the executive of -- of the company.

And if they felt that it was reasonable and appropriate that this level of grants and donations should be made, then that's what actually happens.

I don't see it as a budgetary control issue or -- or anything else. They make their decisions based upon the information that's prevalent at the time.

MR. KRIS SAXBERG: Does the company have a position on what is a reasonable amount to exceed budgets by?

MR. VINCE WARDEN: We do everything possible not to exceed budgets, Mr. Saxberg. Sometimes circumstances are such that it can't be prevented but -- but no amount of exceeding budgets is looked upon favourably.

We -- we do look at actual expenditures compared to budgets on a regular monthly basis at executive committee and we satisfy ourselves that the reasons for the -- any over or under expenditure are appropriate.

MR. KRIS SAXBERG: Do you agree that the increase in cost of operations from 03/04 approved to the test year here, is approximately 10 percent?

MR. WILLIE DERKSEN: That seems about correct, yes.

MR. KRIS SAXBERG: And with payroll increases only amounting to 3.88 percent, doesn't that seem a bit too rich?

MR. WILLIE DERKSEN: Well, I think it stems back to a -- the transition year that I tried to explain earlier. We under-forecasted the costs in that particular year and I think the actuals, if you look at a trend line based upon the actual costs incurred to operate the utility, you wouldn't find that gap, and our graph shows that.

So, it -- it is a little bit unfortunate but in transitioning sometimes those things happen.

MR. KRIS SAXBERG: The cost per customer in connection with the approved O&M of forty-nine point three (49.3) is a hundred and ninety-four dollars ($194); is that correct?

(BRIEF PAUSE)

MR. WILLIE DERKSEN: That's the 2003/04 approved, based upon the forecasted number of customers at that time?

MR. KRIS SAXBERG: Right.

MR. WILLIE DERKSEN: I don't have the numbers in front of me, sir. I'd have to check what the right number was. I recall there was, in our last 2003/04 Application, there was a mathematical error made, or an error made in the number of customers such that the cost per customer was understated in our Application and I'm not sure if that's the particular amount that was understated.

So, I -- I'd be hesitant to agree with that until I looked at the numbers.

MR. KRIS SAXBERG: Perhaps you could undertake to look at the numbers and provide the -- the cost per customer for '03/'04 using the approved O&M of 49.3 million.

MR. WILLIE DERKSEN: I could do that.

--- UNDERTAKING NO. 26: Centra to provide CAC/MSOS the cost per customer for '03/'04 using the approved O&M of 49.3 million.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: And you'd agree that the cost per customer for the first test year here, is two hundred and eleven dollars ($211)?

MR. WILLIE DERKSEN: Yes, I'd agree with that.

MR. KRIS SAXBERG: And then it increases to two hundred and fourteen dollars ($214) for the second test year?

MR. WILLIE DERKSEN: Yes.

MR. KRIS SAXBERG: How significant is -- is the impact of recording time and errors associated therewith on the difference between forecast and actual results?

MR. WILLIE DERKSEN: It wasn't the recording of time that was wrong, it was the basis upon which the forecasted activity rates that was incorrect or that was understated in the forecast.

And so, if we came up with activity rates that were too low from an integrated forecast perspective, the resulting charges to Centra Gas would also be too low. And -- and that's what happened in this -- in this circumstance.

MR. KRIS SAXBERG: Do you agree that if the total operation costs of the consolidated organization are higher than what they ought to be, then that the allocation to Centra Gas would also be higher than it ought to be?

MR. WILLIE DERKSEN: Higher than it ought to be; could you elaborate on that a little bit?

MR. KRIS SAXBERG: If the -- if the consol -- the budget --

MR. WILLIE DERKSEN: Yeah.

MR. KRIS SAXBERG: -- on a consolidated

basis is exceeded, then the allocation to Centra will also be higher than it -- than it should be?

MR. WILLIE DERKSEN: No, not necessarily. It would very much depend upon the circumstances that caused the results to be higher than -- than was budgeted.

For example, if there are significant storm activity, and we have that from time to time on the electrical side, the budgets could be exceeded on the electrical side. But there'd be no related impact to the gas cost of operations, as a result of that.

MR. KRIS SAXBERG: But there's no specific gas operations budget, correct; there's only a consolidated budgets?

MR. WILLIE DERKSEN: The total cost is an integrated basis. The -- there is a budget for gas cost of operations, or gas O&A expense, and that's included in this -- in the materials that we've presented. So there is a budget for gas op -- O&A costs.

MR. KRIS SAXBERG: But, not on a department by department basis, just in -- as a grand total is what you're suggesting?

MR. WILLIE DERKSEN: We're talking a program by program basis, and then with a grand total.

MR. KRIS SAXBERG: If cost of operations

increased only by CPI and customer growth, from the approved amount of 49.3 million, would you agree that the -- the test year request would be closer to 52 million, than the 54 million that's applied for?

MR. WILLIE DERKSEN: I think what I've been trying to say is that the $49 million that was previously approved was based upon a forecast, an amount that was under forecasted. But mechanically, if you increase a low number of -- a lower number than actually incurred by -- by the same percentage increase, it will result in a -- in a future lower number as well.

So mathematically, yes, you're correct. But I -- but the premise that you're using, I find flawed.

MR. KRIS SAXBERG: And it was just a coincidence that the budget was under forecasted by an amount very close to the synergy transfer that was awarded?

MR. WILLIE DERKSEN: Absolutely.

MR. KRIS SAXBERG: Just quickly. With respect to the Gladstone Co-op and the -- the amount -- the net addition to -- to rate base, would you agree that the amount that you're seeking to include in rate base is higher than the net book value of -- of that co-op?

MR. WILLIE DERKSEN: The net book value

as at what date, Mr. Saxberg?

MR. KRIS SAXBERG: The -- the sale.

MR. DARREN RAINKIE: I'm not sure we have the final number on the record here anywhere. I think the last financial statement we have for being on the record, was maybe four (4) or five (5) months before the sale actually occurred. And I'd have to find that number to answer your question, sir.

MR. KRIS SAXBERG: And maybe that would probably speed things up for me. If you could provide the net book value of -- of the co-op, at or around the time of sale, and indicate the difference between that amount and the 1.758 million applied for in the rate base in this Application?

MR. WILLIE DERKSEN: We can do that, sir. And keep in mind that that transaction, the way it was structured, it was structured with respect to the right hand of the balance sheet. We were -- the deal was that we would pay all of the obligations.

Again, it wasn't structured to be based on the left hand side of the balance sheet, and the net value. Having said that, I can provide that number. But let's just recall what the -- what the actual sales transaction was based on.

--- UNDERTAKING NO. 27: Centra to provide CAC/MSOS the net book value of the co-op, at or around the time of sale, and indicate the difference between that amount and the 1.758 million applied for in the rate base in this Application.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: And with respect to the Interlake connection fee issue, has Centra considered requiring the municipalities to fund the difference between what was forecasted to be recovered in connection fees and what would happen if the connection fees are no longer required?

MR. WILLIE DERKSEN: No, sir, we are living by the arrangements of our original deal with the municipality. We're not going to go back to them and ask them for more money.

MR. KRIS SAXBERG: Can you provide -- can you quantify the amount of funding that's going to be foregone by virtue of withdrawing the connection fee requirement?

MR. DARREN RAINKIE: There's an

information request on this, Mr. Saxberg, that lays out the difference between -- between the two (2). I can check and find that at the break and probably get back to you on the record on that one?

THE CHAIRPERSON: Mr. Rainkie, didn't you say at the time that it was difficult to estimate. You were, sort of, assuming the possibility that increased connections as a result of no connection fee could make up for the lack of connection fee over the long haul?

MR. DARREN RAINKIE: That's correct, sir. I think, if I understood the undertaking I just took, it was to take a look at what was originally projected in the original feasibility test which would be a number we could pull out of the feasibility test and what had been collected to date.

Hopefully I understood what the undertaking was.

MR. KRIS SAXBERG: Well, I mean, at the inception of the -- of the expansion there was an amount that you forecast would be recovered by way of connection fees over, I believe, the entire thirty (30) year period; was there not?

MR. DARREN RAINKIE: That's right.

MR. KRIS SAXBERG: And that amount then, you'd have a dollar figure there and you could compare that to what was actually collected and the difference would be what you're foregoing, correct?

MR. DARREN RAINKIE: I think we're on the same page, yes.

MR. KRIS SAXBERG: And that's the information that you're going to look for?

MR. DARREN RAINKIE: That's correct. I mean, I might add that's one of the reasons we didn't want -- going back to your original question of why we don't go back to the Coop; that's one of the reasons that we didn't want these connection fees to be considered a rate and collected by Centra in the first place, is we then take the risk of collection.

You know, and I can't remember, sir, your client's position on that particular issue but -- but the decision that Centra had to go collect those fees led to the risk that we wouldn't collect them in the end in their entirety.

MR. KRIS SAXBERG: Attachments and forecasted volumes have come up short under what was forecast for this expansion; correct?

MR. DARREN RAINKIE: That's correct.

MR. KRIS SAXBERG: And have you measured the financial consequence to existing ratepayers as a result of the non-achievement of attachments and volumes?

MR. DARREN RAINKIE: Yes. You know, I don't have the exhibit number right now, but I think it was either Tuesday or Wednesday of last week when I was chatting on the record with Mr. Peters, I filed the final recalculation of the Interlake/Woodlands/Bifrost Project and that's the information we should be looking at.

MR. KRIS SAXBERG: And that's -- that's what I -- I guess I just want to make sure I understood the exhibit and it's Centra Exhibit 14. And is it the amount of two hundred and -- the net present value of revenue deficiency of two hundred and eighty-four thousand, seven hundred and forty-two (284,742)?

MR. DARREN RAINKIE: Sir, can you just give me one (1) second to locate it and we can deal with it right here.

MR. KRIS SAXBERG: Sure.

(BRIEF PAUSE)

MR. DARREN RAINKIE: Sir, just to make sure I have your question clear, you're asking about the deficiency in the project and to do that I think we would have to compare the original calculation of the contributions back in 2000 and 2001 with the final contribution that was calculated here.

Now, here you have the final amount. We'd have to go back and find the original amount; I have that in my notes. My -- just from my notes, the final true amount is about $7.5 million and the original contribution was about 6.6 million, so there's a difference of nine hundred thousand dollars ($900,000).

Now, I would note though, because there are two (2) tests in the feasibility test, the thirty (30) year net present value test plus the five (5) year revenue to cost ratio test, I would note on line 26 of -- of that particular true-up that the MPV of the revenue deficiency is, let's say, just for the sake of argument, three hundred thousand dollars ($300,000), so that would be to the benefit of the customers because of the pure way that the test works.

So, if I take the nine hundred thousand dollar ($900,000) difference, that I referred to you earlier, and backed off the three hundred thousand (300,000), I think the net impact to customers on a net present value basis is about six hundred thousand dollars ($600,000).

(BRIEF PAUSE)

MR. DARREN RAINKIE: That's a lot of

figures, Mr. Saxberg, in a short amount of time but --

MR. KRIS SAXBERG: I think I'll have to retire to digest them.

MR. DARREN RAINKIE: Or maybe I can -- maybe I can just help and go through that a little bit slower in one (1) time, just so that we can get this proceeding going.

We did an original calculation in the -- when the projects were put forward in terms of the contribution, which we collected from the -- all the levels of government. And that, according to my notes, we collected around $6.6 million between the Interlake Project that went in 2000 and the Bifrost/Woodlands project that was constructed I think late in 2001 or early in 2002.

This recalculation -- so that number is $6.6 million, roughly. This recalculation shows a contribution requirement of $ 7.5 million. So, the difference between those two (2) amounts is around nine hundred thousand (900,000).

But, to be fair, because of the way the feasibility test works, the -- sometimes the five (5) year revenue to cost ratio test comes into play and that, when you do a -- a recalculation it results in a positive MPV, which is what I -- I pointed to you at line 26 of the -- of the final recalculation.

So, if you just want to look at this at a net present value basis, I think you have to take the nine hundred thousand dollar ($900,000) number minus the three hundred thousand dollar ($300,000) number and you get to, I think, a fair representation of about six hundred thousand dollars ($600,000).

MR. KRIS SAXBERG: The -- the existing system customers are in the red by about six hundred thousand (600,000) would be your evidence then, that's the impact --

MR. DARREN RAINKIE: That's the deficiency, yes.

MR. KRIS SAXBERG: For years 4 and years 5, are those number of customers -- are those just forecast or are they actual?

MR. DARREN RAINKIE: Mr. Saxberg, I think on that particular line item, because I looked at that myself when I got this from our expansion people, I think what's happening there is I don't think we have all the revenue.

Because if you look at the revenue in year 3, it's five hundred and thirteen dollars ($513) and then we -- and that's a hundred and -- sorry, five hundred and thirteen thousand dollars ($513,000) for a hundred and sixty-nine (169) customers, then year 4 we go up to three hundred and twelve (312) customers and the revenue is only five hundred and forty-nine thousand (549,000).

I think those additional customers are customers that are paying the basic monthly charge. We've included that revenue, if you remember, a couple years ago we made a change to our terms and conditions of service that if you -- if you sign up with us and you end up not taking gas, we charge you the basic monthly charge.

So, that probably is making this look a little out of whack. But I would rely more on the projective revenue line, on line 7, which is -- which is fairly flat.

MR. KRIS SAXBERG: Okay. Thank you for that. And those are all my questions for this Panel.

Mr. Matwichuk is here, to my left, and perhaps after the lunch break we could set up to provide his direct evidence.

THE CHAIRPERSON: Thank you, Mr. Saxberg.

MR. KRIS SAXBERG: Or, sorry, I'm jumping ahead of -- because I think there's other Intervenors that are -- have questions.

THE CHAIRPERSON: Yes.

Mr. Boyd, do you have any questions of

this Panel?

MR. SANDY BOYD: Yeah, I've got a few.

THE CHAIRPERSON: Do you have an estimate of how much time you require?

MR. SANDY BOYD: I don't think it would be more than fifteen (15) minutes.

THE CHAIRPERSON: Then why don't we do it now, please.

