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
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APPEARANCES

R.F. Peters		)Board Counsel
Marla Murphy		)Manitoba Hydro
Karen Melnychuk		)Direct Energy Marketing
David Brown	(np)	)Limited/Municipal Gas
Nola Ruzycki	(np)	)Energy Saving (Manitoba)
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Kris Saxberg		)CAC/MSOS
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Randall McQuaker	(np)	)Conservation Manitoba
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--- Upon commencing at 9:10 a.m.

THE CHAIRPERSON: Good morning everyone. I hope you had a restful weekend.

Mr. Peters, you have some opening comments?

MR. BOB PETERS: Yes. Good morning, Mr. Chairman, Board Members, ladies and gentlemen. I have two (2) or three (3) matters of a housekeeping nature, if I may, Mr. Chairman.

The first is in Mr. Brown's typical efficient manner prior to the Hearing starting he had e-mailed the Intervenors and -- and Board Counsel and provided in his e-mail a PDF version of the, what has now been marked as Document Number 2; that is Municipal Direct Exhibit 2.

It's a book of documents that he had prepared for his cross-examination. In sending that PDF file there was inadvertently a two-page document attached at the very end.

I'm not aware that that made it through to the paper copy but it was included in the electronic copy and Mr. Brown's request is that we simply remove and destroy it as it is not relevant to the proceedings before the Board.

So, if parties haven't already done so, I'd make that request on his behalf.

The second matter of housekeeping this morning, Mr. Chairman, is to bring to the Board an outline of procedures that I believe represents the latest consensus as to how we will proceed this week and through the balance of this Hearing.

This outline of procedures has been circulated on yellow paper. It shows that for Monday, Tuesday and Wednesday of this week we have Centra's Witness Panel number 2 with us to speak on revenue requirement issues.

I would note on the schedule that Mr. Vince Warden is away from the Hearing Tuesday morning, in light of a previously disclosed and arranged matter. But, to the extent that there are questions that would otherwise be asked of him, he will be back. And so we're not -- we're not concerned that he won't have that opportunity to address questions as they may come up.

You can see on the front page of the outline of procedures, Panel 2, and the order that we see Panel 2 proceeding through the next two (2) and three (3) days. One (1) week from today on page 2 you'll see Monday, June 13th it's anticipated that Mr. Saxberg and his client, CAC/MSOS will have their witness, Mr. Greg

Matwichuk in Winnipeg to testify both on his direct and cross-examination and we've set aside that date for that -- to ensure that happens.

Then turning the page to page 3 on Tuesday, June 14th and June 15th, Centra's third panel on cost allocation and rate design matters, as well as, other matters under Tab 13, which has drawn the attention of a number of Intervenors will be on the stand and they're anticipated to take both Tuesday and Wednesday, that is June 14th and 15th.

Then turning the page again, on Monday, June 20th, it's anticipated that the RCM Tree witness, Mr. Steven Weiss will be in Winnipeg. And by way of e-mail communicated from Dr. Miller this weekend, Mr. Weiss will be the only witness produced by RCM and Tree.

And there is an understanding that the evidence of Steven Weiss will incorporate by reference the matters contained in the Pembina Institute evidence and that Mr. Weiss won't be asked to specifically support any of the calculations or conclusions reached by the Pembina Institution, but Mr. Weiss will rely on them and explain them in his evidence as well.

After Mr. Weiss' evidence on Monday, June 20th, we're left to arrange closing submissions and the date that the parties had come back to the Board on was

Monday, June 27th. And recognizing the parties hadn't checked with the Board, the Board's availability on that date is not totally unfettered.

And so presently, the closing submissions are scheduled to commence at 1:00 p.m. on the day, Mr. Chairman. It is anticipated that it would be certainly a lengthy day if we were going to complete all closing submissions on that day. Or there may be other days that parties will look at to see if we can split it up and maybe Tuesday morning. But, again, it will always be subject to the availability of the Board.

And likewise, if for any reason the Board's availability changes, parties will appreciate being notified and we'll -- we'll accommodate accordingly.

THE CHAIRPERSON: Mr. Peters, we do have some difficulty with the June 27th. We'll talk about it at the break.

MR. BOB PETERS: All right. Thank you sir. The June 27th, as you say, the closing submissions will reconfirm that on record to make sure parties who are monitoring the transcript have an opportunity to be aware.

There was some discussion, Mr. Chairman, that this would be an opportunity to provide oral closing submissions and if any party wanted to submit them in written form, they would have an opportunity to provide them to the Board by the end of the previous close of business day -- the previous business day closing, which in that case would have been Friday.

But, we will finalize that and will notify all parties.

Those are my matters to address this morning. At this time, I'm not aware of any other matters and would suggest that you turn to Ms. Murphy, so she can introduce her next panel of witnesses. Thank you.

THE CHAIRPERSON: Thank you Mr. Peters.

Ms. Murphy ...?

MS. MARLA MURPHY: Good morning, Mr. Chair, ladies and gentlemen, members of the Board.

I'll just take a minute to introduce Centra's revenue requirement panel. To my immediate right is Mr. Vince Warden, you're familiar with, Vice-President of Finance, Administration and Chief Financial Officer for Centra.

Then we have Mr. Willie Derksen who is the manager of Budget Services. Next is Darren Rainkie, who also appeared on the Cost of Gas Panel, manager of Regulatory Services. And then we have Mr. Aziz Aziz who is the manager of Gas Distribution, Planning and Design. And finally, Mr. Dave Case, who's the manager of Customer Service Operations.

If I might just take a minute to introduce you to some of the new faces in the back row as well, starting immediately behind me is My Colleague, Mr. Brent Czarnecki. Beside him is Nancy Williams, who is the Regulatory Financial Analyst. Next, Stan Matwyczek who's the Regulatory Advisor, and Kevin Sachvie, Regulatory Coordinator. Then Mr. Dave Coleman, who's the Maintenance and Environmental Engineer, with the Gas Distribution, Planning and Design Department.

And finally, Mr. Bob Prystenski who's the Manager of Financial Services, and they'll be providing assistance for the witnesses throughout this week. So if the Panel could be sworn, we're ready to begin with the direct.

THE CHAIRPERSON: Thank you, and welcome.

Mr. Singh...?

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

THE CHAIRPERSON: Thank you, Mr. Singh.

Mr. Peters...?

MS. MARLA MURPHY: Maybe I'll just jump in for a minute.

THE CHAIRPERSON: I'm sorry, it's Monday morning. I have to apologize.

MS. MARLA MURPHY: I feel the same way. I might indicate just for the record that the witness qualifications of Mr. Warden, Mr. Derksen, Mr. Rainkie, Mr. Aziz and Mr. Case have all been marked as exhibits.

They're Exhibit Centra 4-1, 4-11, 4-4, 4-2 and 4-6, respectively.

--- EXHIBIT NO. CENTRA 4-1: Qualifications of Mr. Vince Warden

--- EXHIBIT NO. CENTRA 4-2: Qualifications of Mr. Aziz Aziz

--- EXHIBIT NO. CENTRA 4-4: Qualifications of Mr. Darren Rainkie

--- EXHIBIT NO. CENTRA 4-6: Qualifications of Mr. David Case

--- EXHIBIT NO. CENTRA 4-11: Qualifications of Mr. Willie Derksen

MS. MARLA MURPHY: As you're aware they set out the positions of the Panel Members and their qualifications, their experience before the Board, their areas of responsibility and their adoption of the prefiled evidence.

EXAMINATION-IN-CHIEF BY MS. MARLA MURPHY:

MS. MARLA MURPHY: Mr. Warden, would you please outline your areas of responsibility with respect to this Panel?

MR. VINCE WARDEN: Good morning, Mr. Chairman, Members of the -- of the Board, ladies and gentlemen. In my testimony I will be discussing policy issues with respect to Centra's 2005/06 and 2006/07 General Rate Application.

I will also be providing evidence related to Centra's operating and administrative costs, financial targets, Corporate allocation and financing arrangements.

MS. MARLA MURPHY: Mr. Warden, would you please describe the circumstances giving rise to this Application as it relates to non-gas costs?

MR. VINCE WARDEN: On December the 9th,

2004 Centra applied to the Public Utilities Board pursuant to Section 45 of the Public Utilities Board Act for an interim ex parte order to approve an interim rate increase of approximately 2.5 percent of overall revenue effective February the 1st, 2005, sufficient to generate additional revenue of $3 million in 2004/05 and $12 million in '05/'06.

Centra applied for this interim increase in recognition of the losses incurred in 2003/04, and the losses forecast to be incurred for the 2004/05 and 2005/06 fiscal years.

Centra required immediate relief in order to generate additional revenue, so as to reduce the losses that were otherwise projected to be incurred. Without this additional revenue, it was projected that Centra would incur losses of $8 million for 2004/05, $10 million for 2005/06 and $15 million in 2006/07.

These losses would have reduced Centra's retained earnings to a deficit of $8 million as at March 31st, 2007. Clearly this was of great concern to Centra's management and Board -- Board of Directors, and in Centra's view, interim relief was necessary to preserve the financial integrity of the Utility.

Centra filed its General Rate Application on January the 10th, 2005, seeking final approval of interim Order 13/05.

Centra's also seeking rate increases in 2006/07 to recover an additional 2.5 percent of overall revenue for the 2006/07 fiscal year. The 2.5 percent increase in revenue for 2006/07 will generate additional revenue of $13 million for that year.

MS. MARLA MURPHY: Mr. Warden, would you please outline for the Board, Centra's preference regarding the regulatory methodology?

MR. VINCE WARDEN: Centra is of the view that the cost of service methodology is the most appropriate rate setting methodology for a Crown-owned utility such as Centra. It is Centra's preference that the Board determine Centra's rates based on the cost of service methodology and continue to do so in the future.

The cost of service methodology is more flexible in that in -- in that it inherently allows for review of progress in attaining financial targets since the last General Rate Application and the expected progress over the forecast period rather than focussing solely on the rate of return in a specific test year.

The cost of service methodology allows for rate-smoothing in terms of the gradual attainment of financial targets. The cost of service methodology is also more efficient in that it focusses directly on the financial and operation forecast of Centra rather than the calculation of return on equity which is not a factor in the decision making process of management nor in the Company's determination of an appropriate rate application.

MS. MARLA MURPHY: Mr. Warden, is the corporate allocation necessary to hold the Manitoba Hydro electric ratepayers harmless?

MR. VINCE WARDEN: Absolutely. As outlined on pages 5 to 10 of Centra's rebuttal evidence, the corporate allocation is the only allocation to Centra ratepayers related to the costs incurred by Hydro to acquire and integrate the natural gas utility.

Absent the corporate allocation all acquisition and integration costs would be borne by electricity ratepayers and, as such, they would not be held harmless.

With the corporate allocation both electricity and natural gas ratepayers are held harmless.

MS. MARLA MURPHY: Mr. Matwichuk calculates Centra's debt equity ratio differently than Centra. Could you please explain the difference in those calculations?

MR. VINCE WARDEN: Yes. Mr. Matwichuk calculates a debt equity ratio of 63:37 whereas Centra calculates a ration of 84:16.

Two (2) very different conclusions but the only difference in the formula is that Mr. Matwichuk includes share capital of 121 million in the denominator of his calculation whereas Centra excludes this number.

The reason that share capital cannot be included as a component of equity is that Centra's share capital is 100 percent debt-financed by Hydro. It is offset by debt on Hydro's balance sheet.

Therefore, Centra's share capital makes no contribution whatsoever towards corporate equity and it would be incorrect to include this amount as a component of equity in Centra's debt equity calculation. Thank you.

MS. MARLA MURPHY: Thank you, Mr. Warden.

Mr. Derksen, would you please outline your areas of responsibility with respect to this panel.

MR. WILLIE DERKSEN: Yes, good morning, Mr. Chairman, members of the Public Utilities Board, ladies and gentlemen.

In my testimony I will be responding to questions related to the integrated cost allocation methodology and its impacts on operating and -- and administrative costs.

I will also be providing evidence with

respect to Centra's other income, depreciation expense and capital and other taxes.

MS. MARLA MURPHY: Mr. Derksen, could you please advise the Board whether there have been any changes to the integrated cost allocation methodology since Centra last appeared before the Board on this issue in the 2003/04 GRA?

MR. WILLIE DERKSEN: Yes, there have been no changes to the integrated cost allocation methodology since that time.

MS. MARLA MURPHY: Mr. Derksen, would you please outline Centra's cost of operations for 2005/06 and 2006/07 included in this application?

MR. WILLIE DERKSEN: Yes. In this application Centra's operating and administrative costs for the 2005/06 test year are forecast to be $54.1 million and for the 2006/07 test year are forecast to be $55.2 million.

MS. MARLA MURPHY: Can you please confirm whether Centra's requested operating and administrative expenses includes the $3 million synergy benefit transfer that was approved in Order 118/03?

MR. WILLIE DERKSEN: There is no synergy transfer amount embedded into the applied for O&A component of revenue requirement. The amount of applied for O&A expense represents only the anticipated expenditures required to operate the gas utility.

The synergy benefit amount of $3 million that -- $3 million dollars that was previously approved has been appropriately classified as O&A expense in the approved 2003/04 revenue requirement for comparison purposes and it is not contained in the applied for revenue requirement of either test year.

MS. MARLA MURPHY: In his evidence, Mr. Matwichuk comes to the conclusion that Centra's proposed revenue requirements will result in harm to Centra's customers. Can you please comment on that conclusion?

MR. WILLIE DERKSEN: Yes, Mr. Matwichuk's calculation of the comparator for the test of harm to Centra's customers is incorrect. The proper basis of the no-harm calculation for Centra's customers, is based on what otherwise would have happened absent acquisition.

This calculation would be based upon a rate base, rate of return methodology assuming West Coast Energy Inc. ownership. This is different at the rate -- base rate of return calculation contained in Tab 5 under Hydro ownership.

It is not appropriate to simply remove the corporate allocation from the hydro rate base, rate of return scenario and use that as a comparator for the cost of service calculation. The appropriate measurement for no harm is the non-gas cost portion of the revenue requirement, which includes consideration of operational savings, income tax reductions and any other identifiable savings which arise from the transaction.

As noted on page 14 of Centra's rebuttal evidence, Centra's non-gas revenue requirement for 2005/06 is at least $9 million lower than it would have been absent acquisition, even after including the corporate allocation.

MS. MARLA MURPHY: Mr. Warden noted in his evidence that the only amount transferred to Centra is the corporate allocation. Mr. Matwichuk calculated the amounts transferred in a different fashion. Can you please comment on those calculations?

MR. WILLIE DERKSEN: Yes, Mr. Matwichuk incorrectly includes net income in his calculation of amounts credited to Hydro from Centra and also incorrectly includes a synergy benefit transfer from 2000/2001 and 2002/03, failing to recognize that these transfers were reversed after the PUB issued order 208/02.

Mr. Matwichuk compounds the difficulties in his calculation by suggesting and incorporating an arbitrary allocation of synergies between the two utilities based upon the relative proportion of the O&A cost that flow from the cost allocation methodology.

This results in a significantly different allocation of synergies of 2.3 million to Centra and 13.7 million to Manitoba Hydro. Based on Manitoba Hydro's most recent review of the allocation of synergies which -- which allocation takes into account all of the known factors impacting it, Centra receives the benefit of $6 to $8 million in synergy savings.

MS. MARLA MURPHY: Thank you, Mr. Derksen.

Mr. Rainkie, would you please outline your areas of responsibility with respect to this panel?

MR. DARREN RAINKIE: Good morning, Mr. Chairman, Members of the Public Utilities Board, ladies and gentlemen. In my testimony I will be providing evidence with respect to Centra's letter of application and its 2005/06 and 2006/07 requested revenue requirement, including the amortization component.

I will also be responding to questions with respect to rate base and rate of return calculations for each of the test years including working capital, return equity and capital structure.

MS. MARLA MURPHY: Mr. Rainkie, would you please summarize what Centra is seeking with respect to non-gas costs in this Application?

MR. DARREN RAINKIE: Centra is seeking approval of a 2005/06 non-gas revenue requirement of approximately $129.5 million and a 2006/07 non-gas revenue requirement of approximately $142.7 million.

The details of these requests are provided in the cost of service materials at Tab 4 of Centra's Application.

MS. MARLA MURPHY: Mr. Rainkie, could you please comment on the application of the cost of service methodology in the determination of Centra's non-gas revenue requirement?

MR. DARREN RAINKIE: Yes. Similar to how the cost of service methodology has been applied to Manitoba Hydro, Centra suggests that the Board determine the overall percentage increase in revenue for each of the two (2) test years.

This is in contrast to how the rate, base rate of return methodology has been applied in the past, which requires a determination of each specific cost component or line item that makes up the total revenue requirement.

MS. MARLA MURPHY: Mr. Rainkie, in addition to the interim orders outlined in your direct evidence on May 30th, are there other interim orders for which Centra is seeking final approval?

MR. DARREN RAINKIE: Yes. Centra is requesting that the Board give final approval of interim order 54/05 dated April 19, 2005, which approved the amended franchise agreement and feasibility test for the extension of gas service to one (1) commercial customer in the rural municipality of Rosser.