CROSS-EXAMINATION BY MR. SANDY BOYD:

MR. SANDY BOYD: Thank you. These questions are dealing with AMR, the automated meter reading.

I think it's on record at PUB-123 that MHUS charges Manitoba Hydro eighty-eight (88) cents per read; is that correct?

MR. DAVID CASE: That's correct.

MR. SANDY BOYD: And the average customer gets read how many times a year?

MR. DAVID CASE: The average customer is read bi-monthly, so six (6) times per year.

MR. SANDY BOYD: Thank you. And I think, Mr. Case, you'd mentioned earlier the cost of the AMR device is approximately seventy (70) -- seventy dollars ($70)?

MR. DAVID CASE: That's correct.

MR. SANDY BOYD: And I'm going to guess it's going to be financed with long term debt?

MR. VINCE WARDEN: Yes, Mr. Boyd, typically capital expenditures would be financed with long term debt, to the extent that internally generated funds are insufficient to cover off those -- those expenditures.

So, I -- we -- we can't say specifically that we'd be financed with long term debt, because it would depend on how much funds are being generated internally, in any given year.

MR. SANDY BOYD: Thank you. So the average customer at six (6) reads at eighty-eight (88) cents, and I know it will go up as the years go by, but it's like less than five and a half (5 1/2) bucks per customer per year, in present day dollars.

This device is seventy (70) bucks, plus whatever interest it takes to pay it off, and we haven't installed it yet. So, when I look at this depreciation table at Schedule 4.9.2, we've got a line there at 28, AMR/ERT Modules, and the percentage is 12.3 percent. Does that mean we're writing them off at, you know, eight (8) years?

(BRIEF PAUSE)

MR. WILLIE DERKSEN: Mr. Boyd, that would mean that the existing assets that Centra has acquired under that classification are being written off over the equivalent of eight (8) years.

But I think if the plan was approved, we would -- and -- and we would be acquiring significant different assets than what the class had before, we'd look at the appropriate depreciation rate to use, prior to commencing the depreciation of those new assets. And I -- I'd heard -- I -- I think there's something longer than eight (8) years is their recommended estimated service life.

MR. SANDY BOYD: Thank you. If we go to the page where it talks about '06/'07 test year at 4.9.4, and the depreciation under that test year column, it seems to be increasing from what it is now. I think we're starting at thirty (30) K, and we go up to two ninety (290) K. I -- maybe -- I assumed it was due to the AMR stuff.

MR. WILLIE DERKSEN: I believe you're correct, yes.

MR. SANDY BOYD: So on that calc, we're still using eight (8) years?

MR. WILLIE DERKSEN: Yes, sir.

MR. SANDY BOYD: So the -- and -- and you said earlier that the life of the device is probably somewhat longer than that?

MR. WILLIE DERKSEN: That's my understanding, yes.

MR. SANDY BOYD: Do we have any feel for what the life of the device might be?

MR. WILLIE DERKSEN: The forecast life is fifteen (15) years.

MR. SANDY BOYD: Thank you. The life of an average meter is what?

MR. WILLIE DERKSEN: Currently seventeen (17) years.

MR. SANDY BOYD: So, to get an average of seventeen (17), and we have some failures prior to that, and we have some that are longer than that, to land at seventeen (17)?

MR. WILLIE DERKSEN: That's correct.

MR. SANDY BOYD: So, if we have this device on it and the meter fails, somewhat prior to fifteen (15) years, we've shortened the life of this electronic device in that scenario?

MR. SANDY BOYD: I think it depends when you say shorten the life. The life of the electronic device, the electronic device is supposed to fail independently of the meter, it's one (1) or the other.

MR. SANDY BOYD: Yeah, actually I was going to raise that one (1) next. But on this side if the mechanical side fails, prior to fifteen (15), we've stranded the life of the electronic device, and in your example if the electronic device fails prior to fifteen (15), we're stranding the life of the meter.

I'm assuming that when we send an employee out to repair either side we're probably going to change out both?

MR. DAVID CASE: I would say that's a fair assumption.

MR. SANDY BOYD: So those costs would all be on top of what we're talking about here for seventy (70) bucks for the device?

MR. DAVID CASE: Those would be ongoing operating costs.

MR. SANDY BOYD: Presently, when our meter readers go out to customers' premises, they do a few other things than just read meters; is that correct?

MR. DAVID CASE: That's correct.

MR. SANDY BOYD: They're trained for gas leaks, iced over regs., pipe strain, those sorts of things?

MR. DAVID CASE: That's correct.

MR. SANDY BOYD: So, when we look at a pilot project and Mr. Warden had mentioned earlier that up to this point he's never seen a cost benefit analysis that supported a full blown AMR, what other things are, that I'm unaware of, would even justify a pilot?

MR. DAVID CASE: The AMR project would really be a combination of electric and gas. So there are significant benefits on the electric side as well as on the gas as far as the meter -- metering device and it is expanded beyond the reading, as I said last week; that there's certainly advantages through AMR technology where you can do loadside management, you can look at system design.

There's a number of capabilities it offers beyond the meter reading. The issues you've raised would all have to be considerations as part of the business case.

MR. SANDY BOYD: But right now, at this hearing, we're asking for four hundred thousand (400,000) from the gas side without any justification, that I have seen; is that -- I don't know if that's fair or not but that's how I read it?

MR. DAVID CASE: I would say that's your interpretation. The reason for the project is to try to establish whether there is a reasonable case to be made to move forward with it. So I think to say otherwise right now is premature.

MR. SANDY BOYD: Well, I guess what I'm trying to get a handle around is, it's two hundred dollars ($200) per customer to install it, like the cost of the device, and a hundred and thirty (130) to get it installed, without any of these failures that we were talking about earlier.

And let's just figure it's financed with long-term debt, we're getting up to almost triple the cost per customer to get a read?

MR. DAVID CASE: That may be on the project. But, again, without the project you can't learn what the costs -- the real costs are. And, you know, there's some assumptions made here about the life and so on, these are -- there's not an exact science here right now.

MR. SANDY BOYD: Well, for a pilot I would have thought that you would, you know, to justify going ahead with a pilot you'd want the numbers to be somewhat close to see if -- if there is a case.

But they're not close in this case?

MR. VINCE WARDEN: Well, Mr. Boyd, they're not close according to your calculations taking into consideration the meter reading costs only. But there's a number of other benefits that Mr. Case referred to that we've yet to quantify.

The fact that there are those customers that don't allow meter readers on their premises is a big issue for us and there are quite a large number of those -- those meters.

So, time of use rates is something we're looking at at Manitoba Hydro. It's another reason for having a meter that has a capability of going and interrogating readings at any time of the day or night.

So there's a whole host of factors that we have to look at and bring into the equation and not just the cost of the meter -- meter read.

MR. SANDY BOYD: Thank you for that. Right now we have an ERT program which was -- one of the justifications for bringing it in was those hard-to-read customers. Is there a reason that those aren't being installed at these, you know, people that you can't get in for twelve (12) months of five (5) years; we've got a few of those also?

MR. DAVID CASE: We still have a number of ERT's that are installed and useful.

MR. SANDY BOYD: I'm just wondering why we're not installing more of them if -- if these hard-to-read ones are part of the justification for this and it was the justification for ERT, you've got a program that will get the hard-to-reads.

MR. DAVID CASE: So far, the ERT's have only been installed at a small number of customers of these hard-to-reads. It's obvious to us that there are many more customers that were experiencing more problems and the ERT technology is still useful with the proposed AMR technology, which I didn't understand last week.

MR. SANDY BOYD: Thank you. The time of use stuff that you mentioned, Mr. Warden, does that apply to the gas side or is that just electric?

MR. VINCE WARDEN: It is just electric, but there are such things as load -- load management that would -- would apply to the gas side of the business as well.

MR. SANDY BOYD: And how does that help -- like, I -- I'm not going to dispute that because you get a monthly and, I guess, if you had a daily read it would tell you something different I suppose; is that what load management would be?

MR. AZIZ AZIZ: Load management will give us some indication about the actual consumption being used, which will help us in justifying or -- or checking our existing system and by deferring any system looking our capital expenditure in the future. So it will give us information useful in the design and system improvement in the future.

MR. SANDY BOYD: And we presently can't get that when we're only there bi-monthly?

MR. AZIZ AZIZ: We get -- we use assumptions. We get consumption over sixty (60) days, we use degree days during this period, and we get an average. But if you have an instantaneous load you will be able to check your consumption within one (1) hour, and which is we usually use or an instantaneous too.

MR. SANDY BOYD: The RSU's that are presently in place throughout our system for the cathodic protection, a good chunk of those have a pressure transmitter installed with them, and would you not get the same information by looking at pressure at these locations throughout our system?

MR. AZIZ AZIZ: That's right. We get -- we get pressure but pressures, when we get the -- the pressures through the system we simulate the system, try to adjust loads in order to meet this pressure, to say, our readings at this pressure. So but it doesn't give you indication of the load.

MR. SANDY BOYD: Dropping a system in pressure, there's a calculation that tells you what the load was to get that drop; is that not correct?

MR. AZIZ AZIZ: Yes.

MR. SANDY BOYD: Thank you. And at this point in time, is the -- has the corporate approved this pilot?

MR. DAVID CASE: I don't believe there's an approval for the pilot at this time.

MR. SANDY BOYD: Thank you. I've got no more questions.

THE CHAIRPERSON: Thank you, Mr. Boyd. We'll stand down now. If it's all right with everyone we'll come back at one o'clock.

MS. MARLA MURPHY: Mr. Chairman, just before we break, I might indicate that Mr. Rainkie is prepared to speak to the last two (2) undertakings that he took this morning if you'd like to have them on the record now.

THE CHAIRPERSON: Go for it, Mr. Rainkie.

MR. DARREN RAINKIE: I'm going to have to hold up everybody from lunch for a -- for a minute or two (2), but.

The first question was the -- the net book value of the assets from GANG, or Gladstone Austin Natural Gas Co-op. Let me just put the full picture on the -- on the record here.

The -- the original cost of those assets was approximately $3.5 million. Of course, in terms of the accounting, GANG used to back off the infrastructure grants in the constructions and -- the contributions they made to construction, that it received from its customers.

So that backed the number down to about $1.7 million. Of course, if you take the accumulated depreciation of four hundred thousand dollars ($400,000). The net book value of the assets of the financial statements is 1.3 million.

I might add though, if you look at the Information Request CAC/MSOS/CENTRA-28(A) and (B), the estimated replacement costs of the assets are $5.8 million. And the estimated depreciated replacement cost of the assets at the date of acquisition was approximately $5.0 million.

The second undertaking was the difference between the originally projected connection fees in the Interlake Region, and what we've collected to date. And if you look at the schedule that's attached to Information Request PUB/CENTRA-101(H), and you tally up the numbers for both the Interlake and the Bifrost/Woodlands projects which are both in û- in the Interlake.

The original forecast of the ten (10) year connection fees was about six hundred and seventy-six thousand dollars ($676,000). Those -- those fees collected in December 31st, 2004, is four hundred and five thousand dollars ($405,000).

I think that covers off both of those undertakings.

THE CHAIRPERSON: Thank you, Mr. Rainkie. So we'll see you all back in fifty (50) minutes.

--- Upon recessing at 12:10 p.m.
--- Upon resuming at 1:07 p.m.

THE CHAIRPERSON: Welcome back.

Ms. Melnychuk, do you have any questions?

MS. KAREN MELNYCHUK: No, sir. I do not.

THE CHAIRPERSON: Thank you.

MS. NOLA RUZYCKI: No, I do not.

THE CHAIRPERSON: Dr. Miller...?

MR. PETER MILLER: Hi. Yes, I have just three (3) questions that are quick to answer and you can perhaps take them home with you.

CROSS-EXAMINATION BY MR. PETER MILLER:

MR. PETER MILLER: The first has to do

with the feasibility test for connecting to the gas system. Just to make sure that we understand it properly, I wonder if there's some document that outlines the PUB's approved feasibility test and if you could provide that?

MR. DARREN RAINKIE: Mr. Miller, in fact, I was going to lead some direct testimony in the direct evidence for the third panel in that regard.

If you like, I can explain it to you now in advance or you can wait until I put my direct evidence in?

MR. PETER MILLER: Okay. But there isn't some kind of an approved statement of explanation?

MR. DARREN RAINKIE: There is an order from, I think it was, 1994, Mr. Miller, that was the genesis of the current test. There was a hearing before the Board where we came and asked for a thirty (30) year net present value test. So that's part of the equation; that's where the original test was -- was approved.

A few years after that, in the context of the St. Agathe expansion program -- project, the Board added an extra criteria that the revenue to cost ratio of the project had to be at least one (1) by the fifth year.

So unfortunately, it's spread out through two (2) different --

MR. PETER MILLER: No single document?

MR. DARREN RAINKIE: -- two (2) different Board Orders. But the -- the main test is a thirty (30) year net present value test; that's one of the hurdles the project has to meet is that the present value of the incremental revenues have to be at least equal to the present value of the incremental costs.

But up and above that there's another constraint that the revenue to cost ratio has to be at least one (1) or 100 percent, depending how you calculate it, or how you prefer to calculate it, by the end of the fifth year.

Depending on the particular cash flow of the project, either one of the constraints will be the dominant one and dictate what the contribution is.

MR. PETER MILLER: You said that you were going to deal with this under direct testimony. I wonder -- if it's going to be in the transcript tomorrow that would be fine.

MR. DARREN RAINKIE: Yes, it isn't lengthy direct but I think it gets to the point and it'll be in the transcript and of course you can --

MR. PETER MILLER: Okay.

MR. DARREN RAINKIE: -- ask me some follow-up questions if you so desire.

MR. PETER MILLER: Okay. Thanks very much. Well, the other two (2) have to do with the next Panel in particular, but I just wanted to leave them with you if that's all right.

There were a number of questions in response to the very brief treatment of gas DSM on Tab 6, where a -- a response was either declined or deferred because that was so preliminary and high level. And I'm -- I would appreciate it if you could just go through those questions and provide an update on the basis of the more detailed plan that we -- we have.

And I can give you some numbers of the questions where that kind of statement appears. RCM/TREE/Centra numbers 13, 14, 16, 17-B-2, 19 and 45.

MS. MARLA MURPHY: I've noted the numbers. The Panel that deals with that isn't here, so I can't indicated what kind of information they might be able to provide, but we'll certainly look at them.

--- UNDERTAKING NO. 28: Centra to go through the questions in the brief treatment of gas DSM in Tab 6 and provide TREE/RCM an update on the basis of the more detailed plan.

CONTINUED BY MR. PETER MILLER:

MR. PETER MILLER: Thank you. And the other one is, I think, fairly minor. In RCM/TREE/CENTRA-58(D), we asked, comparing different levels of standard, a standard construction power smart gas, power smart electric and R-2000, we asked for the amount of gas savings at each progressive level, and an answer was given in dollars.

I'm just wondering if the gas volume figures that underlay that calculation could be provided.

MS. MARLA MURPHY: We'll certainly pursue that.

--- UNDERTAKING NO. 29: CENTRA to provide to TREE/RCM the gas volume figures that underlay RCM/TREE/CENTRA-58(D).

MR. PETER MILLER: And -- so those are the questions I had. Thanks.

THE CHAIRPERSON: Thank you, sir.

Mr. Peters, you have a few things?

RE-CROSS-EXAMINATION BY MR. BOB PETERS:

MR. BOB PETERS: I have just a couple matters with this Panel, Mr. Chairman, that would arise perhaps by way of undertaking or responses provided subsequent to when I last spoke to them. And I can indicate that I plan to talk mostly with Mr. Case and Mr. Aziz, so the other gentlemen may want to sit back and relax for a change and...

Mr. Case, I want to start with the AMR project that Mr. Boyd talked to you about this morning. And my recollection from your evidence in reviewing the transcript was that there were approximately sixty-six thousand (66,000) inside meters; is that right?

MR. DAVID CASE: It's sixty thousand (60,000) plus, I'm not sure about the sixty-six thousand (66,000).

MR. BOB PETERS: Okay. Maybe I made that up. But you'd go for sixty thousand (60,000)?

MR. DAVID CASE: I'm sorry?

MR. BOB PETERS: You'd agree with sixty thousand (60,000) at least?

MR. DAVID CASE: Yes, sir.

MR. BOB PETERS: And the AMR project, was that designed only at inside meters?

MR. BOB PETERS: No, it wasn't. There's also a number of outside meters. If -- if you were to look at the number of hard-to-read meters, I think about 90 percent of them would be inside meters but there's another 10 percent where we have meters that are enclosed in fences or yard sites that are inaccessible.

MR. BOB PETERS: And when you're talking about hard-to-read meters, is -- is that the underlying justification that you're going to try to convince Mr. Warden supports, going to an AMR project, it's the -- it's the can't-read or can't-get-in?

MR. DAVID CASE: Certainly, one (1) of the benefits on the natural gas side of the business today is that the -- well, for a number of reasons we discussed the other day.

The volume of meters that we can't gain access to in a reasonable amount of time is certainly growing and it's getting more difficult to manage.

I think the other thing we're seeing is the trend with customers who are more concerned about their privacy and unknown people with -- without appointment times arriving on their property and certainly causing them some fears.

MR. BOB PETERS: All right. I -- I've got those points that you've given me. And -- and you went so far as to say that for some of these sixty thousand (60,000) indoor meters, up to 35 percent of them you'd get no readings on and they'd be estimates only; is that right?

MR. DAVID CASE: Yeah. I -- again, I stand to be corrected, it was actually 46 percent. I was using 35 percent as a conservative number but I've since learned it's closer to 46 percent.

MR. BOB PETERS: So it's 46 percent of the inside meters that you have difficulty getting readings on?

MR. DAVID CASE: That's right. And, as I said before, it's not always the same percentage. Obviously, that changes on each read cycle but there is certainly some of those that have been continuous estimates.

MR. BOB PETERS: But the reason you can't get readings on them, one (1) of the reasons is that the people won't let you in?

MR. DAVID CASE: That's correct.

MR. BOB PETERS: And what are some other reasons?

MR. DAVID CASE: We just did a pilot of a sample of a hundred and twenty (120) of these that were twenty-four (24) months plus. And the reasons that we found 34 percent were no answer, 25 percent were vacant, there was another 14 percent where the meters had been locked off. There was 4 percent of the buildings had been boarded up, and then there was various other reasons, including people hiding behind curtains and just not allowing them access.

MR. BOB PETERS: And when you say twenty-four (24) months plus, you're saying it's been twenty-four (24) months or longer since you had an actual reading?

MR. DAVID CASE: That's correct, yeah, twenty-four (24) months to seventy-one (71) months, that was the furthest out.

MR. BOB PETERS: When did you become aware you have meters that have been unread for seventy-one (71) months?

MR. DAVID CASE: Well precisely, just on the weekend actually. The seventy-one (71) months, I knew that it was moving out to five (5) years, but to be precise on seventy-one (71) months, it was only through an evaluation on the weekend.

MR. BOB PETERS: And the 34 percent of those twenty-four (24) plus -- twenty-four (24) month plus, without an actual reading, the 34 percent rates -- 34 percent related to no response from the customer about letting you read them?

(BRIEF PAUSE)

MR. DAVID CASE: I'm sorry you said 34 percent would not allow us to read them; is that what you're saying?

MR. BOB PETERS: Yes.

MR. DAVID CASE: There was no answer at the door.

(BRIEF PAUSE)

MR. BOB PETERS: And you've suggested to the Board that that 34 percent, where there's no answer, may be as a result of -- some of that would be fear and concern about letting a purported stranger into the home?

MR. DAVID CASE: It would appear so. We've had reports back from meter reader personnel who have indicated that it was clear to them that somebody was in the building, but chose not to allow them access for whatever reason.

MR. BOB PETERS: There are other meters inside people's dwellings other than the gas meter; is that correct?

MR. DAVID CASE: That's correct.

MR. BOB PETERS: And that would include a water meter?

MR. DAVID CASE: Yeah.

MR. BOB PETERS: And would you suppose that the utility running the water would have similar underlying concerns, as would Centra, in terms of gaining access and getting readings?

MR. DAVID CASE: Well they do have similar problems, yes, sir.

MR. BOB PETERS: And you know that because you sit on joint panels and joint committees with -- with the City utility?

MR. DAVID CASE: I don't personally, but we have information from people that do correspond with them regularly.

MR. BOB PETERS: Your concern is you want a bill that is accurately read; is that correct? That's Centra's concern?

MR. DAVID CASE: Well we want a bill that's accurately read and we also want a chance to monitor our plant, to ensure it's not being tampered with.

MR. BOB PETERS: In terms of having an accurate bill, based on -- on readings made, it may be that some consumers don't share that view, they're not so concerned about having an actual reading to generate the bill; correct?

MR. DAVID CASE: Yes, sir.

MR. BOB PETERS: And in situations where that arises for some of these other utilities that you are aware of, what do they do?

MR. DAVID CASE: The -- we have information from the City of Winnipeg, that they actually triple the estimate of the normal consumption, as one (1) example. And they had, as I understand, mixed success with that. In some cases the consumers didn't seem to mind paying triple.

MR. BOB PETERS: You understand the City would triple the estimate because they're confident then that at least the consumer's paying their actual costs?

MR. DAVID CASE: Well I think it was that, plus to get the customer's awareness and hopefully to raise their concerns enough where they would contact the utility to have their meter read.

MR. BOB PETERS: Well, in the vernacular, if the City's trying to smoke them out, but by increasing the reading it's -- it's still incumbent on the consumer to decide whether or not to pay it or to continue with the -- with the high estimate, correct?

MR. DAVID CASE: I'd agree.

MR. BOB PETERS: And you had indicated in a previous answer to me that your understanding was some consumers were actually paying the triple estimate?

MR. DAVID CASE: That's right.

MR. BOB PETERS: And why do you suppose they're paying that?

MR. DAVID CASE: I don't have the answer.

MR. BOB PETERS: Okay. Has Centra Gas considered amending or applying to the Board to amend its terms and conditions to allow Centra the opportunity to raise the estimate at certain intervals to gain the attention of the -- of the owner that you're looking to have an actual reading of the meter?

MR. DAVID CASE: Centra is considering a number of options. I don't believe anything's been brought before the Board.

MR. BOB PETERS: Is one (1) of those options increasing the estimate on the -- on the bill after a warning to the consumer?

MR. DAVID CASE: It has been one (1) of the options considered, yes.

MR. BOB PETERS: And is that something that the Corporation finds favour with?

MR. DAVID CASE: I think you're could to have mixed views on that. It certainly doesn't seem a good way to approach it from a customer service point of view.

MR. BOB PETERS: Is it a last resort to having to spend an inordinate amount of money to perform a reading?

MR. DAVID CASE: I think a last resort is to disconnect the service, enforce it.

MR. BOB PETERS: Do your terms and conditions allow you to disconnect for -- for not giving a reading?

MR. DAVID CASE: Yes, I believe they do.

MR. BOB PETERS: And you haven't don't that in seventy-one (71) months for some people?

MR. DAVID CASE: No, we haven't.

MR. BOB PETERS: Why is that?

MR. DAVID CASE: We just haven't chosen that option yet. The other thing, Mr. Peters, those customers have continued to pay their bill as well.

MR. BOB PETERS: Well, it's -- you only disconnect customers who haven't paid their bill?

MR. DAVID CASE: That's right. Well, that's right, but I think the question you had was, have we considered disconnecting for a non-reading.

MR. BOB PETERS: And I thought you answer was you had -- you -- you interpret your terms and conditions to give you that authority to do that?

MR. DAVID CASE: Correct.
MR. BOB PETERS: But you've chosen no to do that so far?
MR. DAVID CASE: That's correct.
MR. BOB PETERS: And you'll only disconnect if they don't pay their bill?
MR. DAVID CASE: That's been the case, unless it's a safety issue.
MR. BOB PETERS: So, if you increase the estimates month-over-month or every couple of months and the consumer keeps paying, you'd see no reason to disconnect them?
MR. DAVID CASE: It doesn't resolve all the issues. So that certainly would have to be considered as well.
MR. BOB PETERS: Have you considered asking the homeowner to pay for the cost of the automatic meter reading unit as a separate appliance?
MR. DAVID CASE: I'm not aware that there's been a direct communication with customers regarding automatic meter reading. We have certainly offered to move meters outside.
MR. BOB PETERS: How much does it cost you to move the meters outside?
MR. DAVID CASE: Round number, hundred

and ninety-five dollars ($195).

MR. BOB PETERS: Two hundred (200) is more round than that. But is that two hundred dollar ($200) figure a number that you are -- that's the same number you gave the Board -- well, let me start again.

You gave the Board the figure of approximately two hundred dollars ($200) to install an AMR unit; that is for the unit itself plus the installation?

MR. DAVID CASE: That's correct.

MR. BOB PETERS: And so for the -- for the same cost, approximately, you could move the meter from inside to outside?

MR. DAVID CASE: Yes, that would be about right.

MR. BOB PETERS: And is that another variable that has to be factored into the business case that you're preparing in attempting to convince Mr. Warden and his colleagues to let you continue with the AMR program?

MR. DAVID CASE: Yes, it would be a consideration.

MR. BOB PETERS: So even if you had the ability, in your terms and conditions, to increase the estimates, as long as the customer is paying it, your track record shows you wouldn't disconnect them?

MR. DAVID CASE: To date, that's correct.

MR. BOB PETERS: And so in order to get an actual reading, you'd want to force the customer into a situation where they don't pay the bill and then you would disconnect them; is that right?

MR. DAVID CASE: Yes, sir.

MR. BOB PETERS: And then before you reconnected them, you'd make it a condition that you had to do a reading?

MR. DAVID CASE: That's correct.

MR. BOB PETERS: Mr. Aziz, you filed with the Board an Undertaking 17, which the Board marked as Centra Exhibit 20, and it had to do with a cost comparison for the four-party and single-party trench programs for an area known as Royal Wood; do you have that document, sir?

MR. AZIZ AZIZ: I'm getting it here.

MR. BOB PETERS: I have it as a single page document, Mr. Aziz, marked, I have it as Centra Exhibit 20?

MR. AZIZ AZIZ: That's right. I have it here.

MR. BOB PETERS: Am I correct, Mr. Aziz, that you told the Board that the whole purpose of the four-party trench program was that you wanted to save the gas company approximately 25 percent of the costs of the costs of installation of service and mains?

MR. AZIZ AZIZ: The whole purpose is -- this is one (1) of the purposes, to achieve a cost saving of the installation for about 25 percent or more.

MR. BOB PETERS: That's the -- that's the hope, is it?

MR. AZIZ AZIZ: That's right.

MR. BOB PETERS: And when you look at what you filed with the Board, because I -- I want to make sure the Board, when they review this, interprets it correctly, and you're telling the Board that for a particular project and subdivision you have in the City of Winnipeg, if you were to have done it on a single party basis, which is the old Centra methodology in my questioning, it would have cost you approximately a hundred and fifty-six thousand nine hundred dollars ($156,900)?

MR. AZIZ AZIZ: That's right.

MR. BOB PETERS: But your actual costs, under the four-party trench, are two hundred and eighty-three thousand dollars ($283,000), correct?

MR. AZIZ AZIZ: This is right, yes.

MR. BOB PETERS: And so what the Board

will see right away is that it's about 180 percent of the single party costs to do a four-party trench?

MR. AZIZ AZIZ: This is what happened last year because our focus was to develop the -- the standards and procedures for the installations in the field, for safe installation. So, our focus was not on cost last year, our focus was to look into the four-party trench and see how they would develop standards and procedures for them to be safe to install in the field.

MR. BOB PETERS: All right. Thank you. Under the single-party trench system at a hundred and fifty-seven thousand dollar ($157,000) cost, that's the cost you want to be 25 percent lower than when you optimize this program; correct?

MR. AZIZ AZIZ: I didn't say it's 25 percent into the gas customers. I says our focus is 25 percent for the whole subdivision, and part of it is the gas and part of it the electric.

So we're looking into a cost saving to the corporation as in the neighbourhood of 25 percent; this is one (1) of the goals. And there is other things we're -- we're considering for the four-party trench.