MS. MARLA MURPHY: Mr. Rainkie, would you please outline Centra's request with respect to the Interlake and Bifrost-Woodlands connection fee schedule?

MR. DARREN RAINKIE: Centra is requesting that the PUB grant approval to gradually reduce and then eliminate after December 31st, 2006, the connection fee schedules for the Interlake and the Bifrost and Woodlands rural municipality expansion projects.

These connection fee schedules were previously approved in Orders 95/00/00 and 172/01 respectively.

In July of 2004, the Interlake Co-op advised Centra that a motion had been passed to request that Centra discontinue collection of connection fees, effective January 1, 2004.

Centra supports the Co-op's request to have these connection fees gradually eliminated in these project areas.

In the current environment of higher gas costs the collection of connection fees is a deterrent for future conversions, and it is hoped that phasing out these fees will enhance natural gas conversions, and in turn the long term viability of these projects.

It is Centra's proposal to have the connection fee schedules eliminated by way of gradually reducing the fees over the next two (2) years, starting January 1, 2005, rather than all at one (1) time, to ensure that the current and future customers are treated as fairly and equitably as possible.

MS. MARLA MURPHY: Mr. Matwichuk contends that Centra's rate base rate of return calculations contain double counting, in that it contains both the corporate allocation and the return on equity.

Can you please respond to that contention?

MR. DARREN RAINKIE: Yes. Centra's proposed revenue requirements and its corporate allocation deal with two (2) distinct issues. Number 1, Centra's appropriate share of the acquisition and integration costs, and number 2, the appropriate level of retained earnings in Centra after the corporate allocation.

Once the corporate allocation has been applied, the appropriate level of net income can be determined under each of the respective regulatory methodologies.

Under cost of service it's based on management's judgment on the pace of attainment of financial targets, while under rate base rate of return it has been calculated based on the equity portion of rate base, and the fair rate of return.

Centra's calculations of rate base rate of return do not include double counting, but rather recognize the very formula that is used under this methodology in order to calculate or determine allowed net income for regulatory purposes.

MS. MARLA MURPHY: In Mr. Matwichuk's evidence he indicates that moving to a cost of service methodology at this point would, quote, "cloud the issue," close quote, of how costs of acquisition are allocated between the gas and electric utilities.

Would you please comment on this assertion?

MR. DARREN RAINKIE: Contrary to Mr. Matwichuk's suggestion, the formalization of the corporate allocation in Centra's revenue requirement will enhance transparency, as it will be clear to both the readers of the financial statements and participants to the regulatory process, the exact amount that has been allocated to Centra to pay for its share of the acquisition and integration costs.

Adoption of the costs of service methodology for setting of gas rates will further enhance transparency, and that the PUB will be using a methodology consistent with that used to set electric rates.

Both of these measures will facilitate comparability and understandability of the revenue requirements and financial statements of Centra and Manitoba Hydro.

MS. MARLA MURPHY: Thank you, Mr. Rainkie.

Mr. Aziz, would you please outline your areas of responsibility with respect to this Application.

MR. AZIZ AZIZ: Good morning, Mr. Chairman, Members of the Public Utilities Board, ladies and gentlemen. In my testimony I will be responding to questions regarding the transmission and distribution business, unit capital cost, capital expenditure and costs -- and costs of operation related to Centra.

As well, I will be providing evidence with respect to the four (4) party trenching initiative.

MS. MARLA MURPHY: Mr. Aziz, would you please briefly outline the capital expenditures for system load growth, included in Centra's Application?

MR. AZIZ AZIZ: The installation of new services and the submission means to attaching customers in existing franchise area is Centra's largest capital investment on annual basis.

For the 2004/05 year, Centra anticipates attaching capital expenditure over approximately -- approximately 9.5 million, for the 2005/06 test year, Centra anticipates capital expenditure of approximately 9.7 million, and for the 2006/07 test year, Centra anticipates a capital expenditure of approximately 9.6 million.

MS. MARLA MURPHY: Mr. Aziz would you please update the Board on the implementation of Centra's Integrity Management System?

MR. AZIZ AZIZ: The Integrity Management System is being developed for Centra transmission pipeline system, to allow a more comprehensive, systematic and integrated process to maintain pipeline integrity by effectively identifying, assessing and mitigating pipeline hazards.

An integral part of the integrated management system is the implementation of the risk assessment software to allow Centra to conduct objectives, risk assessment and optimize mitigation activities accordingly.

The data collection and conversion effort for the risk assessment software was completed in 2004/05. Risk results as well as a risk report will be completed the summer of 2005. Documentation of the integrity management system and completion of the risk assessment software data bridge programming is scheduled to be completed by the end of the fiscal year 2005/06.

MS. MARLA MURPHY: Mr. Aziz, could you please briefly describe the system integrity programs and projects currently in place at Centra?

MR. AZIZ AZIZ: In section 4.4.4 of the application, in addition to the development of the integrity management system, as I have just outlined, there are nine (9) additional transmission and distribution operating programs discussed which include cathodic protection monitoring, close interval surveys, A-frame surveys, pipeline depths of cover surveys, water course crossing investigations, stress corrosion cracking investigation, development of welding procedures, geotechnical instrumentation monitoring and regulator station maintenance.

Other Centra operating programs pertaining to system integrity which are covered under customer service and marketing operating programs include damage prevention programs, leak surveys and right-of-way conditioning surveys.

In Section 5.2 of the Application there are fifteen (15) integrity-related capital programs listed including the Riser rehabilitation project, regulator -- regulator station upgrades, LGS regulator and the relieve vent piping upgrades, Westwood condominium upgrades, Polyethylene Butte fusion remediation project, below grade entry rehabilitation project, Lockport road project, outside meter set rehabilitation and Lockport area of crossing rehabilitation, insufficient groundcover upgrades, southwest transmission pipeline investigation and rehabilitation, Hanover/La Broquerie transmission pipeline investigation, river crossing remediation work, mitigation of ground movement and erosion and cathodic protection upgrades.

MS. MARLA MURPHY: Mr. Aziz, could you briefly explain the four-party trench process and review the benefits of that initiative for the Board?

MR. AZIZ AZIZ: The four-party trench and installation program recently developed integrates Centra's gas installation into the former three-party, which is the electric, telephone and cable tv trench process.

During the 2004/05 construction season Centra activities with respect to four-party trench focussed in developing clear, safe, efficient standards for the design and installation of the plant.

During this period -- this period -- during this period -- this period projects were completed in various areas of the Province allowing staff to gain experience with the new design and provide feedback.

Currently Centra is undertaking an initiative to optimize the process for four-party trenching. To date we have met our -- the current gas and existing three-party processes, integrated gas into the existing three-party process -- process and identified a number of optimization opportunities.

Centra is developing the new four-party process quantifying implementation, cost benefit, reviewing the current cost allocation model and implementing the new four-party process at the referred installation method for the 2005/06 construction season.

The process will be continually monitored and refined during this time. Prior to proceeding with the four-party trench initiative, Centra evaluated the current processes for installing the gas and three-party installation separately, compared to installing all four (4) utilities in once -- at once.

There is also the evaluation demonstrated approximately a 25 percent overall savings associated with four-party trenching. This savings were exclusively associated with the installation of the plant and associated activities.

The optimization exercise I described will include identification of the cost savings for all aspects of the four-party trenching process. There are also some qualitative benefits associated with four-party trenching. The location of the gas mains will always be known relative to the electric cables, as they installed in the same trench.

Improving thirty (30): Damage to the plant during an installation is eliminated as all plant is installed at the same time. An installation of services to new homes will be more efficient as no services will need to be pushed across the road, improve -- improving waiting time.

Gas and electric meters will be installed also on the same side of the house improving -- improving meter reading efficiency.

MS. MARILYN MCLAREN: Mr. Aziz, could you please briefly update the Board on the implementation of Centra's riser rehabilitation program?

MR. AZIZ AZIZ: The riser rehabilitation

program is a multi-year project involving the inspection of approximately sixty-six thousand (66,000) residential services, where meters are installed inside the premises.

This inspections assesses -- assess the condition of the regulator set and service riser. They -- and the pre-authorize those requiring replacement. For services that are determined to be a priority for rehabilitation the meter will be moved from inside to outside the premises, where possible.

Since commencement of the program in 2000 and 2001, approximately ten thousand (10,000) riser rehabilitation have been completed by the end of 2004/05. Centra anticipates replacing approximately three thousand (3,000) risers in both 2005/06 and 2006/07. The program is expected to continue to 2007/08 with plans to rehabilitate approximately three thousand (3,000) additional service risers.

In connection with the service riser -- in connection with the service rehabilitation -- sorry -- in connection with the riser rehabilitation program, a number of piping failures that occurred to residential service riser assemblies, with outside meters that due to soil settlement were identified.

The analysis of this failures has shown that most failures were associated with older service risers, service riser assemblies, where the piping downstream of the meter had limited movement capability due to auxiliary piping.

During 2005/06 Centra intends to identify and then inspect these services to the define the scope of the rehabilitation program and prioritize these -- those sites requiring rehabilitation.

MS. MARLA MURPHY: Mr. Aziz, could you please briefly outline the work pertaining to the mitigation of transmission pipeline ground movement and erosion?

MR. AZIZ AZIZ: In 2004/05, Centra conducted a comprehensive geotechnical and hydro technical review of all its transmission pipeline right-of-ways, to assess the potential for -- for slope movements and/or erosion that could adversely impact pipeline integrity.

The study identified mitigation, recommendations and options for a number of sites. Mitigation options include installation of slope monitoring and instrumentation, installation of erosion protection measures and the topographic surveys to allow remedial measures to be -- to be planned or assessed in the future assessment of the ground movement potential.

During 2005/06, and 2006/07, Centra plans to address this as -- on a priority basis.

MS. MARLA MURPHY: Thank you, Mr. Aziz.

Mr. Case, would you please outline your areas of responsibility with respect to this Application?

MR. DAVID CASE: Good morning, Mr. Chairman, Members of the Public Utilities Board, ladies and gentlemen. In my testimony I will respond to questions regarding the customer service and marketing business unit capital expenditures and cost of operations related to Centra.

MS. MARLA MURPHY: Mr. Case, could you please describe Centra's safety initiatives for the Board?

MR. DAVID CASE: Centra has institutionalized many safety initiatives that help to ensure the safe delivery and utilization of natural gas. I will briefly highlight some of the major initiatives.

The natural gas systems entering -- I'm sorry, the natural gas streams entering distribution systems are odourized with mercaptan that provides a distinct, recognizable smell that enables the early detection of natural gas leaks well in advance of any hazardous accumulation of natural gas in the atmosphere.

The major -- the major natural gas delivery systems are monitored twenty-four (24) hours per day by a SCADA system, which alerts operators to deviations from normal operating conditions.

Centra maintains a twenty-four (24) hour contact dispatch centre to save calls from the public. The contact centre representatives are trained to assess the nature and priority of calls, and if deemed necessary, to dispatch the appropriate, skilled and equipped personnel, who are readily available and strategically located throughout the natural gas franchise areas.

Centra has developed and maintains an emergency response plan that helps to ensure emergency preparedness in the event of any emergency situation. Centra periodically conducts emergency simulation exercises, to test and improve the emergency response preparedness.

Centra has developed and deployed standards and procedures to help ensure that safety, quality and consistency considerations are embedded in the design, construction and operation of the natural gas distribution systems. Centra has developed and deployed comprehensive training programs to ensure that personnel performing natural gas related work tasks are qualified and trained to perform the work in a safe manner.

Public education initiatives are

undertaken to promote awareness of natural gas leak detection and response to hazards and requirements associated with excavations near the Utility infrastructure, natural gas appliance maintenance requirements, combustion air requirements, carbon monoxide hazards, and care for natural gas pressure regulators and meters installed at customer premises.

MS. MARLA MURPHY: Mr. Case, could you please advise the Board of the status of the AMR or Automated Meter Reading Project?

MR. DAVID CASE: Manitoba Hydro does not have a business case to fully implement AMR solution. It is the Corporation's intention to first determine if there are sufficient business and customer service benefits to pursue such a project through a pilot project.

The pilot will involve two thousand (2,000) gas and electric meters, and will cost approximately eight hundred thousand dollars ($800,000), approximately half of which is attributable to each utility.

The main intent of the pilot project is to obtain actual data on the installation costs and determine whether there are sufficient, realistic benefits regarding meter reading costs and enhanced customer service.

The pilot project will deal with some current operational problems by targeting meter reading routes with a high number of problems relating to access to customer premises and skipped meter readings.

By converting a small number of routes, the Company can more thoroughly evaluate the data returned by these test sites.

MS. MARLA MURPHY: Mr. Case, given that Centra is presently at the stage of seeking internal approval for the pilot project, why has Centra included the projected costs in the 2005/06 test year?

MR. DAVID CASE: Centra is projecting a cost to implement a pilot AMR project that will enable it to make informed decisions before proceeding with the full implementation of an AMR. The forecast costs are based on moving forward with the pilot and future implementation. Future implementation is of course conditional upon the success of the pilot project and the cost benefit analysis identified in the pending business case.

This is the best estimate of the Corporation at the time of the preparation of the IFF, and continues to be a reasonable estimation of the cost to be incurred in the forecast year.

MS. MARLA MURPHY: Mr. Case, would you please update the Board on Centra's rural expansion activities?

MR. DAVID CASE: Centra does not have any formal rural expansion plans for Manitoba at this time. Centra does, however, continue to respond to requests of natural gas service extensions by potential customers. One (1) such project is the Shoal Lake Natural Gas Development, which has recently received government funding.

MS. MARLA MURPHY: Could you please discuss the services provided by Manitoba Hydro Utility Services to Centra?

MR. DAVID CASE: Manitoba Hydro Utility Services provides all meter reading services for Centra. In addition to this service, Manitoba Hydro Utility Services also provides trained labour to Centra on a temporary basis, usually during peak construction periods to perform services such as gas meter changes, disconnection and re-connections, riser rehabilitation and construction and maintenance assistance.

The meter reading rates charged by Manitoba Hydro Util -- Manitoba Hydro Utility Services have remained unchanged for the past six (6) years. Centra also benefits from the availability of trained labour being available to it as needed without incurring costs of training or permanent employment.

Centra believes that its gas customers receive excellent value for the services provided.

MS. MARLA MURPHY: Thank you, Mr. Case.

Mr. Chairman, that concludes the direct examination and the Panel is available for cross-examination.

THE CHAIRPERSON: Thank you.

Mr. Peters...?

MR. BOB PETERS: Yes, thank you.

Good morning, Panel. For those who are new to the Panel and those who haven't been here for a while my questions are aimed at the Panel and the person best able to answer is welcome to do so.

And should anybody else want to supplement that answer, again, you're welcome to do so from my perspective.

CROSS-EXAMINATION BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Warden and Mr. Rainkie, when the Board looks at the Application which was found at Tab 1 of the Book of Documents that I had circulated they're not going to find a request from Centra to change the regulatory methodology that is utilized by the Board are they?

MR. DARREN RAINKIE: Mr. Peters, there is no specific request outlined, but I think it's quite clear through the materials that we've calculated the proposed revenue requirements based on the cost of service methodology.

MR. BOB PETERS: While you have calculated the revenue requirement based on a cost of service methodology, Mr. Rainkie, you've also included the revenue requirements on a higher level based on a rate base rate of return methodology, correct?

MR. DARREN RAINKIE: That's correct, Mr. Peters. We are following the direction of the Board in Order 131/04.

MR. BOB PETERS: Is Centra specifically requesting a change in the regulatory methodology that is utilized, Mr. Rainkie, or is that a matter that you are leaving to the Board to decide and stating only your preference?

(BRIEF PAUSE)

MR. DARREN RAINKIE: I guess, Mr. Peters, ultimately the methodology that the Board wants to use is it's under its discretion and we've, I guess, heavily stated our preference in the materials and -- and the direct of Mr. Warden that he just put on the record a few minutes ago.

But definitely we see virtue in moving to the cost of service methodology and I think that's been a consistent position since the 1999 acquisition hearing.

MR. BOB PETERS: Well, let's talk about the history then, briefly, Mr. Rainkie. You will agree that when your -- when your paychecks were signed by West Coast Energy Centra was regulated on a rate base rate of return methodology; is that correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And rate base rate of return is but one (1) of many methodologies of regulating a gas utility; would you also agree with that?

MR. DARREN RAINKIE: I would agree with that, yes.

MR. BOB PETERS: Would you also agree that in essence there is no right or wrong methodology although there may be preferred methodologies?

MR. DARREN RAINKIE: I would agree with that. There's nothing that's right or wrong about either one of them. I think you have to look at the circumstances and apply the one that makes the most sense in the circumstances.

MR. BOB PETERS: And would I be correct, Mr. Rainkie, in interpreting your comments this morning and Mr. Warden's comments this morning as saying because a cost of service methodology would be consistent with the internal reporting requirements by Manitoba Hydro, that is the primary reason that would be of benefit to Centra also in switching to cost of service methodology?