MR. BOB PETERS: So, it's 25 percent of Hydro's and Centra's combined costs?

MR. AZIZ AZIZ: That's right.

MR. BOB PETERS: Would it be possible that you would have a situation where Centra's costs would be higher and perhaps the gas -- the electric side would have costs that were more than 25 percent lower?

MR. AZIZ AZIZ: I'm not -- as I mentioned before, I am not going to be speculating on the costs, how it will be at the end, after we do our own optimization process.

Also, if I look into the hard dollar cost here for the project, there is another cost which is -- hasn't -- we did not include it in this project, such as it is normal when we do, as I mentioned before, crossings for the single-party submeasure, if we cross Hydro primary cables. Hydro has always somebody supervising the crossings and in the past we used to get invoiced for this cost, and maybe right now.

So, this is the cost -- it's not part of the capital expenditure.

MR. BOB PETERS: But it will be included as part of the -- the test that determines whether or not there has been a 25 percent or more cost savings?

MR. AZIZ AZIZ: That's right, yeah.

MR. BOB PETERS: Can you tell the Board, on these line items which you haven't tried to optimize from a cost point of view, which ones you think you can get lower and still not compromise the safety?

MR. AZIZ AZIZ: I -- I think, as -- if I look into the inspection, the contract administration, the joint use trench overheads associated with all this -- so this is, we suspect this will be -- we're looking into all this. Like we're looking into the method of -- the methodology we're going to be utilizing to install this four-party trench right now, which will -- will be reflected in -- in those items I mentioned before.

MR. BOB PETERS: So you think you -- you can get the inspection cost down from fifty thousand dollars ($50,000) to something cheaper than nine thousand dollars ($9,000)?

MR. AZIZ AZIZ: And we might not even require an inspection if we opted to install the four-party trenches in our own --

MR. BOB PETERS: And then under the contractor costs, how do you propose that those costs will be optimized to something lower than twenty-eight thousand dollars ($28,000)?

MR. AZIZ AZIZ: Yeah, like -- like as -- as I mentioned before the contractor was hired to do this work on hourly rate, because there was no provision under unit price for four-party trench. So, we'll be looking into obtaining the, if we're to follow-up, or if we're going to proceed with the installation by a contractor, we'll be looking into the unit price submitted by contractors to do this kind of work, not an hourly rate.

MR. BOB PETERS: And how about this joint use trench cost; just -- we talked about that last time, but how do you see that being reduced?

MR. AZIZ AZIZ: As the joint use cost, which is -- I mentioned before, it's not only the 25 percent of the trench, this is as we have in under -- undertaking, and we provided this, and under Exhibit number 18, and the joint use covers the -- our costs of the trench, which is 25 percent. And sometime maybe the gas will be going separate, and the trench for X number of metre, and this allocated 100 percent to the -- Centra.

And also trenching, the services stops up to the lots from the main. This is also allocated to Centra. So there is other activities besides the trench, and most of -- and the pipe also is laid by the separate crews -- company crews, fused by somebody else.

So, we were looking into trying to integrate the whole installation together. So, some of this costs will be optimized. And especially the trench costs, which is here, came from a contractor was doing it on an hourly rate. So we feel there is the potential of optimization in the trench costs, or joint use trench costs.

MR. BOB PETERS: Mr. Aziz, how many main extension programs does Centra have already installed, using the four-party trench systems?

MR. AZIZ AZIZ: Like I would say in the neighbourhood from, the exact number I don't recall, but maybe all -- most of the subdivision and the City here is going four-party trench and some in Brandon and some in the rural area, if we have -- if there is any potential of four (4) trench, but the total will be in the neighbourhood between fifteen (15) to twenty (20) subdivision or -- or main extensions.

MR. BOB PETERS: Are those that are -- is that how many have already been completed?

MR. AZIZ AZIZ: That's right.

MR. BOB PETERS: And how many are on the drawing board?

MR. AZIZ AZIZ: It will be -- like I don't have the exact number, but I expect if the same construction activities would take place, like, last year, would have maybe the same number.

MR. BOB PETERS: That is fifteen (15) to twenty (20) new ones?

MR. AZIZ AZIZ: Might be.

MR. BOB PETERS: Would the Board be correct in estimating the costs to date have been approximately 180 percent of the single-party trench, for all of the four-party trench programs?

MR. AZIZ AZIZ: Some of them would be more than that, and some of them would be less than that.

MR. BOB PETERS: Are you going to agree with me that at a 180 percent of the single-party trench is the average cost?

MR. AZIZ AZIZ: Between a hundred and eighty (180) to two hundred (200), yes.

MR. BOB PETERS: Is it Centra's intention -- contention, Mr. Aziz, and, Mr. Warden, that the gas ratepayer should absorb the higher costs of the four-party trench program if the saving is never achieved through any optimization?

MR. AZIZ AZIZ: I think as for any new technology or -- or for any new approach is really -- is going to -- I expect it to cost in the beginning more, but our goal is to achieve cost savings and also other benefits because we said there is other benefits, they can actual achieve as -- as with our direct to dollar today, but it might cost lots of dollars in the -- in the future, as Mr. Case mentioned in his testimony.

For example, road rehabilitation, we don't have no services in the roads. So down the road, twenty/thirty (20/30) years if there is any road rehabilitation so it wouldn't cost the gas customer any dollars or any -- it wouldn't cost any -- anything to the gas customers in the future.

So, we have to keep this also in mind.

MR. BOB PETERS: Has the Corporation made a decision that it's going to use four-party trench regardless of whether it's cheaper or more expensive for gas consumers going forward?

MR. AZIZ AZIZ: We're still in -- in -- under review because of we're looking into the optimization. Where -- optimization will be submitted to the sponsors or executive which will make a decision if this is the way to go or not.

MR. BOB PETERS: And when does that optimization review have to be completed, Mr. Aziz?

MR. AZIZ AZIZ: We're in the process right now and I think I would say to be on the safe side, by the end of this year.

MR. BOB PETERS: By the end of 2005?

MR. AZIZ AZIZ: That's right.

MR. BOB PETERS: And at that point in time, can this Board expect Centra to be in a position to quantitatively demonstrate that the project will either go forward or be discontinued?

MR. AZIZ AZIZ: I would say, yes.

MR. BOB PETERS: Mr. Warden, if the four-party trench, I'll call it a pilot program, I'm not sure if Mr. Aziz would agree, but this four-party trench program, if it's not successful in achieving the optimization, will the project be abandoned and go back to the single-party trench for the gas customers?

MR. VINCE WARDEN: Well, I think as Mr. Aziz has indicated, we would have to look at all the factors before we came to that conclusion. But there -- certainly the financial benefits or lack thereof would be one (1) consideration.

We would look at other factors as well.

MR. BOB PETERS: All right. So if this Board decides that it wants a report from the Company on this by year end, that's something that the Corporation would expect to be in a position to provide?

MR. VINCE WARDEN: Well, you know, I'm -- based on Mr. Aziz's schedule, I would expect there would have to be some time for an internal review of that before we were -- would present it to this Board.

But I would think shortly there -- if Mr. Aziz's timeframe of the end of 2005 is -- is met I would expect shortly thereafter we would be able to file something with this Board, yes.

MR. BOB PETERS: Thank you. Mr. Chairman, with that answer, those complete my follow-up questions with this Panel and I have nothing further and thank them again for their answers.

MR. BOB PETERS: Thank you, Mr. Peters.

One (1) last question for Mr. Case: With respect to this difficulty getting into properties to read meters; does this include rental properties?

MR. DAVID CASE: Yes, sir. It would.

THE CHAIRPERSON: Does your ability increase when the tenants are changing or can the problem persist through a succession of tenancies?

MR. DAVID CASE: I don't think I can answer that with any accuracy. I don't know that we have that breakdown.

THE CHAIRPERSON: Does this problem account for a material portion of the unaccounted for gas?

I presume it's one (1) of the factors?

MR. DAVID CASE: I'm not sure how much of a factor this would have in unaccounted for gas. I -- I would be surprised if it's a major impact on it.

THE CHAIRPERSON: You'd indicated before that somewhere -- the estimates were over and some were under?

MR. DAVID CASE: Yes, that's correct. Those estimates, if you think of the -- relative to the magnitude of natural gas that's put through out systems, it would be relatively -- relatively insignificant though.

MR. BOB PETERS: Okay. Thank you, Mr. Case.

Ms. Murphy, do you have any re-examination of this Panel?

MS. MARLA MURPHY: No, I don't.

THE CHAIRPERSON: Then we want to thank the Panel for your evidence and your participation and the way you went about it. Thank you very much.

(PANEL STANDS DOWN)

THE CHAIRPERSON: We'll now move to CAC/MSOS' witness, Mr. Matwichuk. I understand that there's a possibility that CAC/MSOS will move up to the tables in front of us, if that's possible. Thank you.

(BRIEF PAUSE)

THE CHAIRPERSON: Mr. Saxberg, do you

want to introduce your witness, and then we'll have Mr. Hollis perform his duties and we'll get under way.

MR. KRIS SAXBERG: Thank you, Mr. Chairman.

Just before I do that, one (1) minor housekeeping matter. During my cross-examination I was referring to CAC/MSOS/CENTRA-15, and I'd provided copies to everyone. I'd like to mark that as an exhibit for the record. And I believe that would be marked as CAC Exhibit number 8.

THE CHAIRPERSON: Mr. Singh suggests it's number 7. Mr. Singh has corrected his. So, so be it, number 8.

MR. KRIS SAXBERG: Thank you.

--- EXHIBIT NO. CAC/MSOS-8: CAC/MSOS/CENTRA-15.

MR. KRIS SAXBERG: Seated to my left from Calgary, but originally from Virden, Manitoba is Greg Matwichuk, and he is ready to be sworn in.

THE CHAIRPERSON: Mr. Singh...?

GREG MATWICHUK, Sworn:

THE CHAIRPERSON: Thank you, Mr. Singh.

Mr. Saxberg...?

MR. KRIS SAXBERG: Thank you, Mr. Chairman.

EXAMINATION-IN-CHIEF BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Mr. Matwichuk, you are responsible for the preparation of certain written evidence in the form of Exhibit CAC/MSOS-2; is that correct?

MR. GREG MATWICHUK: Yes.

MR. KRIS SAXBERG: And you've also, in addition to -- to your primary evidence, provided answers to Information Requests in the form of PUB/CAC-5-1 to 13, and CENTRA/CAC-5-1 to 4, and RCM/TREE/CAC/MSOS-2-1 to 4?

MR. GREG MATWICHUK: Yes.

MR. KRIS SAXBERG: Do you have any changes that you'd like to make to that evidence?

MR. GREG MATWICHUK: Yes, sir, I do. Mr. Chairman, if I might, there are some minor corrections that I would like to put on the record, just to make sure that the evidence does flow. It --

THE CHAIRPERSON: Yes. Just first, has anyone got any problems with accepting this Witness as an expert witness?

Please continue.

MR. GREG MATWICHUK: Thank you, Mr. Chairman. On page 1 of CAC/MSOS-2, which is the -- my main evidence, which I -- I have a few minor changes I'd like to address.

Page 1, line 27, the sentence begins:

"From the outset the."

It should read:

"From the outset of the Acquisition Proceedings."

Then it goes on.

And then it -- it goes on to read that:

"It is my understanding that Hydro committed to the Board that the synergy savings from the acquisition would offset the costs of the acquisition, integration costs and related financing charges."

Now, throughout my evidence I referred to those as a defined term called "acquisition costs," and I'd like to define it right there. So, right after financing charges, if we could insert acquisition costs in quotes.

And you'll see up on page 2, at the end of that first paragraph is one (1) example where I use it as a defined term.

The next change is at page 3, line 22. And -- oh, I'm sorry, page 2 -- page 3, sorry, line 7. And there's a -- a redundant word in the first line it says:

"Therefore, even under COS, an appropriate transfer..."

And it says "made", and that word should be struck, because thereafter it says:

"...can be made."

Then at -- and I did miss one, I'm sorry, at page 2 at the bottom of the page there's a reference to "Table 1" and in response to an IR Centra/CAC/MSOS-2, Attachment 1, a revised Table 1 was provided and I just wanted to point that out, that there is a Table 1 revised as part of CENTRA/CAC/MSOS-2 Attachment 1.

And for my purposes I always insert the revision. You may wish to do so as well to assist in following along.

Then at page 5, line 12 -- in line 12 there's a sentence that begins:

"Nevertheless the caution at this point is that if the acquisition took..."

And we should insert the word, "place under COS," to make that a complete sentence.

And following that at page 11, two-thirds down the page there is a -- a double indented quote. And I just wanted to make sure that we had a footnote for that quote and that is Order number 118/03.

Page 12 at line 18 there is a Table 5 and I believe Mr. Saxberg has handed out Table 5, revised. And this arose out of changes that were made on the record by Centra with respect to the last column there, "equal annual amount of acquisition costs."

My understanding from the testimony to date that there was a fair bit of confusion emanating from the previous proceeding and the Board Order as to what amount was going to be the -- the amount we're measuring against.

And that, in my evidence, I use the 20.9 which came from Centra's evidence in a previous proceeding and the Board Order 118/03 that and as well as IR responses in this proceeding.

I understand from oral testimony that number now should be looked at as 18.8 million or thereabouts and as a result I have revised Table 5 to reflect that change.

MR. KRIS SAXBERG: With the Board's permission I'd like to mark that document, headed Table 5 revised, as CAC's next exhibit, which would be Exhibit 9?

THE CHAIRPERSON: Very good.

--- EXHIBIT NO. CAC/MSOS-9: Revised Table 5.

MR. GREG MATWICHUK: Thank you, Mr. Saxberg. Then on Table -- sorry, on page 15 there's another minor correction. That's page 15, line 15"

"The Board's past rulings and much of the foregoing analysis."

And then we should insert:

"Both use RBROR methodology for regulation."

So the reference to both obviously is past rulings and foregoing analysis. Okay. Then page 18, line 10, again we have a duplication of words. Line 9, it begins "essentially," and it follows it says:

ôCentra's current filing essentially..."

So we can eliminate the second

"essentially". ôWe've essentially dealt with that.