MR. DARREN RAINKIE: I would state it just a little bit differently, but I think you've got the gist of what we were saying. Just to simplify it down to one (1) simple question that the Board, I think, could ask itself is, what is the best information that it can use in making its rate determination?

Would you rather use exactly what senior management and the board of directors has provided in terms of their recommended financial forecast and the -- and the rate changes included in that forecast or would you rather take those numbers and dump them into a textbook regulatory methodology and then try to reconcile the two (2)?

So, I think if the Board wants to get into the mind and management of senior management in terms of how they're looking at the -- the financial integrity and financial position of Centra and what the rate changes should be flowing from that, that's the best information to use.

MR. BOB PETERS: I'm not sure we'll have any disagreements over this Mr. Rainkie, but, in Tab 10 of the Book of Documents that I prepared and circulated last week, I attach some extracts from Board Order 146 of '99.

Have you a copy of that sir?

MR. DARREN RAINKIE: I do.

MR. BOB PETERS: And on page 73 -- well first of all this order 146 of '99, was the Order in which the Public Utilities Board approved Manitoba Hydro's acquisition of Centra's shares; is that correct?

MR. DARREN RAINKIE: The Order approved the sale of the shares from West Coast Energy Inc. to Manitoba Hydro; just a particular quirk of the Act, I guess.

MR. BOB PETERS: All right. Thank you. And then in the Board's Order on page 73 under Board findings, the Board goes on to indicate that, many of the Intervenors wanted strong -- to provide strong support for the continuing and perhaps expanded regulatory oversight required by the Board. And also there was continuing oversight referenced in a letter from the Competition Bureau.

Are you familiar with that, Mr. Rainkie?

MR. DARREN RAINKIE: Yes Mr. Peters.
MR. BOB PETERS: And to you knowledge, that's accurate?
MR. DARREN RAINKIE: I'm reading it as we speak.
MR. BOB PETERS: But, you don't disagree that that was the thrust of the Hearing in what was -- what the Board had summarized?
MR. DARREN RAINKIE: That's correct. Centra wasn't a formal participant at that Hearing, but I was in attendance in the gallery and I recall those discussions.
MR. BOB PETERS: And at the end of the day, the Board looked at it and said, all that is being asked of us -- asked of the Board was to approve a transaction; is that correct?
MR. DARREN RAINKIE: That's correct.
MR. BOB PETERS: And there was no intention of the Board's jurisdiction over Centra or Hydro changing as a result of the acquisition transaction?
MR. DARREN RAINKIE: That's correct. The only application that was in front of the Board in that proceeding was the application of West Coast Energy Inc. to sell its shares to Manitoba Hydro. The Board

looked at four (4) broad areas in approving that transaction. One (1) was the impact on regulation and concluded that there was no application before it, in terms of changing regulatory methodologies. Of course, at that point they canvassed the various parties on what their preferences going forward.

But, the approval of the transaction itself didn't change the regulatory methodology.

MR. BOB PETERS: And one (1) of the parties that was canvassed was that of the parent company, now Manitoba Hydro; is that correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And even after canvassing the parties, Mr. Rainkie, the Board concluded, as I see on page 73 of the Order, that the transaction will not change any existing regulatory, statutory requirements, which include Centra being regulated on a rate base rate of return basis?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And likewise, Manitoba Hydro will continue to be regulated or have its rate set on a cost of service basis?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: In a previous answer to me this morning, Mr. Rainkie, I'd understood you to be saying that Centra filed this Application before the Board on both the cost of service basis and a rate base rate of return basis essentially because the Board requested it.

Would you agree with that?

MR. DARREN RAINKIE: Well, I think we put forward that invitation at the 2004/05 Cost of Gas Hearing and the Board indicated in their order that came out of that, Order 131/04, that was an appropriate idea and that we should proceed on that basis.

MR. BOB PETERS: One (1) other item of history, Mr. Rainkie, is that was it approximately in the year 2000 that Centra filed a GRA on a cost of service basis; it might have been based on a 2001 future test year?

MR. DARREN RAINKIE: My recollection, it was a 2001/02 GRA based on the cost of service methodology, yes.

MR. BOB PETERS: And while that was filed on a cost of service methodology basis, various concerns were raised as to the sufficiency of the detail of the materials; is that correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And as a result of some of those concerns, the Public Utilities Board ordered additional information be filed to allow the Board to assess the application?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And one (1) of the areas of concern was the -- the comparability of information from 1998 through to 2001?

MR. DARREN RAINKIE: Mr. Peters, I'm not sure what you mean by comparability. I think one (1) of the directives that came out of the -- that was a pre-hearing conference order, I think it was 14/01.

I don't recall comparability being a big issue, but I think the Board wanted information, obviously going back to the 1998 year, which was the last test year application that had been before the Board previous to that.

MR. BOB PETERS: Thank you, Mr. Rainkie. Flowing from that -- that Order 14 of 01, am I correct in recalling that Centra withdrew its application?

MR. DARREN RAINKIE: Ultimately I think that was in relation to our concern over increased gas costs and the change in the agreement with respect to paying income tax in lieu in the future. So I think it was a -- a monetary consideration that resulted in us withdrawing the application; not so much the requirements to file more data.

MR. BOB PETERS: I -- I wasn't suggesting it was the requirement that caused you to refile it, but as you mentioned it, the application was withdrawn, and it was withdrawn after Centra had obtained an indication from the Province of Manitoba, that it would not require payments in lieu of income tax in the future.

MR. DARREN RAINKIE: That's my recollection, yes, Mr. Peters.

MR. BOB PETERS: And recognizing that concession by the Province, Centra also determined that applying for a General Rate increase at a time when the commodity costs were sky rocketing, would not be appropriate.

MR. DARREN RAINKIE: I remember that being a factor as well, Mr. Peters, yes.

(BRIEF PAUSE)

MR. BOB PETERS: Can you tell the Board what benefits will result, should there be a change in the regulatory methodology from cost of service to rate base rate of return?

MR. DARREN RAINKIE: Well, I -- I think one (1) of the benefits in the -- ultimately a Crown owned utility is that you have the flexibility, as Mr.

Warden mentioned in his direct evidence this morning, to look backward and say to yourself, what's happened since the last General Rate Application in terms of net income and reserves and cost.

You also have the benefit to look forward into the integrated financial forecast ten (10) years into the future and say, how does the rate change that's before us today, impact, you know, the future financial liability of the Company.

And as Mr. Warden mentioned, the cost of service methodology, inherently allows rate smoothing. And it allows you to make judgments about the pace of attainment of the financial targets, whereas rate base rate of return, at least in the way it's been applied, historic to this and other jurisdictions, tends to look at one (1) particular test year.

It's a build-up methodology, it builds up your costs, and it says after you look at all your line items and add them up, it equals your total revenue requirement. It doesn't allow you a lot of flexibility, in terms of judgment and attainment of -- of financial targets.

And as I -- I guess I mentioned in a couple questions to you before, I think the best information that the Board can look at in making its determination is the very same information that senior management and the Board of Directors has used in -- in putting forward their proposal, you know, in terms of transparency.

You dump that information into another regulatory methodology, and then we're forever comparing the IFF to the rate base rate of return calculations. And as we've seen through this Proceeding, that can get a little bit confusing, moving between the two (2) methodologies.

So you know, in a -- in a Crown corporation where reserves are there for financial viability and financial stability, I think the cost of service methodology is better than looking at a rate base rate of return methodology that concentrates on return on equity in a specific test year.

MR. BOB PETERS: Well, Mr. Rainkie, you've tried to explain to the Board one (1) of the benefits of switching to a cost of service methodology from a rate base rate of return methodology.

Are there any other current problems other than those that you've just now identified, that would suggest a change is required?

MR. DARREN RAINKIE: I'm not sure there are current problems, I think it would be a further benefit if both sides of Manitoba Hydro's business, that being gas and electricity, could use the same methodology in going forward. It would also eliminate some of the cost and time associated with developing the rate base rate of return calculations.

But I'm -- I'm not, unless Mr. Warden can come up with other dire problems, I'm not sure that it's -- it's that's difficult, but it -- it certainly is a preference in moving forward.

MR. BOB PETERS: I appreciate that answer, Mr. Rainkie.

The -- one (1) of the comments you just made was dealing with time to prepare on a rate base rate of return; that was in fact done on -- in this case, correct? And --

MR. DARREN RAINKIE: That's correct. We provided both calculations.

MR. BOB PETERS: -- and in providing both calculations would I be correct in assuming that the time commitment to provide both was no onerous?

MR. DARREN RAINKIE: It's not perhaps -- onerous is a onerous word, Mr. Peters, but I would say it took more time to produce the rate base rate of return calculations after the IFF was finalized and it -- and that resulted in the application probably being filed later than it would have if we would have went purely on a cost of service basis.

We're not going to eliminate two (2) positions but it -- it does take time to crank out those calculations. They -- you just don't press a button and then instantly appear. You have to go back to your accounting records and pull out the right amounts and do the -- all of the detailed schedules that are entailed with a rate base rate of return methodology.

So it's -- it's not onerous but it definitely is time-consuming and it -- it contributes to a longer timeframe in terms of developing and filing applications with the Board.

MR. BOB PETERS: Are you able to quantify that time, Mr. Rainkie?

MR. DARREN RAINKIE: Well, Mr. Peters, only to the extent that I can look at history and usually Manitoba Hydro has been able to deliver its rate applications about a month or so after the board of directors' meetings.

And I think in this particular circumstance it took us two (2) months. So, you know, it -- it might be as long as an extra month in terms of timing.

MR. BOB PETERS: You indicated it also

took an extra two (2) -- essentially two (2) EFT's to pull the materials together?

MR. DARREN RAINKIE: No, sorry, Mr. Peters. I was saying that -- that if we stopped doing these calculations it's not going to result in two (2) people being out of work. But it -- it's an opportunity cost in that those individuals are fully engaged in other activities and if they don't have to do those calculations they can -- they can see to their other -- their other duties.

MR. BOB PETERS: Thank you for that, Mr. Rainkie.

Mr. Warden and Mr. Rainkie helped us give Ms. Murphy a bit of a heads up that, do you agree that one (1) of the issues surrounding the cost of service versus rate base rate of return methodology has to do with the statutory requirements that are imposed on the Board?

MS. MARLA MURPHY: That's certainly an issue that's been -- been raised and I expect it's one that we'll deal with in final submissions. But I wouldn't want to put our witnesses in the position of having to give a legal opinion today.

They do like my hat but I'd like to keep it off them if I could.

MR. BOB PETERS: I thought we heard in the first week, Ms. Murphy, that Mr. Warden was looking for that honorary degree. I thought maybe that's what he was having bestowed tomorrow morning and he couldn't be here.

But your comment is well-intended, Ms. Murphy. It's not my intention, Mr. Chairman and Board Members, to ask of the Panel members any -- any legal opinion; that is, as Ms. Murphy identifies, probably a matter that's more appropriate for closing submissions, not only by her but by any other party.

What I would like to do though, Mr. Chairman, is to make sure that when we do hear from parties in closing submissions that the sections of the PUB Act that may be applicable are addressed.

And, to that end, Ms. Murphy, I would just like confirmation that at Tab 11 of the Book of Documents that I've prepared and circulated there's a copy of Section 61 of the PUB Act and that would be one (1) of the sections that would be addressed in closing submissions?

MS. MARLA MURPHY: Yes.

MR. BOB PETERS: And, likewise, flipping ahead to Part 4 of the Act which starts at Section 112, there's Section 127 included as the last page in the extracts in Tab 11 and that would be another section that the Board can expect some comment on in closing submission?

MS. MARLA MURPHY: Yes, that's right.

MR. BOB PETERS: Appreciate it and thank you very much.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Rainkie, leaving aside the legislative requirements that may or may not exist, am I correct in reading your Application that Centra intends, even if cost of service methodology is used, to also to continue to calculate rate base?

MR. DARREN RAINKIE: Mr. Peters, this was -- we were hoping that this would be a transition year in which we could provide both sets of calculations to the Board and the Board could get comfort that cost of service is an appropriate methodology to use.

If we -- we would like, in future applications, to only provide cost of service if that is the -- if that is the decision of the Board. That is our preference.

The calculations surely can be done, but as I said they contribute to longer timeframes and can be confusing moving back and forth between two (2) methodologies.

But, definitely our stated preferences is -- is to file future GRA's only on cost of service methodology, if the Board deems that to be appropriate.

MR. BOB PETERS: Mr. Rainkie, at Tab 12 of the Book of Documents that you have in front of you, there's an extract from PUB/Centra Interrogatory number 91, do you have that sir?

MR. DARREN RAINKIE: I do, Mr. Peters.

MR. BOB PETERS: Starting on line 21 of page 1 of 2 of that answer, Mr. Rainkie, I had interpreted the Company's response to indicate that in the future Centra will continue to calculate a net investment or rate base which would include many of the items that are traditionally calculated as part of rate base?

MR. DARREN RAINKIE: That's correct, Mr. Peters. Our cost allocation model does many of its allocations based on plant and we would continue to provide those calculations. I think even Manitoba Hydro on the electric side provides a pseudo rate base calculation in its cost allocation process.

I think that's different than continuing to provide all the calculations in total revenue requirement. For instance, working capital, would we continue to do a fairly lengthy lead lag study or would we use some more of a simple methodology, kind of rule of thumb, if you like.

So, while we would continue to do those calculations for cost allocation, I'm not sure they would be as robust, as if we would come forward to the Board and present both sets of methodologies for their consideration.

MR. BOB PETERS: All right. So, when I read that answer to question 91(b), there's an indication that for cost allocation purposes relatively few differences exist between cost of service and rate base rate of return. The difference is primarily the replacement of a formulaic return on rate base with finance expense and net income, which has a component of judgment associated with it.

In either case, these costs will be allocated on the basis of rate base.

When I read that answer, Mr. Rainkie, does that suggest that the calculation of rate base itself will be less robust to use your words?

MR. DARREN RAINKIE: Well, the only area where I can think that it would be less robust might be like I just mentioned in the working capital calculation. The lead lag study takes a fair amount of time to go through and calculate. And what we might do is use a rule of thumb, like we used to use many years ago in this jurisdiction for that component. Or perhaps might pull something off of the balance sheet as a pseudo calculation of working capital.

But, I think most of the other calculations come out of our financial records and we can provide those in the future. But, I think there's -- that's a different thing than continuing to present a full rate base rate of return calculation at each hearing in the future.

MR. BOB PETERS: In retrospect --

MR. DARREN RAINKIE: Sorry, Mr. Peters, I would also add that there's two (2) parts to this equation; rate base and rate of return. And you know, while we've continued to use the rate of return formula, it is ten (10) years old and as you recall, Mr. Peters, if we want to revisit the rate of return and capital structure in a major way, that's a significant chunk of the Hearing.

That's probably three (3) days of hearing and $250,000 of experts between ourselves and CAC. So, you know, to continue to rely on that without some type of review, probably would require some type of review in the future. Given that Manitoba Hydro isn't looking at a return and equity out of Centra, I don't think we can see fit to spend that kind of money just to provide a calculation for the sake of providing it.

MR. BOB PETERS: We'll come back to that return on equity matter, Mr. Rainkie, but before I leave the rate base side of that equation, I read from the Application that it still would be Centra's intention to file the rate base calculations in any event, whether you used a working capital rule of thumb or an actual lead lag study?

MR. DARREN RAINKIE: Well, Mr. Peters, they would be inherent in some of the allocations, in the cost allocation model. But our preference is to not have to provide the equivalent of Tab 5 in this Application in the future.

There might be a summary calculation included in Ms. Derksen's materials, but we wouldn't write up sixty-five (65) pages or fifty (50) pages of commentary and have, you know, thirty-five (35) schedules in the Application. It might be simply a summary calculation in her cost allocation material.

MR. BOB PETERS: So, does that answer indicate that the Board would not be asked to approve rate base regardless of the methodology chosen?

MR. DARREN RAINKIE: Well, if the Board

determines that we can move forward on a cost of service basis, we'll present our revenue requirements on a cost of service basis only. And, as I said, inherent in the cost allocation model would probably be a pseudo-calculation of rate base so that Ms. Derksen could continue to perform certain allocations based on plant.

We wouldn't be asking for a specific approval of that rate base number but in approving rates the Board would, I guess inherently, be looking at those calculations and making sure that they were reasonable.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Rainkie, at Tab 12 of the documents, referring back to that PUB/Centra/91 Information Request, I took from the answer that whether the Board was using a cost of service methodology or a rate base rate of return methodology, the components of the revenue requirement are identical except for finance expense and net income; have I got that right?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And the difference is that under rate base rate of return you have a formula to deal with finance expense and net income -- sorry, to deal with the -- with the return on rate base but under the cost of service methodology the finance expense and net income has a component of judgment associated with it?

MR. DARREN RAINKIE: Well, Mr. Peters, the net income would have a component of judgment associated with it. Finance expense under cost of service would be the calculation of finance expense coming out of the IFF.

MR. BOB PETERS: So, essentially, the finance expense would be the same under either methodology?

MR. DARREN RAINKIE: Well, because there's a specific way of calculating financing costs as a return on debt portion of return on rate base, there will be some differences.

As I mentioned, we have a lead, lag study on the rate base rate of return side whereas the IFF model will look at the expected cash flows in and out and calculate working capital on that basis.

So the two (2) won't be exactly the same. I think they throw up fairly similar numbers but -- but because they have two (2) different methodologies they won't be exactly the same. But I wouldn't say that finance expense under cost of service is totally judgmental because it has a -- it has an -- it has a calculation in the IFF to support -- to support the determination of that line item.

MR. BOB PETERS: All right. Then you would agree with me, Mr. Rainkie, that the finance expense under cost of service is based on a forecast of what your actual interest on debt will be?

MR. DARREN RAINKIE: That's right. And interest on working capital requirements as well inherently are part of that calculation.

MR. BOB PETERS: And in terms of the rate base rate of return methodology, that finance expense is the average debt cost that's weighted?

MR. DARREN RAINKIE: That's for the long-term debt component, yes. And then there's an element added in for the short-term debt cost as well.

I might add though in terms of judgment, Mr. Peters, is that as I was trying to discuss just a few minutes ago, right now we have a formula for rate -- for rate base rate of return. But, from time to time, you know, it's necessary to refresh that in terms of what's the appropriate capital structure and what's the appropriate return on equity.

So, there is an element of judgment in determining a capital struct -- the appropriate capital structure and appropriate return on equity under rate base rate of return.

The formula has took an element of that judgment away but at certain points in time it might have to be refreshed as well. And I'm not really relishing the fact of sitting here and saying, well, what's the appropriate rate of return and capital structure for a -- for a -- a Crown Corporation using private -- you know, using the -- the, kind of, methodology and the types of discussions that we have that usually are there under a private context.

So, you know, it's -- it's -- I just wanted to make sure that's clear is that rate base of return is a formula methodology but there are judgments on the board's part in terms of capital structure and return on equity.

MR. BOB PETERS: And your point, Mr. Rainkie, is that if and when the Board has to reconsider the appropriate return on equity as well as the capital structure, that would be a matter of expert evidence and in making their decision there would be a matter of judgment that would have to be applied?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: All right. But back to the cost of service methodology, Mr. Rainkie. In determining net income that has a component of judgment associated with it also, correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And in the absence of a formulaic approach to the return on equity, how would the level of net income be determined under a cost of service methodology?

MR. VINCE WARDEN: Well, Mr. Peters, I think we would equate it to what we do on the electricity side of the business which is to look at our long-term financial targets, make some decision about the current conditions, the rate of inflation, the rate increases that have been implemented over the past, and such things as in the case of electricity business, water conditions.

So there is a -- a lot of judgment that goes into the determination of what an appropriate rate application should be at any given time. So it depends on the circumstances and, as Mr. Rainkie indicated, judgment is -- is very much a part of the process.

MR. BOB PETERS: So, I take it that the judgment that you're talking about, Mr. Warden, would be the judgment not only of the management but the executive and the Board all flowing through Centra Gas Manitoba Inc.?

MR. VINCE WARDEN: Well, ultimately, it's the board that determines what recommendation comes forward to this Board based on recommendation of -- of senior management of the Corporation.

MR. BOB PETERS: Mr. Warden, do you agree with me that there is no mandatory requirement that the form of regulation of the electric utility has to be the same as the form of regulation of the gas utility?

MR. VINCE WARDEN: There is no mandatory requirement. I agree with that, yes.

MR. BOB PETERS: And, Mr. Rainkie had outlined the preference of Centra to proceed under a cost of service methodology and -- and you agree with that for the reasons he gave?

MR. VINCE WARDEN: Yes, I -- I absolutely agree with how Mr. Rainkie put that forward. It certainly it would put the regulation of the electricity business, the gas business into a -- a common language.

The only time I or the other members of the executive of Manitoba Hydro look at rate of return is when we file the Centra rate application. It really is meaningless for a Crown corporation.

MR. BOB PETERS: If you could turn with me to Tab 13 of the book of documents. I just want to bring to the Board's attention, Mr. Rainkie, what you had indicated in terms of the components being the same under rate base rate of return as they are under cost of

service, with a couple of exceptions.
Have you got Schedule 3.0.0, sir, at Tab 13 of the book of documents?
MR. DARREN RAINKIE: I do.
MR. BOB PETERS: And when I look down that schedule, Mr. Rainkie, I note that the items such as cost of gas, other income, operating and administrative, depreciation and amortization and capital and other taxes, is the same for the test year regardless of the method of regulation, correct?
MR. DARREN RAINKIE: That's -- that's correct.
MR. BOB PETERS: And that's -- that's not fortuitous that's because those are actual calculations and numbers that are prepared?
MR. DARREN RAINKIE: That's right. That's the forecasts of those particular numbers and they're the same under either methodology.
MR. BOB PETERS: And when we -- when we get to items of finance expense you call it "finance expense" which is a cost of service term or it could be return on debt under the rate base rate of return methodology, correct?
MR. DARREN RAINKIE: That's correct.
MR. BOB PETERS: And there are minor --

I'll call them "minor" although the number is into the hundreds of thousands of dollars, Mr. Rainkie, but relatively minor differences in the -- in the finance expense or return on debt?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And that has to do with the cost of service finance expense being based on the forecasted actual interest on the debt issue as well as on the working capital?

MR. DARREN RAINKIE: That's right. They -- the -- the calculations are approached from a slightly -- they're -- they're intending to get at the same thing but they're approached from a slightly different perspective in terms of the methodologies that are used.

MR. BOB PETERS: And when we come to the rate base rate of return columns for either the '05/'06 test year or the '06/'07 test year, the return on debt is based on the average debt cost that has been weighted?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: When we come down to line 21 in the net income under the cost of service or the return on equity under the rate base rate of return, you're indicating, Mr. Rainkie, that the -- that the amount shown under cost of service as $1.779 million is the net income that would be included in the '05/'06 test year under a cost of service basis?

MR. DARREN RAINKIE: That's correct, Mr. Peters.

MR. BOB PETERS: And that was based on corporate judgment?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: Whereas the rate base rate of return number that's shown is based on the formula that's currently being utilized by the Corporation?

MR. DARREN RAINKIE: That's correct, Mr. Peters.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Rainkie, recognizing what you've told the Board in terms of rate base rate of return side and the formula that's used, the amount that's shown here is based on the formula, correct?

MR. DARREN RAINKIE: Mr. Peters, are you talking about the amount for the return on equity?

MR. BOB PETERS: Under column 2, line 23 those intersect in the '05/'06 test year showing a return on equity of about $11.8 million, correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And twelve point six (12.6) shown over on column 4 under the '06/'07 test year?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And those are items, Mr. Rainkie, that are based on the formula as presently interpreted by the Utility?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And while you've used what the formula applies, Mr. Rainkie, you could also, I suppose, come in and ask for something less than the formula applies; do you agree with that?

MR. DARREN RAINKIE: I guess it's a possibility, yes, Mr. Peters.

MR. BOB PETERS: When we look at the rate base rate of return columns 2 and 4, Mr. Rainkie, when we add the finance expense, that finance expense is to include the return on the short-term debt and the long-term debt, correct?

MR. DARREN RAINKIE: I think that's -- that's right. What we're trying to do is -- is forecast our total interest expense and -- and through short-term and long-term borrowings, yes.

MR. BOB PETERS: And then when you add to that the calculated return on equity of about $11.8

million that comes up with a figure of approximately $30 million as the overall return?

MR. DARREN RAINKIE: That's -- yeah. Commonly referred to as the return on rate base in past proceedings. Yes.

MR. BOB PETERS: And the return on rate base is -- is -- is the debt -- is the return on the debt component as well as the return on the equity component?

MR. DARREN RAINKIE: That's correct. I'm reminded that we've included some interest expense on common assets and inventory in that calculation as well. But those are financing costs like anything else.

So, I just wanted to make -- make sure that was clear; that we've calculated the traditional return on rate base as rate base times the overall rate of return and we've added in interest on common assets and inventory to that equation as well, Mr. Peters.

I might add that -- that treatment, it's not new, that was approved in the 2003/04 GRA by the Board.

MR. BOB PETERS: Thank you, Mr. Rainkie. On the -- on the line item 23 under the cost of service models in both the '05/'06 test year and the '06/'07 test year, one number is 1.8 million and one is 11.3 million, correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And that fairly significant difference is, again, as a result of corporate judgment?

MR. DARREN RAINKIE: That's right.

MR. BOB PETERS: And, Mr. Rainkie, when the judgment can appear to be so vastly different from year over year, does that not suggest that a formula might be a more appropriate methodology rather than using someone's judgment?

MR. VINCE WARDEN: Mr. Peters, maybe I'll just jump in here. When we say "corporate judgment" we do refer to the amount of the rate increase that's being requested in each of those years.

So, in each of -- 2005/06, 2006/07, the rate increase applied for was 2.5 percent. So, the judgment was applied to the amount of the rate increase and that's the amount of net income that results in each of those years from that Application.

MR. BOB PETERS: Mr. Warden or Mr. Rainkie, is Centra aware of any other natural gas distribution companies in Canada that are regulated on a cost of service methodology?

MR. DARREN RAINKIE: I don't think it's something that we've looked at. First of all, you'd have to have, I guess, a Crown-owned utility. To be comparable you'd have to have a Crown-owned utility that owned both gas and electric and I'm not sure that exists.

Mr. Derksen reminds me of Saskatchewan, but of course they have a different way of setting rates altogether and I'm not sure I'm familiar with all their detailed calculations.

THE CHAIRPERSON: Mr. Peters are you amenable to taking a short break?

MR. BOB PETERS: Absolutely. I'm just at the end of my questions on this area and I'll move onto a new topic after the break then.

THE CHAIRPERSON: Okay. We'll take the break now.

--- Upon recessing at 10:30 a.m.
--- Upon resuming at 10:48 a.m.

THE CHAIRPERSON: Okay, Mr. Peters.

MR. BOB PETERS: Thank you.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Rainkie, just to tidy up where we left off before the break, would you agree with me, sir, that the fact that a gas LDC is a

Crown -- is Crown owned or privately owned that doesn't in and of itself dictate what method of regulation should apply?

MR. DARREN RAINKIE: I'm not sure what sure what the authoritative pronouncements are in terms of regulatory methodology, but, I would think it was a very important consideration in terms of what the most appropriate methodology is to regulate the Utility.

I don't see this as we need the slag rate base rate of return to get cost of service. I don't think the question is, which is the most theoretically best methodology, I think the question is, what's the best methodology given Centra's ownership -- current ownership structure?

So, I'm not sure what the defining criteria are in all the jurisdictions across the United States and the world, but, certainly the goals of the organization and how its owned should be an important consideration in that determination.

MR. BOB PETERS: In you answer, Mr. Rainkie, what you've really highlighted for the Board is that the change in ownership is the driving reason for the consideration of the change in regulatory methodology?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And Mr. Rainkie, Mr. Warden, if there was to be a change to the cost of service methodology, what does Centra suggest would be the Board's role in approving capital expenditures?

MR. VINCE WARDEN: Well, I think similar -- I can only judge by what we do on the electricity side of the business and similar to what we do there, the Board's role would be to approve the rate impacts of capital expenditures. That is the -- the costs flowing therefrom that affects the net income of the utility. So, that would be the fixed costs of interest depreciation on any capital additions that would flow to the -- to the ratepayer.

MR. BOB PETERS: Mr. Warden, would there be any ability for the Board to determine the prudence of any plant additions, that is assuming the gas side was regulated on a cost of service methodology?

MR. VINCE WARDEN: There isn't quite the same motivation of the Utility to add to rate base; that is the higher the rate base under a rate of return methodology, the higher the return. So, therefor the same level of scrutiny over capital expenditures under cost of service methodology is not required.

MR. BOB PETERS: So, Centra would see there being a -- no longer any need for the Board to review and ultimately approve the capital expenditures if it changed the methodology to cost of service.

MR. VINCE WARDEN: That's right. There'd be no need to review and approve on a line by line basis, certainly under the cost of service methodology base. Within the purview of the -- of the Board, the Public Utilities Board to look at capital expenditures and to comment thereon, but not to approve the individual line items of the capital expenditure forecast.

MR. BOB PETERS: From that answer, Mr. Warden, if there was an expenditure that was considered imprudent by the Board, how would that be treated under the cost of service methodology?

MR. VINCE WARDEN: There has never been a precedent for that to my knowledge, there has never been a capital expenditure incurred under the cost of service methodology that has been deemed to be imprudent, and I would expect the same to apply.

There is no motivation for the utility to add capital expenditures to rate base, other than those expenditures that are necessary to provide a safe reliable service to -- to customers.

MR. BOB PETERS: So, I take from those last couple of answers, Mr. Warden, that under a cost of service methodology there would be no Board review of the prudency of any capital additions, and therefore that would remove any risk of disallowance.

MR. VINCE WARDEN: The disallowance under a cost of service methodology comes in the form of a reduced approval of a Rate Application, that is the Board can determine that rates will not be as high as applied for by the Utility, and -- and that way indirectly disallow an expenditure. But there's no direct provision for disallowance of specific expenditures under a cost of service methodology.

MR. BOB PETERS: But let's also be clear for the Board that the Board permits the gas utility to come before it on a future test year basis, correct?

MR. VINCE WARDEN: As it does with the electric utility, yes.

MR. BOB PETERS: And so the expenditures that you come before the Board with would be forecast expenditures, as opposed to already committed, correct?

MR. VINCE WARDEN: That is correct, not to say there isn't a retrospective look at costs incurred.

MR. BOB PETERS: But looking forward in terms of capital expenditures, if the Board was to reduce under a cost of service methodology, the rate request of the Corporation, that would simply be telling the

Corporation that it would have to reduce its expenditures somewhere along the line from what it brought before the Board?

MR. VINCE WARDEN: That's correct.

MR. BOB PETERS: And the Company would have to determine where that was?

MR. VINCE WARDEN: That is right.

(BRIEF PAUSE)

MR. BOB PETERS: I want to turn to a new area. And in that discussion with the Panel, Mr. Rainkie, you've agreed with me that Order 149 of 99, which I think had some extracts at Tab 10 of the Book of Documents I have provided you with, that Order approved a transaction of the sale from Westcoast to Manitoba Hydro, correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And inherent in that sale there were risks that were going to result; is that correct?

MR. DARREN RAINKIE: I think the Board, yeah, noted that there are certain risks in any type of acquisition transaction.

MR. BOB PETERS: And those risks would

fall to the purchaser?

MR. DARREN RAINKIE: That's generally my recollection of the Board's view on that issue, yes, Mr. Peters.

MR. BOB PETERS: And those risks, for example, Mr. Rainkie, would include such things as management -- management risk and weather risk, those types of things?

MR. DARREN RAINKIE: Mr. Peters, I'm not clear what the question is. I thought you were talking about the risks of the -- the transaction itself, in terms of obtaining the synergies and -- and the like. The -- the weather risk in that is -- would be inherent under any type of ownership, it's not associated necessarily with the -- with a change in ownership.

MR. BOB PETERS: All right. Then the synergy risks you say -- you would agree with me, Mr. Rainkie, would be a risk that would be on the management of -- of the purchaser?

MR. DARREN RAINKIE: Well, it depends where you record the benefits and the costs of the transaction. And I think that's what we've been discussing in the last two (2) or three (3) Hearings all the way from Order 146/99 to Order 208/02, Order 118/03 and now we've been wrestling with the equation in terms of where the benefits and the costs flow on either -- to either utility or probably more appropriately to Manitoba Hydro.

MR. BOB PETERS: All right. Well, let's -- let's go down that road a little bit, Mr. Rainkie. When Manitoba Hydro acquired the shares from West Coast Energy, Manitoba Hydro's plan was to pay the acquisition costs through the synergy benefits that would result; would you agree with that?

MR. VINCE WARDEN: Not really, no. No. It was not intended that the synergy benefits would ever cover the costs of the -- of the acquisition.

MR. BOB PETERS: I'm sorry, Mr. Warden, I didn't catch your last answer. You're suggesting that the synergy benefits were no part of the equation to pay for the acquisition costs?

MR. VINCE WARDEN: No, they're part of the equation. But it was never intended that the synergy benefits would fully cover the costs of the acquisition.

MR. BOB PETERS: What was intended would be required in addition to the synergies, Mr. Warden?

MR. VINCE WARDEN: Well, ultimately the -- the intention at the time of the acquisition is that ratepayers -- Centra ratepayers would be better off than they would otherwise be under the previous ownership and that was the commitment that was made.

There was an estimate of synergies that were put forward at the time of the acquisition but it was never intended that those synergies cover off the full cost of the acquisition.

MR. BOB PETERS: When we look at the full cost of the acquisition, Mr. Warden, do you agree that Manitoba Hydro was -- was essentially purchasing a cash flow that existed in Centra Gas?

MR. VINCE WARDEN: I never really looked at it as a cash flow. Manitoba Hydro was purchasing the shares of -- of Centra Gas for a negotiated price. But it wasn't a cash flow, no.