And one last one in this main body of evidence, page 19, line 9, and under line 9 there's Table 8 and, again, this is just to reflect that there was a revised Table 8 in response to Centra/CAC/MSOS-2, Attachment 2.

Mr. Chairman, I just have one (1) other

item and it's in an IR response. And hopefully I will get the exhibit number right; CAC/MSOS-5-1, and that is a response to Centra/CAC/MSOS-1. And in the response, on the second line, the sentence towards the end of that line:

"I am not aware that it is not a comparison."

That second "not" should be removed so that it reads:

"I am not aware that it is a comparison that has been prescribed by the Board."

Mr. Saxberg, those are all my changes.

MR. KRIS SAXBERG: And with those changes, Mr. Matwichuk, do you adopt that evidence in its entirety?

MR. GREG MATWICHUK: Yes.

MR. KRIS SAXBERG: Could you identify your qualifications from the perspective of the evidence that you are intending to cover?

MR. GREG MATWICHUK: Yes. Thank you, Mr. Saxberg. Mr. Chairman, I've had the pleasure of testifying before at least one (1) of these Panel Members but -- but not you, sir. And on that basis I would just briefly outline my background for you.

I'm a chartered accountant with the firm of Stephen Johnson in Calgary. The firm and its principals have been operating for over twenty (20) years and all that time have specialized in regulation of -- of utilities. Prior to this, the founders of the firm were members of a large national firm that -- who, in so doing, were conducting their utility practice with that firm.

As for myself, I've been involved in utility regulation in jurisdictions across Canada for over twenty (20) years. And our firm has practiced in every jurisdiction that is regulated across Canada on rate regulation except for PEI.

We've worked in -- in matters, usually financial in nature, with respect to utilities, and that includes gas, LDC's, electricity at all levels, pipeline, whether that's gas or -- or crude oil, telecom, and even milk when it was regulated in Alberta.

While our work is often based on the examination of matters with respect to revenue requirement, we also provide expertise in other areas of utilities, including cost allocation and rate design.

I've written evidence on numerous issues and have testified in -- in Manitoba, Alberta, British Columbia, Ontario and also before the CRTC with respect to telecom matters. I'm familiar with Centra, West

Coast, its predecessor owner, and -- and Manitoba Hydro. Since 1993 I've advised counsel for CAC/MSOS in various proceedings, including GRA matters, cost of gas, rural gas expansion, feasibility studies and so on.

I've testified before this Board on -- on previous occasions, dealing with non-gas revenue requirement, integration and -- and the no-harm issue, predominantly.

In the integration proceeding, provided a baseline methodology to help the Board assess synergies and O&M costs. In that evidence that I provided the opportunity to review synergies and O&M costs on a cost-per-customer basis so that it would include growth and inflation as well as productivity.

My approach was to use that to determine where a starting point and an end point might be for -- for O&M costs. As well, in the 2003/04 GRA there was a similar analysis as well as a -- analyses on various elements of -- of revenue requirement.

Besides utility regulation, our firm still maintains a public practice in accounting. We take on assignments dealing with various non-utility matters and often we may require written and oral testimony before a tribunal or even before a court of law.

If you wish any further details about my background, Mr. Chairman, Panel Members, I have my CV, or I can respond to any questions in that regard.

MR. KRIS SAXBERG: Mr. Matwichuk, have you testified in other proceedings on the subject of the no-harm principle?

MR. GREG MATWICHUK: Yes, I have, Mr. Saxberg. Outside of this province, testified in no-harm with respect to acquisitions taking place in Alberta and British Columbia.

MR. KRIS SAXBERG: Having already been qualified as an expert for the purposes of providing testimony in this proceeding, Mr. Matwichuk, could you describe the purpose of your evidence?

MR. GREG MATWICHUK: The purpose of this evidence, Mr. Saxberg, was to examine the costs in the GRA Application, to determine whether there's a -- a need for an amount to be transferred to Manitoba Hydro from Centra. And if there is such a need, what is the level of that amount that should be transferred, what is the quantum.

And how should that quantum be treated in the revenue requirement of Centra.

MR. KRIS SAXBERG: That being the purpose, could you please describe, in summary form, what your evidence is?

MR. GREG MATWICHUK: Well, at a high level, Mr. Chairman, when I look at the evidence provided by Centra and Centra's restatement of its evidence, including revisions and amendments, I'm -- and including, I'd now like to believe that Hydro has calculated an $18.8 million amount of its annual cost for acquisition and integration.

But setting that aside for the moment, whether Centra needs to be engaged in any of that cost, what portion need it be engaged in? And from my perspective, my analysis shows that the Board came up with a plan to handle that in Decision 118/03.

And my evidence shows that -- using the Board's plan, that a contribution can be made to retained earnings of Centra, and there is more than enough that is available to be transferred as well, together with the synergies in Hydro, to cover the costs of the acquisition and integration.

Now without going into whether we're dealing with rate base rate of return or cost of service, at a high level, if Centra had $12 million of net income, it could distribute $10 million to Hydro, and retain $2 million for retained earnings.

And then we see that a number of objectives are being achieved. The $10 million, when combined with the $9 million of synergies in Hydro, would more than cover off the $18.8 million that was calculated as acquisition costs. Right there the Board's plan would be achieved.

Now the Board provided a plan or a formula for recovery of those costs, and I -- I tend to refer to it as the Board's plan, acquisition costs plan, and it's a long term proposition. And it would appear that the Board was looking for balance when it made that decision, in that there -- they were attempting to ensure that there were no harm to either gas or electric ratepayers.

Now the second objectives being achieved, and that is Centra's objective, is leaving aside, for the moment, how much is actually necessary. What the $2 million allows for Centra to achieve a one point one (1.1) times interest coverage. And it would appear, from the evidence, when I was authoring this particular evidence, that that was a reasonable target. In fact, it's probably more than generous in my view. And we can -- we can discuss that if you'd like, sir.

And prior to today I -- I had understood that Manitoba Hydro's target was one point one (1.1) times interest coverage, and that Centra had similar financial targets. And the reference for that is response to PUB/CENTRA-59.

Now, the -- the $2 million amount retained in income, I understand that's what Centra had asked for in its previous GRA as well. And, Mr. Chairman, just to take a moment to elaborate a little on that, I think what we can use as an anchor for that is the response to PUB/CAC/MSOS-1, which is Exhibit CAC-5-1, CAC-MSOS-5-1.

And attached to that response is a table which is entitled, Comparison of Revenue Requirement under COS and RBROR Cost of Service and Rate Base Rate of Return and Recommended Non-Gas Revenue Requirements.

And what you see there, Mr. Chairman, for each year are the revenue requirements as applied by Centra and what it might look like under cost of service and what it might look like under rate base rate of return.

You'll notice from my evidence, Mr. Chairman, that I use rate base rate of return as a highwater mark, so to speak. And it's a standard or an anchor. So if we could start, as an example, with 2005/06, and I won't go through all the numbers, but suffice it to say that the amounts under rate base rate of return once, what I consider the appropriate adjustments to be made, ends up being 121,868,000.

So just under the premise of it being the highwater mark, if the Board wanted to move over to cost of service, then how would a transfer amount be achieved?

Well, certainly under rate base rate of return the Board has spoken and said, Please use return on rate base equity component, i.e., the return on equity, which on this Table is at Line 11 for each of the test years.

And those amounts are the amounts provided by Centra in its evidence and there's not much dispute about those amounts, Mr. Chairman, because those amounts are determined by a formula and that's this Board's formula. And that formula is -- is consistent with other formulae across the nation that other regulators have developed as well to maintain a very objective way of deriving return on equity.

So, as I say, with rate base rate of return, the return on equity is set and that that was the Board's intention, and certainly as I read it, and it seems certainly as -- as Centra read it from what I can tell from their evidence, that that was the amount that was to be available to Hydro to be combined with their synergies to offset the acquisition costs.

But then turning to cost of service, again, using the rate base rate of return as an anchor point and going to the bottom, Line 17, if we take the rate base rate of return revenue requirement of one hundred and twenty-one thousand eight hundred and sixty-eight (121,868) over to the cost of service and work back, we can see that by providing Centra at Line 14 with one point one (1.1) times interest coverage which is, again, in my view, more than reasonable given the circumstances, and as well we can fit under that standard approximately $10 million of additional income that is available for -- to be transferred to Manitoba Hydro.

And so what you end up with is approximately $12 million of income and it's a two (2) and ten (10) split, two (2) to be retained by Centra and ten (10) to be available to Manitoba Hydro.

And I apologize, Mr. Chairman, in advance. I may inadvertently say Ontario Hydro when I mean Manitoba Hydro and that just comes from -- from past experience working with Ontario Hydro so much. But it certainly is my intention to use the appropriate terminology.

So, this table, Mr. Chairman, is a -- a summary of my evidence in terms of how the Board's objectives can be achieved. Electric ratepayers are left harmless and gas ratepayers are left harmless.

MR. KRIS SAXBERG: Mr. Matwichuk, have you done an analysis with respect to amounts that have been transferred from Centra to Manitoba Hydro in the past to offset or cover the acquisition and integration costs?

MR. GREG MATWICHUK: Yes, Mr. Saxberg. In my evidence on, I'm just turning to it, page 14, there is a Table 7 which is entitled, Amounts Collected in Centra Revenue to the Benefit of Hydro, and what this table shows is that there are three (3) elements that are available to the benefit of -- of Hydro.

And I think based on the -- the testimony I've heard today and -- and read in the transcript, I think we've got to step back a moment and -- and talk about each of these items.

Certainly, net income is an amount that is earned after all other costs have been taken care of. It's the residual. That is the amount that the owner decides how much will remain in the company and how much will be removed through either a distribution or a dividend.

And I think a poignant example of that, particularly in this context, because what I -- what I've heard is that the net income must reside in Centra, and I -- I must vehemently disagree with that. Net income is the owner's entitlement; the owner decides how to deal with that.

And the poignant example I'm referring to is Manitoba Hydro. When it had sufficient net income, the Province at one point decided, Well it's time to remove some of that net income. And there was a distribution in excess of $200 million from Manitoba Hydro to the Province.

So, it will be up to Manitoba Hydro as the sole shareholder of Centra to determine how much will be retained in Centra and how much will be dividend out or distributed to the owner, Manitoba Hydro.

Here, in this Table 7, the three (3) amounts that we're talking about that flow to the benefit of Manitoba Hydro, are net income and, obviously, if there -- there's a loss, that it's on a net basis; the synergy transfers; and corporate allocations.

So, historically this table looks at 99/2000 through 2003/04 and then, based on the information that was available at the time, '04/'05, '05/'06 and '07 -- '06/'07 were forecast amounts.

So what this table does is it says, How much are attributable to each of those three (3) items. And the net income -- well, the net income is the net income as stated, historically, and the amounts that were included in the forecast.

I'm not aware of whether we know what '04/'05 net income is to date but given the date of year, I -- I would think that we should know that pretty soon.

The synergy transfer, I understand that there's some debate with respect to the synergy transfer, as to whether that is an amount in or out and -- and whether it existed in any particular year. And I'm prepared to take -- take that debate on.

The corporate allocation, the information at the time was that in each and every year it was and was expected to be on a forecast basis, 15.1 million.

So, when I total all those up over those years, it's 138.7 million, it's the hundred and thirty-eight three (138683) at the bottom of the table. When I combine that with the synergies of $6 million a year in Manitoba Hydro, I get 185 million.

And over that same period the annual cost of acquisition using the 20.9 million as it was provided as evidence coming into this proceeding, is 160 million. And -- and the differential would obviously be 25 million.

Now, we can break these down -- amounts down and suggest that one (1) goes up and one (1) goes down, and we can deal with that in cross-examination if we have to do that. But generally speaking, sir, I don't think you'll find much change, that what we've got here is the amounts that flow to the benefit of Manitoba

Hydro.

And what I mean by that is, costs incurred by Centra ratepayers, and amounts that are recovered in rate revenue that are available for and under the control of Manitoba Hydro, or 138.7 million, and the costs of acquisition using the 20.9 million, for a 160 million.

I'm sorry, I left out the $6 million of synergies. So there was a -- a net benefit to Hydro of twenty-five point (25.) -- 25.0 million owed approximately over that timeframe.

MR. KRIS SAXBERG: Have you recalculated that analysis using the revised evidence with respect to the yearly impact -- or incremental cost of acquisition, borne by Manitoba Hydro Corporation -- corporate?

MR. GREG MATWICHUK: In direct, you have caught me off guard, Mr. Saxberg, because no I have not undertaken to do that, but, if -- if it's needed I can provide it.

MR. KRIS SAXBERG: Well, directionally, which way does it go?

MR. GREG MATWICHUK: Well, directionally with the reduced acquisitions costs, it would be a larger differential.

MR. GREG MATWICHUK: So, in your view, taking into account your analysis, have Centra Gas ratepayers paid their fair share of acquisition and integration costs on a historic basis?

MR. GREG MATWICHUK: Well, when you ask that question, Mr. Saxberg, I again look to the Board's plan. And the Board set out a plan as to how the costs of acquisition were going to be recovered.

And in terms of Centra's responsibility to recover those costs, Centra's contribution was the return on equity amount. And the -- these amounts exceed the amounts that would have otherwise been required under just simply return on equity. So, Centra has paid more than its fair share.

MR. KRIS SAXBERG: Thank you. I want to now ask you some questions that flow out of Centra Gas's rebuttal evidence. So, perhaps we could turn up collectively, Centra's rebuttal evidence, and in particular page 5 of 53.

MR. GREG MATWICHUK: And is that Centra Exhibit 2?

MR. KRIS SAXBERG: Now, you've stumped me. I can check.

That is Centra Exhibit 3.

MR. GREG MATWICHUK: Three (3). Thank you.

(BRIEF PAUSE)

MR. KRIS SAXBERG: On page 5 of Centra's rebuttal evidence, Centra indicates that:

"The parties are generally in agreement with respect to the no-harm principle."

Do you have any comments regarding that assertion?

MR. GREG MATWICHUK: Okay.

(BRIEF PAUSE)

MR. GREG MATWICHUK: And you are referring to lines 1 through 5?

MR. KRIS SAXBERG: That's correct.