(BRIEF PAUSE)

MR. BOB PETERS: In order 208/02 found at Tab 14 of the documents, Mr. Warden or Mr. Rainkie, this was the Order in which the Board directed Manitoba Hydro to account for the transaction on Manitoba Hydro's book for regulatory purposes, correct?

MR. VINCE WARDEN: Correct.

MR. BOB PETERS: And when, for regulatory purposes of this transaction is this the same as the -- as the audited financial statements of the Corporation,

Mr. Warden?
MR. VINCE WARDEN: The question is whether the costs are being accounted for in accordance with this order on the audited financial statements, yes.
MR. BOB PETERS: There's no -- there's no separate books in terms of how you account for this transaction?
MR. VINCE WARDEN: There's no separate books, no.

(BRIEF PAUSE)

MR. BOB PETERS: And on turning to page 47 of Order 208 of 02 found at Tab 14 of the Book of Documents, this is where the Board indicated that the ratepayers of Hydro and Centra should be held harmless as a consequence to the transaction, correct?
MR. VINCE WARDEN: Correct.
MR. BOB PETERS: And the Board goes on that the risks and benefits associated with the transaction integration should accrue to the shareholders of Hydro?
MR. VINCE WARDEN: That was the Board's position. Yes.
MR. BOB PETERS: And that led to the

Board indicating that the recording of the costs associated with this should end up on the books of Manitoba Hydro?

MR. VINCE WARDEN: Correct.

(BRIEF PAUSE)

MR. BOB PETERS: When there is reference in the third sentence on page 47 to the risks and benefits accruing to the shareholders of Hydro, which risks and benefits is that interpreted as meaning?

(BRIEF PAUSE)

MR. VINCE WARDEN: Well, it is interpreted, I believe, and we are interpreting a statement of the Public Utilities Board, but I interpret those words to mean that any costs associated with the transaction, and any benefits flowing therefrom, should ultimately accrue to the shareholders of Hydro, and I'm interpreting by that, the electricity ratepayers.

Having said that, of course, the ultimate goal and commitment is to keep both electricity and gas ratepayers harmless as a result of this transaction, and that's what we've done.

MR. BOB PETERS: In the same order, in terms of risks and benefits, Mr. Warden, do you agree that one (1) of the risk would be whether or not management could find the synergies that were supposed to result from this transaction?

MR. VINCE WARDEN: Yes I agree. Synergies were very important to the -- to the success of the -- of the acquisition.

MR. BOB PETERS: And would you also agree that one (1) of the risks in purchasing the shares of Centra was whether or not the return on equity would materialize as -- as built into the rates?

MR. VINCE WARDEN: No, as I've said many times, return on equity is not something we were seeking, we weren't looking for a return to electricity ratepayers. We were looking, as we do, as a Crown corporation, we were looking to make sure that the -- the ratepayers pay no more, no less than the cost of serving those -- those customers.

MR. BOB PETERS: But the Corporation that Manitoba Hydro purchased in 1999, had built into its existing rates, then, a return on equity; correct?

MR. VINCE WARDEN: It did.

MR. BOB PETERS: And that return on equity has been in rates since 1999 through to and including what's before the Board today?

MR. VINCE WARDEN: Well, Manitoba Hydro has not reduced rates to remove any return on equity that was there previously, so on that basis, yes I would agree that is still embedded in rates.

MR. BOB PETERS: And also there was an amount embedded in rates when West Coast owned the gas utility for income tax, correct?

MR. VINCE WARDEN: Correct.

MR. BOB PETERS: And am I correct, Mr. Warden, that that amount was in the neighbourhood of $11 or $12 million a year?

MR. VINCE WARDEN: That is correct.

MR. BOB PETERS: And the initial intention was for that $11 or $12 million to be applied against the one (1) time tax liability that resulted as a result of Centra -- Centra's shares being purchased by Manitoba Hydro?

MR. VINCE WARDEN: Well there was a one (1) time tax payment as a result of the purchase, which had to be repaid in an orderly basis because the $11 million was already embedded in rates, that was a reasonable way to recover that cost.

MR. BOB PETERS: However, following Order 208/02, the Gas Company came forward in a -- in a hearing that gave rise to Order 118/03, and that income tax liability, that one (1) time tax liability, was -- was not paid off in seven (7) or eight (8) years by the income tax, but, it was rather amortized over thirty (30) years, correct?

MR. VINCE WARDEN: Yes and you -- you covered this briefly with -- with Mr. Rainkie earlier, and that is the decision of government to not require -- Provincial Government that is, to not require taxes to be paid on a going forward basis. Therefore, that allowed Centra to withdraw its application for a rate increase at that time.

MR. BOB PETERS: Is it put another way, Mr. Warden, instead of using all of that $11 million to pay off the tax liability, and -- and then get ready to pay -- pay the Government an amount, in lieu of taxes, in subsequent years, Centra used some of that money to avoid a rate increase to consumers?

MR. VINCE WARDEN: Correct.

MR. BOB PETERS: But of that $11 or $12 million that was in rates for income tax when Manitoba Hydro purchased the Corporation, you're presenting using approximately half of that to pay the one time tax liability, that is the principal amount over thirty (30) years plus the accrued interest?

MR. VINCE WARDEN: Well that -- that's what falls out of -- what was previously in -- in revenue requirement and -- and what we are now amortizing of that tax liability. We don't specifically identify it that way though, we look at what our total revenue requirement is in order to attain a level of net income for -- for Centra, sufficient to rebuild retained earnings; so that amount is not specifically identified for paying tax.

MR. BOB PETERS: But there is an amount specifically identified for tax, attributed to income tax; correct?

MR. VINCE WARDEN: In -- in part of the cost structure, that's correct, yes.

MR. BOB PETERS: And that's approximately half of the $11 or $12 million that's -- that was in rates?

MR. VINCE WARDEN: That -- that's right.

MR. BOB PETERS: All right, and turning to page 11 of Order 208/02, found at Tab 14 of the Book of Documents, there's a summary of the financial costs of the acquisition, Mr. Warden and Mr. Rainkie, have you found that on page 11?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And the upshot of it is that the net book value was $121 million, and the premium paid by Centra was another $121 million; would you agree with that?

MR. VINCE WARDEN: To get to the two forty-two (242), yes.

MR. BOB PETERS: It makes it easier when the numbers are the same for my math, Mr. Warden, but in subsequent PUB decision in -- in Order 118/03, there was reference, and -- and that -- I think in Tab 18 of the Book of Documents, there are some extracts from that -- there's also an extraneous page at the front of that, but the extracts to Order 118/03 are found.

And in Order 118/03 at -- found at Tab 18, I'm looking at page 65, and in the middle of the first paragraph, jumping a bit ahead here, but I'll come back to it, Mr. Warden, there's a reference to the Board that -- that there's an amount of money that includes a component related to purchase goodwill, and the write up of net assets to fair market value, which arguably should not be paid for by Centra ratepayers, but rather paid for by Hydro.

Do you see that statement?

MR. VINCE WARDEN: I do.

MR. BOB PETERS: And if I turn back to Tab 14, the write up in assets and the purchased goodwill would be the total of $121 million that is summed up by

adding up the write up of assets to fair market value,
the write up of liabilities, plus the goodwill?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: Can you tell the Board whether -- and -- and when I call that -- sorry, when I take the write up of assets to fair market value, and the write up of liabilities, and the goodwill, is it proper to refer to that as a premium that was paid by Manitoba Hydro for the shares of Centra?

MR. VINCE WARDEN: I don't have any problem with that, yes, I -- I think premium is an okay term.

MR. BOB PETERS: I'm not using it in a pejorative sense, but I'm just wondering if that's the accounting terminology that would be appropriate?

MR. VINCE WARDEN: We don't refer to it as a premium, it is the -- the excess of -- of the purchase price over the -- over the book value. But again, I don't -- I don't have a big problem with calling it a premium.

MR. BOB PETERS: All right, then I might use that for ease of -- ease of reference, and I have your -- your position on that. In the reference to the Board Order that I showed you from 118/03, found at Tab 18, there was a statement that arguably the write up of net assets to fair market value and the purchased goodwill should not be paid for by Centra ratepayers.

Do you recall that statement?

MR. VINCE WARDEN: Well I think that is the -- the inference from that paragraph, yes.

MR. BOB PETERS: And the inference would be that would be the -- the premium amount of the additional $121 million in excess of net book value.

MR. VINCE WARDEN: Again, that would be the inference, yes.

MR. BOB PETERS: Can you tell the Board in the Application that's before them, whether any of that $121 million premium is being paid for by Centra ratepayers?

MR. VINCE WARDEN: Well, yes, definitely to the extent that the corporate allocation is intended to recover the cost of the -- all the costs incurred in the acquisition of Centra.

Centra ratepayers are paying their fair share of the -- of the acquisition keeping in mind that both electricity and gas ratepayers are held harmless; that's the paramount consideration in the Utility's view, in that gas ratepayers are better off than they would otherwise be under the previous ownership.

MR. BOB PETERS: So, this Application

does include payment by Centra's shareholders -- sorry, Centra's ratepayers, its customers, on account of the -- of the premium?

MR. VINCE WARDEN: Well, as I just indicated, the corporate allocation is a -- is a means of recovering, from both electricity and gas ratepayers, the costs of the acquisition in a fair and equitable way.

MR. BOB PETERS: All right. If we turn ahead under Tab 208 to page 48, Mr. Warden, there's an indication, and I'm going to read under Point Number 2 from page 48 of Order 208/02 found at Tab 14 of the Book of Documents:

> "The Board notes that Centra's current rates include a component for rate of return. This component of Centra's rates plus realized synergistic savings will, over time, recover the acquisition premium and the financing charges related to the purchase price. The Board believes that this treatment is consistent with the economic intent of the transaction."

I've read that fairly accurately have I?

MR. VINCE WARDEN: You did it very well.

MR. BOB PETERS: Thank you. When -- when

the Board notes that Centra's current rates include a component for rate of return, that was approximately $15.1 million in rates based on the '03/'04 test year?

MR. VINCE WARDEN: That's right.

MR. BOB PETERS: And, in addition to that, it says:

"This component of Centra's rates..."

Meaning the return on equity -- sorry the rate of return on equity:

"... plus the synergistic savings..."

And those synergistic savings were not fully quantified at that time; would that be correct?

MR. VINCE WARDEN: That's correct.

MR. BOB PETERS: And it was intended from that then that the return on equity plus the synergistic savings would pay for the acquisition premium and the financing charges related to the purchase price.

Was that correctly the intention as stated by the Board?

MR. VINCE WARDEN: That was the intention as stated by the Board at that time, yes.

I should point out that the synergies, although not fully realized, they -- they were identified at the time that there was -- there was an estimate of what the synergies would be and we've been working towards attaining those synergies.

MR. BOB PETERS: All right. Thank you.

MR. DARREN RAINKIE: Mr. Peters, I would also add, this is the part of the Order I've never understood because I think the return on equity that was embedded in Centra's rates was intended to pay for the net book value and then it says:

"The synergy savings should pay for the acquisition premium."

Well, in a regulated utility, when you generate synergies, the shareholder doesn't get to keep them like it would in a private company. Those synergies are given back to customers in the form of reduced rates.

So, how a $15.1 million return could cover-off $242 million worth of acquisitions costs, I've never understood because it just doesn't work that way in a regulated utility when you generate synergy savings.

MR. BOB PETERS: Well, I have your point, Mr. Rainkie. But did the Corporation ever seek clarification from the Board in respect of Order 208/02?

MR. DARREN RAINKIE: I think we've been seeking clarification, one, through the 2003/04 General Rate Application and through this General Rate Application. This is -- we're still trying to deal with some of these clean up issues from five (5) or six (6)

years ago, Mr. Peters.
And I think we've finally landed on a -- on corporate allocation as -- as a good way of doing that.
MR. BOB PETERS: Well, we'll come back to it then, Mr. Rainkie, and maybe we'll find out the degree to which further clarification may be needed.
But we've seen the $242 million that had been considered the acquisition costs; that number has grown in these proceedings, Mr. Rainkie, to $253.8 million in terms of total costs, correct?
MR. DARREN RAINKIE: That includes also the acquisition and integration costs up and above the purchase price, Mr. Peters.
MR. BOB PETERS: And Mr. Rainkie, just to help the Board with that, at Tab 15 of the document -- Book of Documents, there's an extract from CAC/MSOS information request 100(e). And if I look on the attached schedule, the last page of it, this is the Corporation's reconciliation of going from a $242 million purchase price through those costs of acquisition and integration that you've talked about to come to a total of $253.8 million, correct?
MR. WILLIE DERKSEN: Yes, that's our calculation of that and I should also indicate that it

excludes certain of the integration costs that the Board view weren't appropriate. So, this doesn't represent the total of the acquisition and integration costs, only those amounts that were allowed by the PUB in its Order 208/02.

MR. BOB PETERS: Thank you Mr. Derksen. And you've showed those disallowed acquisition integration costs on line 36 of the schedule, correct?

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

MR. BOB PETERS: All right. But, following it through, we end up at a number of $253.8 million and that's the number that ends up on the books of Manitoba Hydro, have I understood that correctly?

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

(BRIEF PAUSE)

MR. BOB PETERS: Now, here's something Mr. Derksen, maybe you can help the Board out, yourself and your colleagues, when we have $253.8 million of total allowed costs there was and is a requirement that that be paid for on an annual basis, correct?

MR. WILLIE DERKSEN: Well, there's a requirement I think that the annual cost related to that $253 million be covered on an annual basis. That's correct.

MR. BOB PETERS: If I can draw your attention to Tab 17 of the Book of Documents, there's PUB/Centra 54 Information Request and there's attached to it a schedule and this schedule, Mr. Derksen, was to show the annualized costs associated with the acquisition of Centra, would that be correct?

MR. WILLIE DERKSEN: What this schedule shows is that if there was an original principal of $253 million and if $20.9 million was paid annually to extinguish that -- those costs, that if the interest rate that we financed the acquisition at, it would be extinguished -- the principal would be extinguished over thirty (30) years.

MR. BOB PETERS: Mr. Derksen, you weren't with us the first week, but Mr. Warden brought good news to the meeting or to the Hearing that $20.9 million is no longer needed and if I understood his evidence, it's now $19 million required on an annual basis.

Mr. Warden, have I got that right?

MR. VINCE WARDEN: No.

MR. BOB PETERS: So, you didn't bring good news?

MR. VINCE WARDEN: Maybe I can try one

(1) more time to clarify the difference between the twenty point nine (20.9) and the 19 million. The twenty point nine (20.9) was really put on the record, I believe, originally for illustrative purposes. And it's a very simple calculation as this schedule you were just referencing shows.

That if you were to amortize the costs over a thirty (3o) year period, that is all costs, principal and interest, over a thirty (30) year period, 20.9 is -- 20.9 million is a number required to do so.

The 19 million, however, is simply the carrying costs; that is the interest on that debt without repayment of that principal annually. So 19 million, the carrying costs, which includes actually 17 million of finance expense and $2 million of the amortization of the write-up of the fixed assets.

So, I hope that's clear.

MR. BOB PETERS: Oh, it's not, but, I'll keep working on it until one of us has a light turn on. It may be me Mr. Warden.

When I look then, if I take the Board and you to the schedule attached to PUB-17, you're telling the Board that on the $253.8 million of total acquisition integration costs over thirty (30) years, you'd need $20.9 million a year to -- to pay off the principal and the carrying costs?

MR. VINCE WARDEN: The principal and interest, yes.

MR. BOB PETERS: And are you now telling the Board that the principal will not be paid off in thirty (30) years?

MR. VINCE WARDEN: No, at the end of that thirty (30) year period, presumably we will have -- by the time we have written off the write-up, that I referred to earlier, the amount that we -- we will have at the end of that thirty (30) year period on Hydro's books, is the original investment of $242 million. So, that would still represent our investment in Centra Gas.

MR. BOB PETERS: When the Board looks at the $253.8 million number that Mr. Derksen and I just went through, that $253.8 million number includes the $121 million premium, does it not?

MR. VINCE WARDEN: Yes, it does.

MR. BOB PETERS: And your objective then is to pay off that premium over a period of thirty (30) years?

MR. VINCE WARDEN: The write-up of the fixed assets would be paid off over the thirty (30) year period, yes.

MR. BOB PETERS: So, that's the $121

million would then be the amount that you would seek to pay off, which is the premium or the write-ups?

MR. VINCE WARDEN: Yes, if we refer to -- again to Tab 14, page 11, that amount that we're amortizing over that thirty (30) year period is the net of the seventy-three (73) and the seventeen (17).

MR. BOB PETERS: Are you also amortizing the goodwill of 65 million?

MR. VINCE WARDEN: No, we're not.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Warden, and, Mr. Derksen, I thought I was with you, Mr. Derksen, when you told the Board that you had gone from $242 million up to $253.8 million, and that was going to be the sum total of the acquisition and integration costs; are we together on that?

MR. WILLIE DERKSEN: Yes, we're together on that.

MR. BOB PETERS: And if you could turn with me to Tab 15 of the Book of Documents. Tab 15 of the Book of Documents, Mr. Derksen, shows the total costs that we've now agreed upon as being $253.8 million, correct?

And that's on line 40.

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

MR. BOB PETERS: And I also see on the schedule at the back of Document 15, which is CAC/MSOS/CENTRA-100(E), that Centra intends to finance that $253.8 million entirely by debt?

MR. WILLIE DERKSEN: Well, that's how it was financed at the get go, Yes. There was a $250 million debt issue that was taken out and that's Hydro that financed it. The rest of it was short-term debt.

MR. BOB PETERS: All right. The decision as to how to pay for Hydro acquiring Centra's shares was a decision made by Manitoba Hydro, correct?

MR. VINCE WARDEN: Correct.

MR. BOB PETERS: Centra had no say in how that would be done?

MR. VINCE WARDEN: That's right.

MR. BOB PETERS: And Centra's ratepayers certainly didn't have a say in how that was going to be done?

MR. VINCE WARDEN: Nor did the electricity ratepayers.

MR. BOB PETERS: Because it was done by Centra's management and ultimately its board of directors?

MR. VINCE WARDEN: Centra's and Hydro's management at the time, yes.

MR. BOB PETERS: I suppose if, hypothetically at least, Mr. Warden, Manitoba Hydro could have brought in the piggy bank and paid $253.8 million of cash for that -- for its acquisition?

MR. VINCE WARDEN: There was no piggy bank to bring in.

MR. BOB PETERS: But, hypothetically it could have?

MR. VINCE WARDEN: Well, it would make no difference at the end of the day whether we had cash sitting around not being used, which wasn't the case, or whether we went to the market to borrow that -- that money.

We -- there would still be a cost associated with it.

MR. BOB PETERS: All right. Let's go from the $253.8 million of which Centra was going to -- which Centra -- I'm sorry, which Manitoba Hydro financed 100 percent through debt; we're together on that?

MR. VINCE WARDEN: We are.

MR. BOB PETERS: And then if we turn to the schedule attached to Document number 17 in the book of documents, which is the last page of PUB/CENTRA-54, that's the schedule on how that $253.8 million of debt was going to ultimately be retired; have I -- have I that correct?

MR. VINCE WARDEN: Again, this is for illustrative purposes only showing that if a debt -- if a payment of $20.9 million per year was made towards a debt of $253 million that it would be extinguished, principal and interest, over a thirty (30) year term.

MR. BOB PETERS: So, you're telling the Board this is a hypothetical illustration because this is not Manitoba Hydro's intention as to how to -- how to pay off that debt?

MR. VINCE WARDEN: It's a hypothetical calculation, yes.

MR. BOB PETERS: So, Manitoba Hydro doesn't need $20.9 million each and every year to pay off, over the next thirty (30) years, the $253.8 million of debt?

MR. VINCE WARDEN: If we are going to pay it off over that period of time, we would need $20.9 million. As I've indicated though, it's not out intention to pay it off over that thirty (30) year period.

We have an ongoing investment in Centra which is represented by the amount that we're carrying as an investment on Manitoba Hydro's accounts. And what we do require though is the financing costs associated with carrying that investment.

MR. BOB PETERS: There's two (2) aspects from that answer, Mr. Warden. The first is, you require the financing costs associated with that investment that you've now quantified at $19 million a year?

MR. VINCE WARDEN: Well, I think I quantified the financing costs at 17 million and the write -- the write off of that -- of the asset write-up -- the amortization of that write-up, that is, over that thirty (30) year period as the $2 million per year.

So, seventeen (17) plus the two (2) is the nineteen (19) that we're referring to. Yes.

MR. BOB PETERS: If I was to have you restate the schedule attached to PUB/54 -- PUB/CENTRA-54, the beginning balance should be what that you were trying to finance, Mr. Warden?

MR. VINCE WARDEN: Well, the beginning balance would not change. It is the two hundred and fifty-three, eight sixty-one (253-861).

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Warden, I think I

have your point. But let me try it just one (1) last time. On the schedule attached to PUB/CENTRA-54, you're asking the Board for the carrying costs shown on line 7, but you're not seeking to pay down any of the -- I'll call it the principal amount, of the acquisition and integration costs, through that $19 million figure?

MR. VINCE WARDEN: That's right.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Warden and Mr. Derksen, does it then become Centra's position that to keep the Utilities whole, $19 million needs to be found each and every year to do that?

MR. VINCE WARDEN: That is correct, yes.

MR. BOB PETERS: Now, Mr. Warden, just help me out with the $19 million figure. $2 million of that nineteen (19) comes from Tab 14, page 11 of Order 208/02, it comes up from the write up of liabilities to fair market value, which is a total of $17 million; is that correct?

MR. VINCE WARDEN: Well, it comes from -- the net of the write up of assets and liabilities, the seventy-three (73) minus the seventeen (17).

MR. BOB PETERS: So that $56 million

number is the source of the -- of the $2 million in your
amortization chart for the debt?

MR. VINCE WARDEN: That's right.

MR. BOB PETERS: Now, let's move from --
from that figure of $19 million -- oh and I can't move
from it, I guess I just -- at the end of thirty (30)
years, Mr. Warden, what you will have done is paid the
debt, but that debt would be continuing because the
assets would -- would be replenished at that point in
time?

MR. VINCE WARDEN: We would be paying the
carrying costs on the debt. We would still have an
investment -- I think I indicated earlier that -- that
the investment would be $242 million. Actually, it would
be the one twenty one (121) plus sixty-five (65), so it
would be $186 million at that point in time.

MR. BOB PETERS: And on that you would
carrying the debt forever?

MR. VINCE WARDEN: Yes, as long as there
was an investment in Centra.

(BRIEF PAUSE)

MR. BOB PETERS: And that means that on
your books, on -- on Manitoba Hydro's books, what would

be the total amount of your investment in the gas utility?

MR. VINCE WARDEN: At the end of that thirty (30) year period, Mr. Peters?

MR. BOB PETERS: Would it be $186 million at the end of the thirty (30) years?

MR. VINCE WARDEN: It would, it would yes.

MR. BOB PETERS: All right. Turning back to the $19 million number, that's the amount of money you're asking the Board be considered as appropriate to pay the debt on the acquisition and integration costs over -- year over year?

MR. VINCE WARDEN: Well, not to pay the debt, but to service the debt.

MR. BOB PETERS: You're paying the interest only and no principal, is that what your distinction is?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: So when one (1) pays the debt they're paying principal, when one (1) services the debt they're only paying interest?

MR. VINCE WARDEN: Well, that's the way I would interpret it, yes.

MR. BOB PETERS: No, appreciate that,

okay, my mistake; thank you for that.
To service the debt of $19 million, you want to look to both Centra and Manitoba Hydro to pay that $19 million, correct?
MR. VINCE WARDEN: Yes, the annual costs of servicing that debt, including the amortization that we referred to earlier, is being allocated to both electricity and gas ratepayers.
MR. BOB PETERS: One (1) of the arguments that one (1) of the Intervenors puts forward, is that you presently have, in rates, an allowed return of -- on equity of approximately $15 million, and you'd agree with that amount as being the -- the amount in present rates for the allowed return on equity?
MR. VINCE WARDEN: Yes, that would be based on what was there at the time of acquisition, the net income that would result therefrom would be about $15 million per year, that's right.
MR. BOB PETERS: And to assist the Board in -- in seeing that, if you could turn to Tab 17 of the Book of Documents, in PUB-54 on page 3 of 3, at the top there's the breakdown of how the $15.1 million was calculated in terms of the allowed return on equity, based on an '03/'04 test year.
MR. VINCE WARDEN: Yes.

MR. DARREN RAINKIE: Mr. Peters, I -- I would note that part of the -- that $15 million number is from the '03/'04 GRA. Part of that number, though, is from the growth and assets between the time Manitoba Hydro acquired Centra and when the '03/'04 rates were set; that number would be something lower if you went back to the time of the acquisition.

But it -- it may become important in the discussions we have later, I'm not sure, but just to make sure that's -- that's clear.

MR. BOB PETERS: But what you're trying to tell the Board, Mr. Rainkie, is that when -- when Manitoba Hydro acquired Centra's shares, the total allowed return on equity, on a normalized basis, wouldn't have been quite $15.1 million?

MR. DARREN RAINKIE: That's correct, in fact we didn't even have the equity return on the -- on the tax deferral at that point, that came later in '03/'04.

MR. BOB PETERS: And therefore it was around the $13 million mark?

MR. DARREN RAINKIE: Twelve (12) or $13 million I think is a -- is a good figure to use, Mr. Peters.

MR. BOB PETERS: Mr. -- Mr. Warden, you

understand the position of one (1) of the Intervenors to be that you are already recovering from your gas consumers approximately $15.1 million on a normalized basis, as -- as return on equity; correct?

MR. VINCE WARDEN: No, no, that isn't, but do I understand his position; yes, I understand his position. Is the position right; no.

MR. BOB PETERS: All right, you've said that in your direct, and you've said it again, and I -- I think the Board's clear, but you will acknowledge that there is, in present rates, an amount of approximately $15.1 million that is on account of allowed return on equity?

MR. VINCE WARDEN: Yes, but the -- the important point that's being missed is that that $15 million is not being taken out of the -- of Centra, it's being left there.

MR. BOB PETERS: All right, and -- and let's go to that step now. Centra's -- what you're telling the Board is gas consumers should continue to pay that $15.1 million, and leave it in the gas company?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And continue to pay that $15.1 million, whether the Company is regulated on a rate base rate of return methodology, or on a cost of service methodology?

MR. VINCE WARDEN: Yes. The -- the method of regulation should not make a difference in that respect.

MR. BOB PETERS: And you're telling the Board that the $15.1 million should not be used to help pay down the $19 million of annual obligation that Manitoba Hydro has on account of the amortization of -- sorry, on account of paying the interest on the -- the debt?

MR. VINCE WARDEN: No, I'm saying it should be used. And that's the purpose of the corporate allocations, to -- to allocate to Centra ratepayers their fair share of the acquisition costs and the residual, the amount left over goes into retained earnings of Centra.

MR. BOB PETERS: I don't want to misstate your position, Mr. Warden, but you're -- you're on one (1) hand telling the Board the $15.1 million on return on equity should stay in the gas utility; correct?

MR. VINCE WARDEN: To stay in the gas utility to pay their fair share of the corporate allocation with any difference flowing to retained earnings for the benefit of Centra ratepayers.

MR. BOB PETERS: And while the $15.1 million of return on equity is to stay in the gas utility, you want to set up a charge or a cost to Centra, that that would be a cost charged to them for the benefit of the parent company?

MR. VINCE WARDEN: Well, there's -- there's a corporate allocation, a below the line -- after net income is determined, there's an allocation to Centra to reflect their cost of the -- their fair share of the acquisition, with the balance going into retained earnings as I mentioned.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Warden, does -- does Centra see that $15.1 million on return on equity as something distinct and different from a synergy benefit to Centra?

(BRIEF PAUSE)

MR. VINCE WARDEN: Yes. It is different then a synergy benefit.

(BRIEF PAUSE)

MR. BOB PETERS: If Centra is to pay

fifteen (15) of the $19 million on account of the annual interest on the acquisition costs, Mr. Warden, does it flow then that the parent corporation would end up paying the remaining $4 million?

MR. VINCE WARDEN: Yes. And that was the case in fiscal year 2003/04. As you know, we have amended that allocation now in this application, you know, for -- for '04/'05 such that the -- the parent will be paying $3 million more, Centra will be paying $3 million less.

MR. BOB PETERS: What you're telling the Board is that for the $19 million, you're now saying that the transfer from Centra should only be $12 million, correct?

MR. VINCE WARDEN: The transfer to Centra is only $12 million.

MR. BOB PETERS: Well, the corporate allocation figure is to be $12 million?

MR. VINCE WARDEN: Correct. Corporate allocation to Centra is $12 million. The corporate allocation to electricity ratepayers is $7 million.

(BRIEF PAUSE)

MR. BOB PETERS: I may have misspoken,

but the corporate allocation, it's an allocation being charged from the parent to the subsidiary, correct?

MR. VINCE WARDEN: Yes, Mr. Peters. It might be clearer if we did refer to the segmented note that is in Manitoba Hydro's consolidated financial statements. I'm not certain whether that was filed as a part of these proceedings, Mr. Peters.

If it would be helpful, though, we could copy this one (1) page for clarification to show how that allocation flows between gas and electricity ratepayers.

MR. BOB PETERS: To try to pre-empt you from having to photocopy that, Mr. Warden, at Tab 19 of the Book of Documents, can you check and see if this is equivalent to what you're looking to bring to the Board's attention?

(BRIEF PAUSE)

MR. VINCE WARDEN: Well, not really. These are the financial statements of Centra Gas Manitoba. The -- the note that I was referring to is in the financial statements of -- the consolidated financial statements of Manitoba Hydro which shows more clearly, I believe, the allocation between the two (2) entities.

MR. BOB PETERS: Well, then I'll take you up on that and ask your counsel, by way of an undertaking, to provide to the Board a copy of the consolidated financial statements containing the information you're portraying, including the notes, and we'll review that at a subsequent time.

MR. VINCE WARDEN: Yes. Mr. Peters, I was proposing only to copy the one (1) page, that is the segmented information note which we can review later if you choose.

MR. BOB PETERS: That'll be satisfactory. Thank you.

MR. VINCE WARDEN: Thank you.

--- UNDERTAKING NO. 5: Centra to provide Board with consolidated financial statements of Manitoba Hydro.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Warden, that reduction in the corporate allocation from Manitoba Hydro to Centra, is because Manitoba Hydro has more synergies than was previously determined?

MR. VINCE WARDEN: Yes, as I indicated in my previous testimony, the synergies being realized on the electricity side of the business are higher than earlier forecast, and it's taking us a little bit longer to gain the synergies on the gas side of the business, so the allocation was modified accordingly.

MR. BOB PETERS: In the prior case before the Board there was reference in the Order 118/03 that a temporary synergy benefit transfer would be permitted to allow the Corporation, that is to allow Manitoba Hydro and Centra, to pay off what was then the $20 million of annual requirement, correct?

MR. DARREN RAINKIE: I think that's a fair representation, Mr. Peters.

MR. BOB PETERS: Well, back in Order 118/03, when the Board heard from you, you had told the Board that Hydro needed $20.9 million to -- to pay off the cost of acquisition integration; would that be correct?

MR. VINCE WARDEN: Again, Mr. Peters, that was the theoretical calculation, that is the amount, as we previously discussed, the principal and interest to -- to repay that debt over a thirty (30) year period.

MR. BOB PETERS: And it was theoretical, Mr. Warden, because that's not what practically happened, is that what you mean?

MR. VINCE WARDEN: That's right.

MR. BOB PETERS: What did practically

happen is this Board approved a $3 million temporary synergy transfer from Centra over to Manitoba Hydro, correct?

MR. VINCE WARDEN: Yes, that's right.

MR. BOB PETERS: And the rates of the Centra ratepayers were -- was adjusted to be $3 million higher than would otherwise be the case?

MR. VINCE WARDEN: Correct.

MR. BOB PETERS: And if Manitoba Hydro didn't need that $3 million, what has happened to it?

(BRIEF PAUSE)

MR. VINCE WARDEN: Well, it was only a transfer for purposes of rate determination. As you may recall, the rate increases that Manitoba Hydro, or Centra was allowed to implement effective April the 1st, 2003, was 0.4 percent, which included in that amount a $3 million transfer to -- to Manitoba Hydro.

MR. BOB PETERS: Isn't the $15 million, or the now $12 million corporate allocation just for rate purposes, as well?

MR. VINCE WARDEN: Yes. And at that time Manitoba Hydro was not making a corporate allocation. So if you go back at the financial statements of 2000 and

2001, there was no corporate allocation made between -- or to Centra ratepayers.

The purpose of the corporate allocation, in part, was to make it very clear as to how those costs were being split, between electricity and gas ratepayers, and I -- I hope it's done that.

MR. BOB PETERS: All right. So, the $3 million and the $15 million, were then for the same -- intended for the same purpose, in terms of rate setting?

(BRIEF PAUSE)

MR. VINCE WARDEN: Sorry, would you repeat that, please?

MR. BOB PETERS: Well, characterizing the $3 million that the Board allowed in Order 118/03, and the $15 or $12 million being sought now, both of those are on account of benefits to be reflected in the rate setting process?

(BRIEF PAUSE)

MR. VINCE WARDEN: I guess we can accept that statement, Mr. Peters. The $3 million was a -- an amount to be included in Centra's rates as a contribution towards the acquisition costs of Centra, as is the -- the 15 million, now twelve (12).

The purpose though, of showing the fifteen (15) and the twelve (12) directly on Centra's financial statements, is to make this cost allocation more clear than it was before. I think it was very unclear as to exactly how the $3 million -- we talked at the last Proceeding about that being $7 million -- $7 million at one (1) point, reduced to three (3) by this Board. I think it was very unclear as just to how that -- those monies would flow.

So, the explicit allocation -- corporate allocation that we now show on -- on Centra's financial statements, directly on those statements, is to make that very clear. That is the amount that -- that Centra ratepayers are contributing towards the acquisition of the gas company.