MR. GREG MATWICHUK: Okay. I believe what Centra was referring to was that back on page 4, it indicates that benefits of the purchase should accrue to both gas and electricity ratepayers, and I think that the no-harm principles go further than that.

I have outlined in summary form, the no-harm principles under Q-5 in my evidence on page 4, so that's CAC Exhibit 4 -- or sorry, CAC Exhibit 2, page 4.

And there are four (4) main principles. 1, and I'll abbreviate them, is that customers of the acquired company -- acquired company are to be held harmless.

The no-harm standard means that those customers will be at least no worse off. And the test for harm, and I think this is critical too because it often gets lost in the shuffle, is that the test for harm is that we rely on the historic cost, i.e., what it cost when first devoted to public use?

And I think it's important that we pause on that because not only is that a principle that is adhered to across the country, it is enshrined in the statute under which this utility is regulated, I believe.

And I can't remember the section but if someone wants to ask me that I can go to it. So the salient parts of this is that -- oh, sorry, and the last -- I shouldn't miss the last one but it didn't seem to be an issue, is that the last principle is that not only should customers not be adversely affected from a rate or price point of view but they shouldn't be affected from a service point of view.

So, going through each of those principles, Centra is the acquired company and first and foremost its customers should be held harmless.

Centra's customers should be at least no worse off and it means that if there are some synergies that are to be found those customers may benefit from those synergies unless there are some extenuating circumstances and I'll get back to that in a moment.

The historic cost principle, that is -- is paramount because what it's saying is that we're looking at net book value to include in rates only. Nothing above net book value. And anything above net book value should be expressly prohibited from being recovered in Centra's rates; that's what that principle is saying.

On terms of service levels, I'm not aware of anything on the evidence that indicates that Centra has been adversely affected -- I mean, that Centra's ratepayers have been adversely affected.

Now, I mentioned extenuating circumstances with respect to the second principle of no worse off. And what I mean "extenuating," I mean "unusual." The case at hand is we've got one (1) utility with one (1) set of ratepayers purchasing another utility with another set of ratepayers.

And, yes, indeed, those are unusual circumstances. But, again, I go back to te Board's plan. The Board recognized these unusual circumstances. When I -- when I look at what takes place in other jurisdictions in terms of acquisitions, sales of major assets outside of the normal business operations of utilities, the Board has found balance between the two (2) utilities.

And to me that's -- that's -- it appear -- it appears to me that's why the Board did what it did. It came up with a plan or a solution of having Hydro benefit from the return on equity in Centra as the owner should, together with the synergies found in Hydro.

And when you put those two (2) together, they are in excess of the acquisition costs. As such, when you carry out that plan, the Board is not burdened by the issue of synergy sharing which we can get into later in my evidence, is essential because of the nebulous nature of the synergies.

ItÆs very difficult -- it's like trying to nail jell-O to the wall, in the vernacular. So, I view the Board's solution in that regard as simple and effective because it achieves the objectives, no harm to either ratepayer.

And just one (1) other point, Mr. Saxberg, I'd like to make on that is that it -- it can be achieved as I tried to outline in my response to PUB 1, it can be achieved through either a rate base rate of return or cost of service.

And we can get into that in terms of discussion about above the line or below the line and I think that discussion will be critical as we go forward.

MR. KRIS SAXBERG: Also on page 5, Mr. Matwichuk, Centra states their disagreement with you that electric ratepayers would be held harmless in the absence of the corporate allocation.

What are your comments in response to that?

MR. GREG MATWICHUK: That was on page 5 as well, yes. Yes. I -- I note -- note that Centra suggests that my conclusions are flawed because they fail to recognize the corporate allocation is the only allocation to Centra ratepayers related to costs incurred by Hydro to acquire and integrate, and absent the allocation all acquisition and integrations costs would be formed by electricity ratepayers.

Well, I disagree with that. And the reason is, is that when you carry out the Board's formula, electricity ratepayers do not incur the costs of acquisition. They're covered off by two (2) elements: the return on equity from Centra and the synergies in Hydro that resulted from the acquisition.

If Centra were to carry out the Board's plan, the acquisition costs would be recovered by those two (2) elements. And, as -- as I understand it, that is the way Manitoba Hydro anticipated when it replied to a response in its GRA.

Centra also acknowledges the BoardÆs plan in various locations in -- in its evidence. And I just wanted to -- if we could just move quickly to CAC -- Exhibit CAC/MSOS-9, which, Mr. Saxberg, you handed out earlier. And this is the Table 5 Revised I spoke about. And, as well, in my evidence, the premiss that I used for Table 5 is outlined on page 6 of my evidence, starting at page 5 actually, at the bottom, I say:

"There are three (3) components to analyse: Centra's return on equity, the synergies in Hydro and the amount of the acquisition costs."

So, I don't want to belabour this point but I just wanted to outline that this is -- this was the original premiss. On page 6 you'll see the arithmetic expression there that as long as Centra's return on equity and the synergies in Hydro are greater than or equal to the amount of the acquisition costs, then the Board's objective has -- has been achieved.

So, what Table 5 revised shows are the numbers attached to each of those elements.

And if we can just drop down to the -- the second set of numbers first, the "Centra's Equity Component 04/05/06" is in -- by the time we add all the equity components together, is in the neighbourhood of thirteen (13) to fourteen (14) million.

The synergies in Hydro, as we've heard new testimony in this proceeding from Centra, are nine (9) million. The sum of those two (2) provides a range of 22 million to 23 million, which, in my addition, are greater than the 18.8 million of acquisition costs.

And I won't belabour the rest of the narrative in this, other than to say that on the second page there's an example that -- which is important. And we can draw on -- in a later discussion, is -- in the second paragraph:

"If Hydro were to have acquired a utility in another jurisdiction..."

In a similar fashion, the way Nova Scotia acquired a US utility or UtiliCorp from the US acquired West Crude and Power (phonetic) in BC.

"...the regulator of the acquired company would not allow nor did they allow customers of the acquired companies to pay for any part of the acquisition rates."

And I provide other examples in -- in another response to -- to the Board, PUB/CAC/MSOS-7, I was asked to give examples where regulators did not allow recovery of fair market value adjustments in goodwill and rates. I'll leave those for the record, unless I get questions on that.

But just to use that example, in Manitoba's situation, the Board has similarly spoken. Hydro should use the income it derives from the utility, to which it's entitled as the investor, and combine it with the synergies.

And as -- as I noted in -- in terms of the acquisition, it was Hydro that initiated the acquisition. Centra's ratepayers did not make the request, and when -- when I look at it, Mr. Chairman, on a high level basis, even if there were some incremental amounts that did not -- were not recovered by the Board's plan, the differential in handling it in Centra versus Hydro, is probably a factor between five (5) and ten (10).

In other words, because of Hydro's size, it can absorb much greater differential than Centra could, in terms of rate impact to those customers. I don't think we can see it in the -- you know, third or fourth, fifth decimal place for Manitoba Hydro, whereas it would be much more of an impact in Centra.

And I think that's something that the Board recognized in terms of the size factor as well. Sorry, for that long winded answer.

MR. KRIS SAXBERG: Mr. Matwichuk, on page 6 of the Centra rebuttal evidence --

OBJ MS. MARLA MURPHY: Mr. Chairman, I'm sorry to interject, but I'm having a bit of an issue with the approach to this line of questioning. There's a bit of a quirk in the process here, in that Centra filed its rebuttal evidence in advance of when the Intervenors come to testify.

And in theory, Centra's rebuttal evidence is the last word on these topics, and I appreciate that it crystallizes some of the issues. But if Mr. Saxberg is proposing to go page by page and line by line through that rebuttal evidence, and in essence give rebuttal to rebuttal, I wish to make an objection to that.

THE CHAIRPERSON: What's your plans, Mr. Saxberg?

MR. KRIS SAXBERG: Well I am going to continue on and put the rebuttal to Mr. Matwichuk and ask for his -- his view on the matter. And the reason I'm going to do it that way is because there's been a long history in these Proceedings of approaching the Intervenors' response to Centra's rebuttal evidence in that fashion.

And it's something that, in past Proceedings, this Board has allowed from Intervenors. And I think that it's -- it's information that's useful to the Board, because it does focus attention on the --

on the main differences between parties to do it this way.

THE CHAIRPERSON: You can't phrase your questions in another way?

MR. KRIS SAXBERG: Well I can phrase them in other ways, and --

THE CHAIRPERSON: Without referring to the rebuttal evidence?

MR. KRIS SAXBERG: Sure. I mean, it accomplishes the same -- the same from -- from my perspective, and so if that's the Board's --

THE CHAIRPERSON: You should be able to draw out your points taking that approach I would think.

MR. KRIS SAXBERG: Well, let me try it that way.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: In this Proceeding Centra has revised its evidence as to the location of synergies within each of the respective organizations. Has that revision of evidence impacted your evidence, Mr. Matwichuk?

MR. GREG MATWICHUK: Mr. Saxberg, when I originally embarked on this evidence I understood that there was to be $6 million of synergies allocated to

Hydro. And since I -- since the time of writing the evidence, I understand that actually $9 million of the synergies were being allocated to Hydro.

To me that solidifies the point that is being made, and that is that with the return out of Centra and the synergies in Hydro that the cost of acquisition can be carried out -- can be covered off, sorry, and recognize that the synergies are becoming increasingly difficult to segregate, measure, track.

And I think what the -- when I -- when I look at the synergy -- the history of synergies going back to the 1999 purchase proceeding, they originally estimated to be between twelve (12) and fifteen (15) million and that's what we saw in the purchase proceeding.

At the integration proceeding there was even a wider range of ten (10) to sixteen (16) million and eventually settled on something like fifteen (15) million. In the 03/04 GRA, the last time I was here, there were two (2) or three (3) renditions of what the synergies would be and how they would be allocated.

Then we came to the 2005 interim ex parte where we heard that there was a ten (10) and six (6) division between Centra and Hydro and -- for a total of sixteen (16) and now we find that there's a seven (7) and nine (9).

So, it seems to me that it -- it's never a hard number and the further we go out the more difficult it's going to be to -- to measure and so I would suggest that we get a handle on that number quickly here and -- and deal with that matter of allocation.

MR. KRIS SAXBERG: Is the $7 million synergy estimate, that is the estimate of synergies within Centra of $7 million; is that a reasonable amount in your -- from your perspective?

MR. GREG MATWICHUK: Well, as I said in my evidence, I have a bit of a problem with -- with the allocation of -- of the sixteen (16) million because if, in fact, there are sixteen (16) million, I take a look at the two (2) companies and how very different they are in operations and size, in particular, and just based on size it's intuitive and -- and, sorry, combine that with the cost allocation model that's used, that the costs do get allocated to each entity.

One would intuitively think that the costs are -- or I should say that the synergies follow the costs and we could, if we had enough information, we could do that calculation.

But on this record, I'm not aware of sufficient information to do that cal -- specific calculation. I look back in history and the synergies that were expected to be found in Centra seem to be getting lower and lower and that comes as no surprise. It's a smaller company. Smaller -- much smaller customer base. With a larger customer base it's far easier to -- to achieve those synergies that -- as the customer base that Hydro has.

So, I'm not confident in the fact that -- or in the proposition that the proportion of synergies attributable to Centra are seven-sixteenths.

THE CHAIRPERSON: But your view is based basically on, sort of, intuition in a sense; just sizing up the two (2) companies?

MR. GREG MATWICHUK: Mr. Chairman, yes. I mean, that's the first part is that the relative size of the companies and the fact that the costs are originally recorded in Manitoba Hydro and then are allocated out based on various cost drivers.

So when you think of various cost drivers, you think of the number of customers, floor space, number of computers, you know, those types of cost drivers that are typically used in cost allocations.

And if you put your mind to it you think of those cost drivers in each of the companies, the relative amounts will likely bear out that the drivers for Centra will be substantially smaller than seven-sixteenths, i.e., about half.

And -- and given that the costs are first recorded in Manitoba Hydro and then are -- are parcelled out based on those cost drivers, one would expect that the synergies should follow those cost drivers as opposed to certain costs, certain synergies. And that -- that's on a -- a global perspective.

MR. KRIS SAXBERG: What's the -- what's the upshot if synergies are not properly measured within the Centra organization?

MR. GREG MATWICHUK: If the synergies are not as they were expected in -- in Centra, that means that there's less of a benefit that's flowing to the Centra customers. And the -- the costs may not be borne out in -- in reality, relative to what they're forecast.

MR. KRIS SAXBERG: And the Board's heard evidence in these past few weeks from the Centra Panel that rate -- Centra ratepayers should pay a contribution towards the acquisition and integration costs because they are enjoying benefits flowing from the transaction; do you agree with that?

MR. GREG MATWICHUK: Well, there's a general principle that -- and -- and Centra dealt with this and I -- I believe it's, you know, it's generally fair that when you enjoy benefits, then there are costs to enjoying those benefits.

But here we have both sets of ratepayers enjoying benefits and both sets of ratepayers, to the extent possible -- and I'm quoting the Board again -- to the extent possible, should be held harmless, and I'll return to that. But both ratepayers will be held harmless if we continue to follow the Board's plan.

But an overriding principle in this particular situation is that the customers of the acquired company must be at least no worse off. Because we must -- we must stick with historic cost and when -- when first devoted to public use.

If we introduce costs of -- historic costs like goodwill or market value write-ups, which is essentially what Hydro and -- and Centra have attempted to do in various renditions since the -- the acquisition, then we'd be violating those principles. And, again, my simple reading of the governing statute is, is that we -- we shouldn't be embarking on that route.

Now, the risks and benefits of the acquisition should occur to the acquired company. And so if Centra customers are to be held harmless and do not receive any additional benefit, then the potential risks should accrue to Hydro, based on it having initiated the transaction in the size alone, and I would significantly mitigate against any individual ratepayer impact.

The significant risk that gas customers would be worse off with Centra's current application relative to the new -- new acquisition, that's very difficult because that may or not have -- have happened. If you wish to explore that further, that's fine.

But if both sets of customers are to be held harmless, then any benefits that happen to accrue to Centra, which would be relatively minor in the scheme of things for Hydro, it would be appropriate for those benefits to remain with -- with Centra. But I -- I am making the proviso that as long as both sets of customers remain harmless.

MR. KRIS SAXBERG: Do you have any -- do you have any concerns with the Board ceding to Centra's request to switch from rate base rate of return regulation to cost of service regulation?

MR. GREG MATWICHUK: Well, yes I do have some concerns, Mr. Saxberg. Now, I -- I understand that there are some motivations to at least consider the -- the cost of service methodology. And this, I -- I should say that, you know, it has been used, has been tested in various jurisdictions across Canada. It is typically the case where there is very little equity component.

When I first got introduced to regulation it was with Ontario Hydro and it had in the neighbourhood of five (5) to 10 percent equity, and it was regulated on a cost of service basis.

Centra -- and we'll get -- probably take time to get into this, but Centra is a stand alone regulated utility. We are here to regulate the gas rates that Centra provides its ratepayers. We're not here to -- to determine combination electric and gas rates. We're not here to evaluate a consolidated entity. These rates are going to be determined for a stand alone gas company for its customers.

But getting back to the issue of cost of service, the only differential between the two (2) essentially -- well there are differentials, there's in terms of no tax, no return on equity, but in replacement for that return on equity is a net income number.

So, one (1) -- I mean one (1) is a substitute for the other. And it's all a matter of how you come up with the net income. One (1) objective way jurisdictions have used in cost of service to come up with a net income is to use a -- an interest coverage. And -- and to adhere to it pretty strictly.

What I see in -- in Centra's Application, if we go to cost of service, is that it's debt income amounts are going to exceed -- well, in the first year exceed one point two (1.2), and in the second year, I -- I don't have a figure in front of me, but I think upwards of one point four (1.4) or one point five (1.5) times interest coverage.

And I mean I view that the one point one (1.1) is excessive and -- and there are a lot of reasons for that, or there are reasons for that I should say.

The -- the rate of return in return on rate base, there is an objective way to establish the net income amount. And the Board, like other Boards in Canada, have a formula. And that formula has -- was established in a 1995 decision by this Board, and it emulates -- actually, I should say others emulated Manitoba Hydro, because I think Manitoba was one (1) of the -- were the first to come up with a formula. But very similar to other formulas across Canada.

And those -- those formulas have been -- had the test of time, had the test of intervention, have been reviewed at the National Energy Board level, Ontario Energy Board Level, BCUC has also reviewed its. And whole they may have tweaked it a little, it's essentially the same formula that they started with. And -- and Manitoba Hydro -- or sorry, Manitoba PUB's formula is -- is -- has remained the same. It's a very objective way to determine the net income amount.

If the Board wanted to go to cost of service, the net income amount, there's got to be a similar objective way, or rather than just relying on management's judgment, because management's judgment is not something that's very easily tested in this regulatory format. Certainly compared to a formula approach.

Now Centra has, in terms of its -- its cost of service, as I mentioned there's no income tax component, they each have debt financing, they each have a net income component. One's -- one's explicitly net income, the other's referred to as return on equity.

In Centra's case, they've -- besides the net income they've dealt with a corporate allocation, and I'm sure we'll address that in greater detail.

I'm not sure if that answers your question there.

MR. KRIS SAXBERG: Well, ultimately, are you recommending any particular form of regulation?

MR. GREG MATWICHUK: Oh, yes, sir. Mr. Chairman, Centra has been regulated on a rate base rate of return. Centra continues to have a capital structure akin to its capital structure before it was owned by Manitoba Hydro. There's -- there's no getting around that; that's what exists.

Manitoba Hydro is the shareholder, and has full ownership of the share equity, $121 million, in Centra. That's what it says in the audited financial statements of Centra and that was the result of the purchase.

Centra has been regulated on rate base rate of return. It is a -- continues to be an objective way to determine a fair return. And what I mean by a fair return, Mr. Chairman, it provides for a fair return and there's lots of jurisprudence and in terms of the courts it's been tested throughout history and before regulators. It has been exhaustively addressed by academics and experts who have been before this -- this regulator and others.

And has been determined to be a way to achieve fairness. A fair return that allows for recognition of risk and that risk is the risk of fluctuating cash flows.

And the risk -- there are risks of Centra and there are risks of Manitoba Hydro. They're very different and that's why I would tend to think that this Board would regulate them on different bases.

And, Mr. Chairman, what I'm advocating is that while there may be a temptation to go to cost of service simply because the -- the owner is a Crown Corporation, based on what the Board has set out as its plan to handle the acquisition costs based on how Centra has been regulated, based on the ability to objectively determine a fair rate of return to -- to Centra's owner, I'm suggesting, sir, that rate base rate of return would continue to be the superior method of regulation for this entity.

MR. KRIS SAXBERG: Do you have any comments with respect to whether or not the net income requested in the 2006/07 test year is a fair amount of net revenue?

MR. GREG MATWICHUK: I addressed this a bit in my evidence and -- but more particularly in response to PUB-1. And this is on the second page of that response and what I -- I did was I had assumed that a starting case that there would be one (1) times interest coverage.

In other words, thatÆs before net income. And the reason I did that largely was that Centra -- interest coverage is -- is an attempt to provide some kind of -- of cushion for some risk as well and to allow for retained earnings to be maintained or enhanced.

But why would we do that? Well, we would do that if there were -- if Centra, as the entity, was exposed to significant market risk such as going to the capital markets.

Centra is no longer exposed to going to the capital markets post the purchase. Yet, in return for paying a debt guarantee fee it receives investment through debt through Manitoba Hydro.

Now, what I'm unclear about is whether those are the rates that are mirrored down from the province or whether there's an increment in there. I'm not sure that there's evidence on the record to confirm or deny that.

But Centra's risks are essentially taken care of through the debt guarantee fee. And this is recognized in the financial community. The last time that DBRS had a debt rating or a credit rating, I should say, on -- on Centra was February 2002.

And in that report it stated that while there may be some of the key ratios that they look at, are not as good as they should be, DBRS says, We're not that concerned about it because they have a debt guarantee. And -- but Centra's ratepayers pay that debt guarantee fee to -- to acquire that guarantee. So there's a -- there's a quid pro quo there.

And, as a result, DBRS, as a major bond rating company, has said, We're not so concerned and therefore we will give Centra what they call a flow-through rating. So whatever Manitoba Hydro's rating is, Centra gets it too, regardless of diminishing or -- or degradating ratios.

So in terms of net income enhancing retained earnings, there's a lesser emphasis on it, diminished importance, because Centra's got protection through the debt guarantee and Centra's ratepayers have paid for that protection.

So, therefore, when you look at another entity that might be on cost of service and they, you know, were not subject to debt guarantees, didn't have that benefit, they probably need some more coverage. But Centra doesn't, in this case, require that coverage.

THE CHAIRPERSON: Mr. Saxberg, do you think we could have a short break now?

MR. KRIS SAXBERG: Yes. I think it might be a good time.

--- Upon recessing at 2:55 p.m.
--- Upon resuming at 3:15 p.m.

THE CHAIRPERSON: Mr. Saxberg, you can commence at any point.

MR. KRIS SAXBERG: Thank you, Mr.

Chairman.

CONTINUED BY MR. KRIS SAXBERG:

MR. KRIS SAXBERG: Mr. Matwichuk, Centra Gas says that even with the inclusion of a $15 million corporate allocation, Centra ratepayers are benefiting -- benefiting to the tune of about $9 million, in comparison to the way the world would have unfolded, had there not been an acquisition; what -- what are your comments?

MR. GREG MATWICHUK: When I looked at Centra's calculation, that's, I believe -- when I was looking at anyway, was at page 14 of the rebuttal. And I think it's been addressed in a couple exhibits this morning.

And overall, what page 14 of the rebuttal shows, is a calculation of differential between what Centra has applied for, and what Centra has suggested might have happened absent the acquisition.

Well, first of all, I think the starting point is highly speculative in terms of what might have happened absent the acquisition. And I think I'd like to address it this way, Mr. Chairman, is that what West Coast may or may not have done seven/eight (7/8) -- eight (8) years down the line, since it sold Centra, it would be very, very difficult to determine.

And to emphasize that, what West Coast did two (2) years after the sale it sold Centra, it sold itself to Duke. So who knows what Duke would have done today, and how it would have managed the operation in -- in Manitoba.

And that, I think, is indicative of the very first three (3) lines there, operating and administrative -- well, operating and administrative, those are the costs that are probably the most -- the least fixed, the most flexible, and subject to the most discretion, particularly with management in terms of how they want to operate a company.

I know that this Board had admonished Centra when its cost per customer and O&M was -- was getting above two hundred dollars ($200) per customer. At sixty-two dollars ($62) -- sorry, at 62 million, that's shown in this particular -- page 14, and I always hate to do things off the cuff, but I'm looking at 62 million, and that's in the neighbourhood of about two hundred and forty-two dollars ($242) per customer.

And I think that's quite a ways from where the Board had expected Centra to be, and so what -- what would have taken place in the meantime, what -- how many rate proceedings would have taken place, and what the Board would have said to -- to Centra, and its owner, whoever it was at that time, pure speculation.

Depreciation and amortization, capital and other taxes, I notice those two (2) lines are -- are the same. And that's -- that's assuming that Centra's rate base, its infrastructure would have been managed the same way Manitoba Hydro managed it.

And again, I don't know that you can come to that conclusion. Another item is the return on rate base, and I'm having trouble with -- with some calculations that Centra has done. I'm not sure that we're comparing apples to oranges -- sorry, I'm not sure that we're comparing apples to apples.

In the calculation provided in Exhibit -- Centra Exhibit 23, and that was handed out this morning in response to Undertaking 22, where Centra undertook to provide the absent acquisition scenario with a 38 percent debt equity ratio.

And in its response, Centra has provided some different numbers. First of all, the rate base number is different than the rate base number that was used in its calculation on page 14, and that comes from Attachment 2 to the rebuttal; two (2) different rate bases.

Now, they're not that much different, but I notice that they're different, and I couldn't understand why. Second, the after tax return on equity on page 2 of 3 of Centra Exhibit 23, Centra has 9.5 percent.

On Attachment 2 to -- Attachment 2 to the rebuttal, at line 6, Centra used nine point two six 9.26. So I was curious about that, and I read about it down below, and Centra suggests that it should be 9.5 percent because of additional risk, twenty-five (25) basis points.

And they base that on a prior Board Order 8/94. And I would suggest to you, Mr. Chairman, that that would be erroneous to rely on 8/94 because subsequent to that is when the Board set the formula, in decision -- in Order 49/95.

And that formula would not have the flexibility built into it to adjust the -- the risk factor and therefore adjust the rate of return; the rate of return would remain at 9.26.

So, when I do the calculation -- sorry, I come up with a -- a larger difference than -- than Centra; mine's closer to a million dollars. And that comparison I'm talking about is the 40 percent equity, versus the 38 percent equity.

And that's using the 9.26 percent, which, in my view, should be used to remain consistent, and --

and remain whole with the Board's formula, and also using the -- the rate base consistently between the two (2).

So for 05/06 the -- at the outside there would be a $9 million benefit. But I'm suggesting to you, sir, that the evidence isn't strong that it -- it would be that high based on the impact on return for a lower debt equity ratio, and -- and the 38 percent, I would suggest to you, is something that West Coast would have -- would have, and indeed did have, in -- in that range in the past on an actual basis.

It's -- it didn't maintain 40 percent debt equity all the time. And on the O&M, again, there are indications that that is overstated as well. And I believe there was a -- yes, there was an exhibit earlier on in the proceeding, and I don't know which number it is offhand, but it is this bar graph exhibit.

And I look at that and the first six (6) years, if I count them correctly, '93 through '98 I see that Centra, under West Coast, adhered fairly closely --

MR. KRIS SAXBERG: It's Centra Exhibit 16

MR. GREG MATWICHUK: Centra Exhibit 16. Thank you, Mr. Saxberg. And that -- that line above the bars during the West Coast ownership is probably high based on accounting adjustments that I heard discussed earlier today.

And then I -- I look at, for example, 2003, where I understand the bar represents fifty-three point six (53.6) and the line, the dot, the diamond above represents 59 million, which is about a $5 million different. It's not the $7 million synergy that we've been discussing.

So, I'm not sure that the $62 million is a reliable figure from a -- a number of perspectives. So, like I say, at the outside it would be 9 million but I -- I'd suggest to you, Mr. Chairman, that it's probably quite a bit lower than that.

Then I turn to another exhibit which was handed out this morning, is Centra Exhibit 24, and that was a similar calculation which compared the 2006/07 test year against what Centra is suggesting would be representative of would take place absent the acquisition.

So, I have the same comments that I have in this year, and I won't review them all. But to me it's -- it's even more poignant because on the face of it there's no benefit. The amounts are essentially the same and with -- with the margin of error that we've talked here -- about previously, I don't have confidence in the absent the acquisition number being as high as 142.9 million.

And so, at the same time, when there is -- there is no benefit on the Centra side, what we do have is $9 million of synergy benefits on the Hydro side and in the neighbourhood of twelve (12), perhaps even $14 million of benefits on the -- on the Hydro side in terms of return on equity attributable to Manitoba Hydro.

So, well, there's the benefit on the -- on the Hydro side and no benefit on the Centra side certainly in '06/'07, and the trend would certainly appear to be more in line with '06/'07 given the net income amounts that are being suggested for the years after '06/'07.

So, in summary, sir, I -- I'd suggest that the absent the acquisition calculation performed by Centra is likely what were stated in '05/'06 and probably in '06/'07 as well and so there -- there may be harm in -- by the time we get to '06/'07.

MR. KRIS SAXBERG: Thank you, Mr. Matwichuk. Could you provide your comments on the proper calculation of the debt equity ratio?

MR. GREG MATWICHUK: Well, I've noticed that there's been a fair bit of testimony on this -- this issue. And it -- it strikes me that what we have to start with, again, are some fundamental principles. The regulatory principles and the regulatory precedent are well established in this regard. What Centra is proposing here is contrary to those well-established principles.

And the fundamental principle in rate regulation is called stand-alone principle. And it has been adopted, espoused, adhered to by regulators across the country, and it's a principle that applies equally to debt and equity.