MR. BOB PETERS: Thank you, Mr. Warden. In Tab 18 of the Book of Documents in front of you is extracts from Order 118/03, and on the bottom of page 65, last paragraph, there's an indication that the Board expects that over the next two (2) to three (3) years, Hydro and Centra will realize further synergies as operations become more integrated, sufficient to offset all acquisition and integration costs incurred by Hydro, and eliminate the requirement for a synergy benefit transfer in the future.

You read that with me, sir?

MR. VINCE WARDEN: I did.

MR. BOB PETERS: And was the Board mistaken in that -- in that expectation, and that's -- synergies will never be realized, so that the costs of integration and acquisition will be offset by them?

MR. VINCE WARDEN: Well I think this is partly the reason why we now show the allocation directly on the financial statements of -- of Centra. I think it was very unclear to the Board and others at that time, as exactly -- as to exactly what the synergies would cover.

The costs that are being incurred in Centra, and in Manitoba Hydro, as a result of the acquisition are lower than they would otherwise be, absent the acquisition. So therefore, would they ever be sufficiently lower to pay the total costs of -- of the acquisition on their own; I don't think Manitoba Hydro ever indicated that would be the case.

We have stated that total synergies to date are $16 million, and I believe we have a filing that supports that -- that total of $16 million.

At the time of the acquisition I do recall that we committed to a minimum of $12 million in synergies, so we've exceeded the synergy estimate that we had back at the time of the acquisition. So the $16 million is close, close to the nineteen (19) that we just talked about, but it was never intended that those two (2) numbers would be the same.

MR. BOB PETERS: On page 66 of Order 118/03, also found at Tab 18 of the Book of Documents before you, Mr. Warden, there was another expectation, at the top of that page, by the Board, and there the Board expects that the need for a synergy benefit transfer will be eliminated by no later than March 31 of 2005, and if possible earlier.

What you're telling the Board is that -- that there won't be an elimination of a synergy benefit transfer, because that's what's needed, in essence, to pay off the majority of the $19 million?

MR. VINCE WARDEN: No, no, I'm not saying that at all. There is no synergy benefit transfer between the two (2) utilities today. They -- their costs are what they are, and inherent in those costs are realization of synergies.

There is, though, this cost of $19 million that has to be borne by someone, either electricity or gas ratepayers. And it is being allocated to those ratepayers in a way that reflects the -- to a certain extent, the amount of synergies that are being realized within those respective utilities.

So, the benefits of the acquisition exceed -- definitely exceed the cost. But those costs have to be allocated in -- in a fair manner and that's what the -- the fifteen (15) and four (4) of last year did, is allocate those costs of the acquisition between electricity and gas ratepayers.

But there -- and there is no synergy benefit transfer occurring between the two (2) utility today.

MR. BOB PETERS: Well --

MR. VINCE WARDEN: So, we have to distinguish between a synergy benefit transfer, and the costs -- the real costs of the acquisition. Somebody has to pay those, and obviously the -- the Utility that receives the benefit should be paying those -- those costs, that's fairly fundamental I think.

MR. BOB PETERS: Maybe I'm dicing the words here, Mr. Warden, but the Utility you want to pay $12 million of those costs of acquisition, is the gas utility; correct?

MR. VINCE WARDEN: That's correct.

MR. BOB PETERS: And the gas utility, you say, can pay that amount because it has received benefits

through synergies at least in an equal amount to that?
MR. VINCE WARDEN: Well, through synergies, and through rate relief that they otherwise would have experienced -- or the rate increases they otherwise would have experienced, under the previous ownership.
And I think our rebuttal evidence speaks to this, if you want to go to page 14 of the rebuttal evidence there is a schedule provided that shows what the estimate of -- of costs would have been -- revenue -- revenue requirement would have been, under the previous ownership.
So there's -- there's synergies being realized within the gas company. There's also lower rates that are being realized by ratepayers within the gas company.
Between the two (2), they're more than sufficient to pay the -- the transfer of $12 million in '04/'05.
MR. BOB PETERS: And just to conclude before the lunch hour here, Mr. Warden, some of that rate relief that you say exists for Centra's customers will now be taken back from them so that they can help pay for the cost of acquisitions by Hydro?
MR. VINCE WARDEN: Well, it's fair at

some point, that they should pay some -- some cost increase. We can't go on forever without Centra ratepayers having a -- some increase to their rates to cover our costs.

As we indicated earlier, since the date of acquisition the only other rate increase they've experienced were the distribution costs of the utility of 0.4 percent effective April the 1st of 2003.

MR. BOB PETERS: Do you agree with me, Mr. Warden, that's it's now effectively impossible to identify and track and measure the synergies that have been afforded to either utility as a result of the acquisition?

MR. VINCE WARDEN: I absolutely agree with that and, you know, I -- at some point I hope that we can look forward rather than looking back at the acquisition.

We keep, through these proceedings, referring back to the -- to the acquisition. We've been through at least two (2) hearings, two (2) proceedings doing that, and yes, I -- I think the further we move from the acquisition date of 1999, the more difficult it becomes to estimate what would have occurred under the previous ownership; absolutely, I agree with that.

MR. BOB PETERS: And what you estimate

occur -- would have occurred, had the previous ownership continued with its ownership, again, is only based on assumptions that you can make, and of course, it's -- it's, at best, hypothetical?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: Mr. Chairman, in light of the hour, perhaps this would be an appropriate time for the lunch recess?

THE CHAIRPERSON: We will come back together again at 1:30, thank you.

--- Upon recessing at 12:00 p.m.
--- Upon resuming at 1:30 p.m.

THE CHAIRPERSON: Mr. Peters, are we expecting Mr. Saxberg back?

MR. BOB PETERS: Certainly I do expect him, although I'm not aware as to where he might be at this moment. Perhaps -- perhaps as Mr. Saxberg is entering, we could have Ms. Murphy attend to the two (2) documents that she has handed out in terms of answers to undertakings.

THE CHAIRPERSON: Ms. Murphy...?

MS. MARLA MURPHY: Thank you. Just -- I wanted to file a response to Undertaking 5, which was taken by Mr. Sanderson on the 31st of May at transcript page 549. And by my record, I believe that would be Centra Exhibit number 11.

THE CHAIRPERSON: I believe that to be true.

--- EXHIBIT NO. CENTRA-11: Response to Undertaking given by Mr. Sanderson May 31st, page 549.

MS. MARLA MURPHY: And then following up on Mr. Warden's undertaking this morning, Undertaking 6, I don't have a transcript reference yet, but it is the copy of the portion of the hydro electric 53rd annual report that he referred to this morning. And I believe that should be Centra Exhibit number twelve (12).

THE CHAIRPERSON: Thank you.

--- EXHIBIT NO. CENTRA-12: Response to Undertaking No. 6

MS. MARLA MURPHY: Thank you.

THE CHAIRPERSON: Mr. Peters, we're back to you.

MR. BOB PETERS: Thank you, Mr. Chairman, Board Members. The lunch hour sometimes allows us to digest things, and Mr. Warden let's see how my digestion was of your evidence from this morning.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: The total cost to Manitoba Hydro to acquire Centra was $254 million, correct?

MR. VINCE WARDEN: Correct.

MR. BOB PETERS: And the acquisition was financed 100 percent by way of debt?

MR. VINCE WARDEN: It was.

MR. BOB PETERS: And the annual debt servicing of the interest only component is $17 million on that acquisition?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And there's also an annual amortization of the net assets, the write up, that is of the assets and the debt?

MR. VINCE WARDEN: Correct.

MR. BOB PETERS: And that amount was $2 million?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And that 17 million plus 2 million, brings us to $19 million being the total annual cost to Hydro?

MR. VINCE WARDEN: That's right.
MR. BOB PETERS: And one of the things you are before the Board, in this Hearing, is to have the Board adjudicate as to how those costs should be recovered, correct?
MR. VINCE WARDEN: Yes, we have a proposal before the Board as to the appropriate split of that between the electricity and gas ratepayers, yes.
MR. BOB PETERS: And the proposal that you have, in terms of the split between the gas and electric ratepayers, is the gas ratepayers would pay 12 million, and the electric ratepayers would pay -- would pay $7 million?
MR. VINCE WARDEN: Correct.
MR. BOB PETERS: And the $7 million paid for by the Hydro electric ratepayers, that is based on the amount of synergies that the Corporation estimates have been recovered as a result of the acquisition?
MR. VINCE WARDEN: That's right.
MR. BOB PETERS: And that leaves the $12 million as the amount that Centra is to contribute to the annual $19 million costs, and your evidence, as I understood it, is that $12 million represents their -- Centra's ratepayers' share of the benefits as a result of the transaction?

MR. VINCE WARDEN: The synergies and benefits, yes.

MR. BOB PETERS: All right. You've broken down benefits to include synergies and benefits. The synergies and benefits, whatever they total, 12 million of that is the amount that you want to allocate to the gas company as their share of the annual costs incurred by Manitoba Hydro of $19 million?

MR. VINCE WARDEN: That's correct. Yes.

MR. BOB PETERS: Now, that $12 million, you will agree with me, is comprised of either synergy benefits that have been achieved, or the benefits that Manitoba -- sorry, the benefits that Centra has achieved by West Coast no longer being the owner?

MR. VINCE WARDEN: I agree with that.

MR. BOB PETERS: And those are the two (2), and only two (2), sources of -- of benefits that you're seeking to utilize to help pay for this $19 million expense?

MR. VINCE WARDEN: Of monetary benefits, that's correct; yes.

MR. BOB PETERS: You suggested to the Board before lunch that one (1) of the sources of these monetary benefits was that West Coast was no longer the parent, and as a result of which, certain financial benefits have been -- have been achieved by the gas utility?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And in -- on page 14 of the rebuttal evidence, and that's not in my brief of documents but it was filed May 26th by the Corporation, fifty-three (53) pages worth, and on page 14 you provided a snapshot as to how it is possible to estimate some of the benefits that Centra achieves with West Coast no longer being the owner?

MR. VINCE WARDEN: That's right.

MR. BOB PETERS: And you'd agree with me that there are many assumptions on page 14 of your rebuttal evidence?

MR. VINCE WARDEN: There are.

MR. BOB PETERS: And what you had to do was to pretend Manitoba Hydro was stepping into West Coast's shoes, and you had to make those assumptions and carry them through the numerical exercise?

MR. VINCE WARDEN: As best we could. Yes.

MR. BOB PETERS: All right. And as best you could because you show an increase in operating and administrative expenses, and you don't know for a fact that that number would be the case, but you've made some assumptions to increase it year over year to get to that number?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And when I look at the year that you used to calculate the benefits, you picked the first test year of 2005/06; correct?

MR. VINCE WARDEN: Yes, I did.

MR. BOB PETERS: If we looked at one (1) year later, that is the second test year that's before the Board of 2006/07, the numbers would become different, would they not?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And they become different because on the net income line under the test year you have $1.779 million, and we know from Schedule 3.0.0 found at Tab 13 of the materials, that that number would increase to approximately $11.3 million for the next test year?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: So there's an $11 million approximate increase on that one (1) line item?

MR. VINCE WARDEN: Yes, there is.

MR. BOB PETERS: While we're looking at that, on the income tax line item --

MR. VINCE WARDEN: Excuse me, Mr. Peters, that assumes, of course, a 2 1/2 percent rate increase in that year.

MR. BOB PETERS: Understood. Understood. On the income tax line item you attempt to depict a $4 million savings as a result of West Coast no longer being the owner of Centra's shares, correct?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: You'd agree with me that that $4 million is not related to synergies?

MR. VINCE WARDEN: Well, it depends how you define synergies. It's -- it's a cost, though, that is no longer borne by Centra ratepayers specifically.

MR. BOB PETERS: And it's no longer borne by them because of the change in tax status and how this Board has dealt with the amount presently in rates on account of income tax?

MR. VINCE WARDEN: That's right, Mr. Peters, and actually for the -- as Manitoba Hydro has defined synergies, we -- we don't include that as a synergy; a benefit, but not a synergy.

MR. BOB PETERS: All right. If we -- if we take into account the -- the new test year, and do the math, and exclude the -- the gas costs, wouldn't it be the case that there would be approximately $142.6 million in the '06/'07 test year, and only $138 million in the absent acquisition line?

MR. VINCE WARDEN: Well, no, I think the absent acquisition line would also increase for just normal increases in costs, so the operating administrative line would -- would go up by the amount of -- I think we assumed inflation of 2 percent per year. So that would go up accordingly.

There could be some increases in the other line items. I believe we produced such a schedule, I just -- if you can give me a moment I'll check on that.

(BRIEF PAUSE)

MR. VINCE WARDEN: Mr. Peters, we -- we do have the -- a similar schedule for the next test year, we're just in the process of producing that -- printing it. And we can -- we can provide that if you require.

MR. BOB PETERS: Certainly, I'll -- I'll have a look at that. But would you agree with me at this point, Mr. Warden, then, that if we -- if we change that net -- net income from the $1.8 million, to a number that would be more -- more usual, that more usual number would be in the eleven (11) to twelve (12) to $13 million number; wouldn't that be correct?

MR. VINCE WARDEN: More usual based on

the previous ownership of Centra, yes, I agree, that is the -- the net income -- traditional net income amount.

MR. BOB PETERS: And it's also more usual to what you expect that you'd be seeking in the '06/'07 test year, correct?

MR. VINCE WARDEN: Well it's an amount that results from a 2 1/2 percent rate increase in that year. I -- I'm not sure I would say it's usual. I think it provides an addition to retained earnings, which moves us towards the long term debt equity ratio of 75:25, that we're striving to achieve. Usual depends on the circumstances though, so I wouldn't characterize it as usual.

MR. BOB PETERS: Well then would you agree with me that that eight (8) or $9 million difference that's shown, could just as easily be wiped out if the -- if the net income number was nine (9), ten (10), $11 million more?

MR. VINCE WARDEN: On the other hand we could look at the 2004/05 test year, in which that net income was a negative number, and there would be a larger difference.

So you could say that between '04/'05, that is what the ratepayers have experienced to date, and what the acquisition would show would be even greater than the 8.9 million shown here.

MR. BOB PETERS: That would assume, Mr. Warden, that the corporate allocation number was applied to that year as well; correct?

MR. VINCE WARDEN: Well, yes, the corporate allocation number has been applied to the test year, and as well as, '04/'05.

MR. BOB PETERS: In turning to Tab 13 of the Book of Documents, just to move to there for a moment, Mr. Warden. You'd agree with me that the essence of the application that is being made before the Board results in the return to the parent company being more in the neighbourhood of $45 million as opposed to $30 million, as it has been in the past, correct?

MR. VINCE WARDEN: You're going to have to help me with that one, Mr. Peters, no I don't -- I don't see that as being --

MR. BOB PETERS: All right. And I -- I don't disagree -- you don't see it on page or schedule 3.0.0, at Tab 13, but if we had another column in there for '03/'04 test year, as approved by this Board, there would be no amount shown for corporate allocations, would there?

(BRIEF PAUSE)

MR. VINCE WARDEN: Well, there are corporate allocations regardless of whether it's approved by this Board, or not. There -- there is, as reflected in the financial statements of Centra, there is a corporate allocation, that's a fact.

MR. BOB PETERS: Well, you've made the corporate allocation on -- on the financial records, but at this point, it hasn't been approved by the Board, you'd agree with that?

MR. VINCE WARDEN: Well, it hasn't been approved for rate setting purpose, that's all we're discussing here. For accounting purposes though, it has to be allocated, there's no option, it has to go there.

MR. BOB PETERS: Well, whether or not there's an option, Mr. Warden, that might be a matter for -- for the submissions, for rate setting purposes, the $15 million has not been approved for the '03/'04 fiscal year, for example.

MR. VINCE WARDEN: For rate setting purposes, I agree, it has not been approved for rate setting purposes.

MR. BOB PETERS: All right. Then you would agree that for rate setting purposes, what the Board would have seen in '03/'04 would have been a total return, which included the interest as well as return on equity, would have been in the range of the $30 to $32 million range.

MR. DARREN RAINKIE: Maybe I can help out here, Mr. Peters. I think it was about -- around $30 million return on rate base, although remember that return on rate base includes the provision for financing costs. So, while the regulatory way of referring to that says return, it's really just paying financing costs. It's really only the return on equity that's -- that's a return, per se, in that equation. So --

MR. VINCE WARDEN: I think Mr. Peters, once again though we're confusing things with the return on equity approach, and a cost of service approach. And it does get confusing when you attempt to apply a return on equity approach to -- to a utility that is -- that is being managed and its statements are being produced on a cost of service basis.

MR. BOB PETERS: That may be -- that may be correct, Mr. Warden, but in terms of the return to the Corporation, as Mr. Rainkie pointed out, there would have been a return, in the '03/'04 year, of approximately $30 million, which would have included the finance expense, as well as net income.

MR. VINCE WARDEN: Well, no I -- I don't agree there's a return to the Corporation, at all;

there's no return to the Corporation.

MR. BOB PETERS: The revenue requirement for those years then, Mr. Warden, would have been such that there was a $30 million revenue requirement for finance expense and return on equity.