But before I go there I think what we need to do is to consider some of the things that are being said about stand-alone principle. And it's been captured in regulatory literature by respected academics and by cost of capital experts.

For example, Dr. Roger Moran (phonetic) -- Moran, he's a cost capital expert from the United States and -- and he writes as follows:

> "The true cost of capital depends on the use to which capital is put, and not on its source. The Hope and Bluefield Doctrines (phonetic)..."

Now each of those are famous cases on cost of capital, Hope and Bluefield.

> "...have made clear that the relevant considerations in calculating the company's cost of capital are

alternatives available to the investors, and the returns and risks associated with those alternatives. The specific source of funding, and the cost of those funds to the investor, are irrelevant considerations."

And Dr. Moran provides a great example. He suggests:

"That if an investor borrows money at the bank at an after tax cost of 8 percent, and invests the funds in a speculative oil exploration venture, the required return on the investment is not the 8 percent cost, but rather the return foregone in speculative projects of similar risk."

And he goes on to say that:

"The identity of a subsidiary's shareholders should have no bearing on the cost of equity.

It is not the parent's weighted average cost of capital that determines a subsidiary's cost of equity, but a parent's cost of capital, is itself a weighted average of equity costs of all subsidiaries."

And I don't think that should come as any surprise.

Now, in addition to academics, because regulators take the input of academics, and to establish these regulatory principles. And I can tell you that regulators across Canada, in Ontario, for example, the Ontario Energy Board, in a recent decision, and I believe it was a 2002 decision, and I quote:

"A longstanding regulatory principle espoused by the Ontario Energy Board, and by other regulators in North America, is the stand alone principle. Applying this principle, the issue is what ought to be a perspective fair return on investment for a utility on a stand alone basis, not how a perspective return may compare, or compete with other business units of the parent company."

And in Alberta, the Board there, the EUB, in a recent decision in 2001, the Board considers that:

"The stand alone principle is a fundamental principle of utility regulation."

In an earlier decision with respect to -- to Nova, where the operating company of Nova, or the operating entity, and this is actually not even a separate corporation, this was a division of Nova, Alberta Gas Transmission Division of Nova, the Board stated:

"The Board considers that AGTD's..."

And that's -- so that's Alberta Gas Transmission Division of Nova:

"...capital structure, including its common equity ratio, should be consistent with its business risks and an ability to track capital on reasonable terms. In this regard, the Board agrees that -- with Nova, that AGTD's capital structure should be determined independent of that of Nova, i.e. its parent, on a stand alone basis.

In addition to the foregoing criteria, the Board considers that it must be satisfied that AGTD, as a stand alone utility, is able to attract its necessary capital requirements on reasonable terms."

When you look at Centra, and the way it's able to attract capital is by getting debt infusion from Manitoba Hydro, plus paying debt guarantee fee, and that would be comparable, hopefully, to the rate that it would otherwise have to charge -- or it would otherwise obtain in the marketplace.

And based on the -- the research that I've done for an A rated utility, which Centra was before it was purchased by Manitoba Hydro, and -- and did get an A rating after owned by Manitoba Hydro, again, there was a flow through rating that the -- the interest rates on the -- the debt, would -- would be comparable, or perhaps even lower than what's currently being charged.

In a separate decision, the EUB said one (1) of the costs, which is deducted from revenue, is the interest or carrying charges on the deemed debt portion of a utility's capital structure. The capital structure capital structure is, of course, set on a stand alone basis, focussing only on regulated utility operations in question.

Now, Mr. Chairman, I -- I don't intend to go through reams of decisions other than -- unless -- unless you'd like me to, but these decisions are consistent across the country that stand alone should be adhered to.

While, I don't have any BCUC decisions with me, I can tell you that I have talked with the Executive Director of Alberta -- or sorry, the British Columbia Utilities Commission, and he assured me that they adhere to the stand alone principle in -- in their jurisdiction as well.

And to take the Centra/West Coast example, when the Ontario Energy Board, or the EUB, or this Board for that matter, looked at return of the various Centra companies, because they -- there were various Centra companies at that time, owned by West Coast. They looked at the return, the capital structure, and so on, with respect to those subsidiaries owned by West Coast. Those regulators looked at the risk profile of -- of the individual utilities, not of West Coast.

And under West Coast, Centra typically had a debt -- debt equity of around 60:40, and whereas the operating company may have had that capital structure, it was clear that West Coast was financing on a different capital structure, with more debt.

And so it's -- it's not the -- how it's financed, it's how the capital structure should be set, given the risks of the operating company, the one that we're setting the rates for.

And so when Centra suggested my evidence does not consider the matter on a consolidated perspective, well there's -- they're right, and there's a very good reason for it, and it's to prevent cross-subsidization.

And we can look at it from the reverse perspective, Manitoba Hydro does not send down its debt to Centra without a debt guarantee fee, because that would be cross-subsidization.

So, on a stand alone basis, it has to incur a debt cost that it would otherwise in the market, it has to be comparable.

Now, I've -- I heard Centra suggest that there's a distinction in that there was an acquisition of an investor owned utility by a Crown owned utility. And Mr. Chairman, I suggest to you that is a distinction -- distinction without a difference.

There are many Crown owned utilities across -- across the -- the country. And -- and it doesn't matter whether they require it, or they simply restructured and owned, in Alberta we have EPCOR Utilities, which is owned by the City of Edmonton, Enmax, which is owned by the City of Calgary, Hydro One, in Ontario, is owned by the Province, Newfoundland and Labrador Hydro is owned by the Province.

All have debt equities calculated on the basis of including share capital. All have utilities with debt equity ratios that are determined independent of ownership. They all have credit ratings that are based on debt equity with share capital included.

If you look at the -- the credit ratings of each of those entities, they're based on the share capital being part of equity. And for that matter, if you look at the most recent Centra debt equity -- or credit rating, DBRS, calculated the capital structure with share -- share capital included.

And I submit to you, sir, that the -- the finan -- debt equity ratios have a financial definition. It's a commonly held financial definition, chartered accountants have a definition, financial experts have a definition, and it's the same definition.

And when you look to audited financial statements, those audited financial statements are hopefully the -- a source of reliability, and that's why they are audited. That readers of financial statements will be able to determine, on a transparent basis, that the debt equity ratio is a function of total debt and total equity, the latter including share capital.

Now, how does this impact Centra? Unfortunately, I -- I think Centra -- I'm not sure that they meant to say this, but maybe they did, that I suggested that Centra need not be concerned with debt equity ratio, well that's not the case and I didn't say that.

And -- and I notice that when Centra suggested that they didn't have a cite in my -- my evidence, so that's why I was wondering whether they really meant to say it.

But in any event, the point that's made in -- in my evidence, is that the importance of Centra's debt equity ratio is somewhat diminished when it -- from when it was owned by West Coast. When it was owned by West Coast, Centra went to the market on its own, and so it was essential that it maintained its debt equity ratios.

Currently, Centra obtains a step through Hydro, and pays a debt guarantee fee. So, there is a -- a bit of a diminished importance, and it -- in terms of the amount of earnings that it has to retain in -- within the entity, are not as high.

Centra, I believe under West Coast, 65 to 70 percent dividend ratio -- dividend policy. So they -- they retained 30/35 percent of their earnings, to meet -- to ensure that the -- they were within debt covenants, and that they showed strong financial statements because they had to go to the market, the open market; here

Centra has some protection through Manitoba Hydro.

So, while it isn't -- it is still important, it has diminished importance, and therefore that helps me in assessing that one point one (1.1) times interest coverage is -- is certainly sufficient.

MR. KRIS SAXBERG: Mr. Matwichuk, could you explain why you say that the corporate allocation has been double counted and should be removed from the revenue requirement on a rate base rate of return methodology?

MR. GREG MATWICHUK: Perhaps what we should do -- I think maybe the best source is Centra's Application, which I believe is Centra Exhibit 1, and Tab 3, Attachments, Schedule 3.0.0.

MR. BOB PETERS: Mr. Chairman, if that's assistance to Mr. Matwichuk, Mr. Saxberg and the Board, we have that at the Book of Documents that I circulated, at Tab 13. And I appreciate Mr. Matwichuk wasn't here when we handed those out, but as -- if he looks at it and is satisfied it's the same schedule, then the Board has it in both places.

MR. GREG MATWICHUK: Thank you, Mr. Peters. Yes, that is the same schedule.

So when I look at that schedule, and obviously I'm going to focus here on lines 19 and 21.

And again I go back to the Board's plan as a starting point. The Board stated that Hydro can cover off its acquisition costs by the combination of return on equity in Centra, and the synergies in Hydro.

So, that was the intended purpose of the return on equity component, according to the Board, given this new situation where Centra -- Centra is owned by Manitoba Hydro.

Then, as I understand Centra's evidence, that is also Centra's -- or Centra has the same intention for the corporate allocation. And -- and I believe in one (1) or two (2) IR Responses, they indicate that that's particularly the case, whereas it was fifteen (15) and it's now twelve (12), we're still talking about the same number that it was the intention to cover off Centra's share of the acquisition costs.

So once we've determined the amount under rate base rate of return; i.e., the inclusion of revenue requirement for return on equity, which has the intention of covering off part of the acquisition costs, it simply renders a corporate allocation amount unnecessary.

And that is from a perspective of -- of intent, in a response to an IR, and I just forget which one (1) it is, bear with me please. PUB/CAC/MSOS-3, which I think is Exhibit CAC/MSOS-5-3.

There was a question by the Board, please explain how corporate allocation results in double counting. And what I provided there at the bottom of the page was under rate base rate of return, we have an equity return and I'm using a nominal amount here of -- I'm sorry, I should say a notional amount of 12 million. And a corporate allocation amount of 15 million. So when you add those two (2) together you get 27 million.

So that's 27 million that Hydro would have entitlement to from Centra. And it's a whole other issue as to whether that gets distributed, but Hydro has an entitlement to it. And it's up to Hydro to make the determine (sic) whether it's going to distribute to itself from Centra.

So the 12 million plus the 15 million gives you 27 million. You divide that by the equity component of rate base of 132 million, and that gives you in excess of 20 percent return to the owner.

Mr. Chairman, I -- I would suggest that there is no jurisdiction in this country that would allow a return to the owner on its investment of 20 percent. And none of the formulas I can assure you, would allow that return either. So that's why I'm suggesting that there is double counting, because of the intention and the result.

Now, I also note that Centra, in terms of its cost of service application amounts, particularly with respect to 2006, we'll come back to 2005 in a minute. That if you look at, in Schedule 3.0.0, that was contained -- I'm sorry, Mr. Peters, I forgot your exhibit number already.

MR. BOB PETERS: I have it at Tab 13 of the book of documents that was circulated --

MR. GREG MATWICHUK: Thank you.

MR. BOB PETERS: -- for the reference of the parties.

MR. GREG MATWICHUK: And -- and that -- and if we look at lines 19 and 21, under cost of service for 2006/07, and -- and we don't have to worry about the individual amounts because we know they still total the same. So you have 15 million, 15.14 million, 11.3 million, for a total of 26.4 million, and again, those are amounts that are entitled to the owner. The owner is Manitoba Hydro.

When you look at -- you total those amounts, 26.4 million, the return, based on the equity portion of the rate base, that would be 19.3 percent.

So, even under a cost of service basis, Centra's Application is excessive in terms of the entitlement to the owner, compared to what any privately held utility would be entitled to in this country.

And it similarly applies in 2005/06, when you add the fifteen point one (15.1) to the one point seven seven nine (1.779), or as it might be now, four point seven seven nine (4.779) and twelve point one (12.1), you still get sixteen point nine (16.9). And that would be in excess of 13 percent.

Again still excessive, because -- and I come back to my earlier comments as the rate base rate of return methodology allows one to determine what a fair return would be. And that fair return is based on the risks associated with that entity, relative to alternative investments, alternative utilities, comparable utilities.

And again, Mr. Chairman, across the country, you wouldn't see the likes of those returns being allowed in -- in the current years -- current test years.

MR. KRIS SAXBERG: What are your ultimate recommendations to the Board?

MR. GREG MATWICHUK: Mr. Saxberg, my recommendations are outlined in the end of my evidence on page 29 of Exhibit CAC/MSOS 2, and first and foremost, I'm recommending that the Board do continue with the use of rate base rate of return methodology, and I -- I believe I've outlined my reasons for that in terms of -- of fairness, objectivity.

But regardless of the Board's choice, that the revenue requirement should be no more than what would be determined by the Board under rate base rate of return methodology.

And in the case of rate base rate of return methodology, to recommend that the $15.1 million amount be removed from -- from revenue requirement -- non-gas revenue requirement, and I -- you don't need to turn to it, but I can tell you that's what was done in my response to PUB-1 under CAC Exhibit 5-1.

And in the case of cost of service, we should remove all the amounts that accrue to the benefit of Hydro, and ensure that and -- the -- only the amount that is necessary be available to transfer to Hydro.

And my suggestion, sir, is that all of these amounts with respect to transfers are done below the line. And we have enough chartered accountants in the room to -- to get the flavour of that is, we establish what net income is, if we're doing a cost of service basis, and then without assigning an allocation or a cost, above the line, in other words, above net income, we determine what net income is, and then below net income we determine the amount of the allocation, cost transfer, or dividend.

Because that will make it transparent. There will be no suggestion of because there was an allocation, we've incurred a loss, and we have to recover that loss in future years; that's not what the Board's plan was.

The Board's plan was to use earnings in excess of the cost to operate the utility to transfer to Hydro to help offset the costs of the acquisition.

MR. KRIS SAXBERG: Thank you, Mr. Matwichuk. Do you have any other comments at this point in time?

MR. GREG MATWICHUK: No, I believe those are all my comments at this stage.

MR. KRIS SAXBERG: Thank you, then, that concludes my direct examination.

THE CHAIRPERSON: I think probably it's an appropriate time to stop for the day then. So we'll recommence tomorrow and we'll begin the cross-examination of your witness.

MR. KRIS SAXBERG: Thank you.

THE CHAIRPERSON: So, thank you very much. Good night.

(WITNESS RETIRES)

--- Upon adjourning at 3:50 p.m.

Certified Correct,

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Carol Wilkinson, Ms.