MR. VINCE WARDEN: Only under the -- some assumption of rate base rate of return methodology, which does not apply, in my view, to -- to the new -- to the Centra as we know it today.

MR. BOB PETERS: All right. Well then -- then include in my question an assumption that rate base rate of return methodology does apply, would you agree that the year over year increase in the return that would be built into the revenue requirement would go up by approximately $15 million under you proposal before the Board?

(BRIEF PAUSE)

MR. VINCE WARDEN: Would you maybe just state that again, Mr. Peters? I -- I had -- having some difficulty agreeing with your assumption so if you can maybe restate that I'll -- I'll try and answer.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Warden, it maybe helpful on Tab 13 of our Book of Documents, Schedule 3.0.0, and I appreciate that I haven't got a column in there of the 2003/04, but I'm asking you to agree that in terms of revenue requirement that was requested of the Centra ratepayers, there would have been $20 million approximately for the finance expense and another ten (10) or $12 million on account of the net income line; would you agree with that?

MR. VINCE WARDEN: Yes. I can agree with that much.

MR. BOB PETERS: All right. And if we were now to continue to assume that rate base rate of return methodology was used and I go to the '05/'06 test year column 2, I see, again, approximately $20 million of revenue requirement being sought on account of finance expense or return on debt, correct?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And if I go down to line 21 there's an additional $11.8 million sought as a return on equity?

MR. VINCE WARDEN: In 2006/07, yes.

MR. BOB PETERS: No. You've jumped a year on me. I'm under the rate base rate of return column, Mr. Warden?

MR. VINCE WARDEN: Okay, we're back to the rate base. Okay. Yes. I'll agree with that.

MR. BOB PETERS: All right. And -- and my third point, still under rate base rate of return methodology is that when comparing the '03/'04 test year to the '04/'05 -- sorry, the '05/'06 test year, there's a $15 million increase now that is being sought under the line item of corporate allocation?

(BRIEF PAUSE)

MR. VINCE WARDEN: Well, again, Mr. Peters, we are mixing up rate base rate of return with cost of service. If we were to restate '03/'04 on a cost of -- on a rate of return basis, then all the line items that you see there would change.

So, the operating and admin. number, for examples, would have to go up to the -- similar to the number that we've shown on our rebuttal -- page 14 of our rebuttal evidence in which we show $62 million. That line item would have to increase if we were to restate this as you're trying to do.

You're trying to impose a rate of return methodology on a cost of service methodology and to do that on a -- on a -- to single out the corporate allocation line and attempt to do that is inappropriate.

You have to look at each line item. We can -- we can certainly produce the schedule for '03/'04. But each of the line items would look different than they do on Schedule 3.0.0.

MR. BOB PETERS: Sorry, I didn't want to suggest I was restating anything, Mr. Warden, and maybe you can tell me, under the 2005/06 column number 2, which line item didn't exist the last time you had a GRA before the Board?

MR. VINCE WARDEN: Well, on that point, the corporate allocation, we did not have a specific -- specific line item for the corporate allocation.

MR. BOB PETERS: And that corporate allocation amount of $15.1 million wasn't buried in the other line items was it?

(BRIEF PAUSE)

MR. VINCE WARDEN: You're asking me to recall how we submitted our rate application the last time around. There was this complication with synergy transfers; I believe the amount we asked for was $7 million, reduced to $3 million.

I'm not sure which line item we included that in; probably in the -- I think it was a separate line item, as a matter of fact. So, presented somewhat differently, but the intent of the previous application was still the same was to recover the costs incurred to run the gas utility.

So, to line these up side-by-side with our previous application could be done and should be done if we want -- if we're trying to compare the two (2) -- two (2) applications, because they were different in format.

MR. DARREN RAINKIE: I'd also note, Mr. Peters, you used the word that we were seeking the numbers under column 2. Of course we're not, we're seeking the numbers that are under column 1. So, we're not seeking a net income of 11.8 million in 2005/06, we're seeking a net income of 1.8 million.

So, while column 2 might be a comparator in terms of rate base rate of return, it is definitely not our application.

MR. BOB PETERS: And, Mr. Rainkie, if for any reason the Board concludes that the numbers have to be determined under a rate base rate of return methodology, you're still seeking then a net income of $1.8 million, regardless of the methodology?

MR. DARREN RAINKIE: That's correct, our

total non-gas revenue requirement is requested, is $129.5 million for that year.

MR. BOB PETERS: Mr. Rainkie, Mr. Warden, when you tell the Board that the $15.1 million shown here as corporate allocation, is to represent Centra's share of the benefits of the -- sorry, Centra's share of the costs of the acquisition, based on their share of the benefits and synergies.

Those benefits and synergies don't show themselves on any other line items, compared -- in the -- in Schedule 3.0.0, do they?

(BRIEF PAUSE)

MR. DARREN RAINKIE: Mr. Peters, can you restate that question, I'm not sure I understand where you're going on it.

MR. BOB PETERS: Perhaps this way, Mr. Rainkie. In 1999, the approximate return on equity that -- that was realized, would have been in the neighbourhood of $15.1 million, correct?

MR. DARREN RAINKIE: I think we went over that this morning, it's probably more in the neighbourhood of twelve (12) or 13 million. There's been some growth in plant since that time.

MR. BOB PETERS: All right. And if it was twelve (12) or $13 million back in '99, compared to the ROE calculations or the return on rate base calculations shown for 2006, of approximately $12 million, it's -- it's roughly the same number, correct?

MR. DARREN RAINKIE: Yeah, it's in the same magnitude, Mr. Peters.

MR. BOB PETERS: So, we can't say that there's been a benefit received as a result of a lower ROE being exacted from the Centra ratepayers, can we?

MR. DARREN RAINKIE: Mr. Peters, once again though, we're not asking for an approval of column 2, that's the comparator that we're providing for the Board's information under rate base rate of return we're asking for the non-gas costs that are embedded in line and column number 1, which include a $1.8 million net income for 2005/06.

MR. BOB PETERS: But you are, Mr. Rainkie, asking for column 3 on Schedule 3.0.0, for the next text year, '06/'07, correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And that includes a net income of about $11.3 million?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: Mr. Warden, on this

corporate allocation to the gas utility, Manitoba Hydro's synergy benefits that it's achieved, are in addition to that; would that be correct?

MR. VINCE WARDEN: That is correct, yes.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Warden, still on Schedule 3.0.0 at Tab 13, you've told the Board in -- in your direct evidence and you've essentially amended the amount of the corporate allocation that's being sought, downwards from $15.1 million down to 12 million; would that be correct?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And that's because the share by Centra of the cost of acquisitions and integration has been reduced from twelve (12) -- from fifteen (15) to $12 million?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And that $12 million would have been Centra's share right from the outset, that didn't just arise in a test year, but that would have arised (sic) in the previous years as well; would that be correct?

MR. VINCE WARDEN: No. I indicated that

the allocation is something that is reviewed each year in the preparation of the financial statements for the -- for the Corporation, the consolidated financial statements. And that in reviewing that allocation last year for '03/'04, the amount of $15 million to Centra Gas, $4 million to electricity ratepayers, was considered appropriate.

But, allocation was reviewed once again at the end of this fiscal year '04/'05 and it was determined that, as I indicated, we are achieving synergy benefits more quickly in the electricity side of the business than we are in the gas and it was deemed appropriate to adjust the allocation as -- as we've talked about.

MR. BOB PETERS: You'd agree with me that the cost didn't change in the year over year analysis?

MR. VINCE WARDEN: No, it's the synergies that -- the attainment of those synergies that change year over year.

MR. BOB PETERS: And the only change in the attainment of synergies that Manitoba Hydro has recently achieved at least $3 million more in synergies?

MR. VINCE WARDEN: That was the -- our analysis, yes.

MR. BOB PETERS: And therefore Centra's

share was reduced by that same amount?

MR. VINCE WARDEN: Correct.

MR. BOB PETERS: In the notes to financial statement that you wanted to draw to my attention, Mr. Warden, you've now filed Centra Exhibit 12 and that contains the note 19, to which you were referring in your evidence this morning?

MR. VINCE WARDEN: Yes Mr. Peters.

MR. BOB PETERS: And I note from what you've just handed out and marked as Exhibit Centra 12 that, and I'll read:

> These costs are allocated to gas and electricity segments in accordance with the synergy benefits derived by each of these segments as a result of the acquisition.

MR. VINCE WARDEN: Yes, Mr. Peters, I'm glad you drew attention to that because in reviewing that note, I think better wording would be, these costs were allocated to gas and electricity rate -- sorry gas and electricity segments in accordance with the synergies and benefits derived by each of these segments as a result of the acquisition. And I will, in fact, make that change for the 2004/05 financial statements.

MR. BOB PETERS: The wording that you

have on note 19 is essentially the same wording you have on note 13 of the Centra financial statements, isn't that correct, found at Tab 19?

MR. VINCE WARDEN: It is correct, yes.

MR. BOB PETERS: Well it's not correct in Tab 19 either, is it?

MR. VINCE WARDEN: I'm -- it's not incorrect, I'm just saying that better wording would be to clearly -- make it clear that there are synergies and there are benefits and it would be clearer to separate the two (2) or to at least identify the two (2) separately.

(BRIEF PAUSE)

THE CHAIRPERSON: Mr. Warden, just while Mr. Peters is pondering some point, going back into something you said earlier, and I just want you to correct me, if I mis-heard you before.

When you were talking about reducing the $15 million down to 12 million, I thought at one point in time, you said that partly the reason that you did that was because the synergy savings hadn't developed quite as quickly at Centra that you thought it would, but, it had developed at Hydro.

So the impression I got was that basically what you were doing was reducing the charge against Centra because of the overall, do no harm principle that you were following. Please correct me if I misheard you.

MR. VINCE WARDEN: No, Mr. Chairman, that I believe is what I -- accurately depicts what I did say.

THE CHAIRPERSON: Thank you.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Warden, did you also tell me before lunch that it's not possible to quantify and accurately calculate the synergies?

MR. VINCE WARDEN: Well, the synergies are an estimate because we have to make some assumptions about what would have occurred absent the acquisition. However, we have been fairly consistent in determining the total quantum of those synergies to be $16 million.

And when we do review -- every time we do review those synergies we do come up with that -- that number. So, we're -- we're reasonably confident that $16 million of synergies have been achieved.

MR. BOB PETERS: And you're telling the Board, how much of that resides in Manitoba Hydro and how much of that resides in Centra?

MR. VINCE WARDEN: Well, even there, the

-- we have to make some assumptions about the total quantum and then we have to make further assumptions about how that split is achieved between -- between electricity and gas.

But, based on our best estimate, the -- the split is approximately nine (9) -- nine (9) and seven (7).

MR. BOB PETERS: Nine (9) being in the gas utility?

MR. VINCE WARDEN: No, nine (9) being in the electric side of the business.

MR. BOB PETERS: And if there's 9 million on the electric side of the business, why is it that only 7 million of synergies are being utilized to help pay down the $19 million cost of acquisition?

MR. VINCE WARDEN: Well, it is based on the total benefits. It's not only synergies. It's synergies plus benefits.

So looking at the total synergies and benefits derived and adhering to the no harm principle as being paramount, we -- we allocate based on -- on our assumptions of both synergies and benefits in -- in both sectors.

So, there is a slight residual benefit remaining on the electricity side but there's a greater residual benefit residing on the gas side of the business.

MR. BOB PETERS: You don't use the ratio of how those synergies are achieved to do any calculations against the total costs, do you, Mr. Warden?

MR. VINCE WARDEN: Not strictly based on the synergies. But you look at the ratio of synergies plus benefits then -- then, yes, that is essentially how the allocation is -- is derived.

MR. BOB PETERS: All right. Just then on a high level, the synergies plus benefits on the gas side, you're telling the Board, represent 7 million in synergies and then an estimate of $9 million in benefits for a total of 16 million total to the gas side?

(BRIEF PAUSE)

MR. WILLIE DERKSEN: Yes, Mr. Peters, the other benefit that we've identified for the purposes of this calculation would be the base level of income that Centra had at the point of acquisition.

So, there is about $12 million of income. When Hydro acquired Centra part of the economic calculation is how much was the income that Centra's providing plus how much benefits-- how many synergy benefits can we get out of this? And between those two (2) amounts that made the transaction favourable from a financial perspective.

So what we've done here is we've taken for 2005/06 the Centra base income level, the $12 million, if you like, plus the Centra synergy benefit which is about $6 million -- six (6) or $7 million, and Hydro having a synergy benefit in the order of nine (9) or $10 million which gives us a total of twenty-eight (28); sixteen (16) synergies, twelve (12) base income.

And Hydro's portion of that twenty-eight (28), based upon it's $10 million, or nine (9) to $10 million of savings is about -- results in -- in about an apportionment, if you apply that ratio -- pardon me, if you applied that ratio to the $19 million it comes up with $7 million of the nineteen (19) should go to Hydro and twelve (12) of it should go to Centra.

MR. BOB PETERS: Just help me with though, what is the ratio, Mr. --

MR. WILLIE DERKSEN: Okay, the --

MR. BOB PETERS: -- Derksen?

MR. WILLIE DERKSEN: -- the ratio is 10:28, which is about 36 percent for Hydro and 64 percent would be to Centra then.

MR. BOB PETERS: To calculate that ratio, Mr. Derksen, you've included the base level of income as I understand your answer?

MR. WILLIE DERKSEN: That's right. That's what I've done, yes.

MR. BOB PETERS: And -- and the base level of income that you're using, that's attributable to the return on equity --

MR. WILLIE DERKSEN: At the point of --

MR. BOB PETERS: -- that Centra was earning?

MR. WILLIE DERKSEN: -- acquisition, yes, that it was earning at the time.

MR. BOB PETERS: So how is the base level of income -- the base level of income is the return on equity that Centra was earning at the time --

MR. WILLIE DERKSEN: That's right.

MR. BOB PETERS: And the return on equity was being paid for by Centra's ratepayers?

MR. WILLIE DERKSEN: That's right.

MR. BOB PETERS: And so how is it a benefit to them to have to continue to pay the return on equity?

MR. WILLIE DERKSEN: What I'm looking at is the benefit to the acquirer from an economic perspective. What Hydro -- Hydro paid -- let's say it would have bought the Company for a $120 million, and that it could afford to pay that if the only benefit it was getting was the income that Centra would generate.

(BRIEF PAUSE)

THE CHAIRPERSON: We sense a sort of an understanding operating on two (2) levels sort of simultaneously. We're just going to have a ten (10) minute break, and we're going to reflect a bit, and then when we come back we'll go all the way through to the close. And it will give us all a chance to think how we get through this little patch, thank you.

--- Upon recessing at 2:15 p.m.
--- Upon resuming at 2:33 p.m.

THE CHAIRPERSON: Mr. Peters...?

MR. BOB PETERS: Yes, Mr. Chairman. I want to just wrap up on this area, and move on, maybe to the delight of the witnesses, and maybe myself as well.

But having said that, I wanted to just come back and try to walk through the last couple of points, and to do that, Mr. Chairman and Board Members, you'll need a copy of Centra Exhibit 12, and also I would

ask you to turn to Tab 15 of the book of materials.
And Tab 15 of the Book of Documents, I should say, Tab 15 is the book that I have provided.

CONTINUED BY MR. BOB PETERS:
MR. BOB PETERS: At Tab 15 of the Book of Documents that I circulated, is a copy of CAC/MSOS/CENTRA-100(E), or 100, and it includes all components. And of course Centra Exhibit 12 is the extract from the Manitoba Hydro Electric Board 53rd Annual Report.
Mr. Warden, are you still with me?
MR. VINCE WARDEN: I think so.
MR. BOB PETERS: Or am I with you, I'm not sure which I should ask, but sir, I note a difference between Centra Exhibit 12 and what is found at Tab 15 in the Book of Documents, being CAC/MSOS/CENTRA-100.
And I find that difference on top of page 2 of 2, of the Book of Documents, where Centra is indicating that the sharing of the transaction costs is calculated in accordance with the Board Order, and it goes on to say the 15.1 million, which represents Centra's share of the cost, is equal to Centra's return on equity as calculated in the '03/'04 GRA, correct?
MR. VINCE WARDEN: Yes, I see that, Mr.

Peters.
MR. BOB PETERS: Would -- would you agree with me that -- that what was Centra's share of the ROE in the '03/'04 GRA is no longer relevant to the determination of how much Centra should pay of that total $19 million costs of acquisition and integration?
MR. VINCE WARDEN: Yes, I would agree with that, as well; I think there is a difference in -- in our evidence in that regard, and I think the discussion we just had before the break with respect to the allocation being based on synergies and benefits is -- is probably the -- well, in fact, is the way we are looking at this for purposes of preparing our financial statements.
MR. BOB PETERS: All right. And is -- is that how the Board should be looking at it, for the purposes of setting rates, as well?
MR. VINCE WARDEN: I would encourage that, yes.
MR. BOB PETERS: And Mr. Derksen, if I go back then to the note in the financial statements, either on Centra Exhibit 12, or to those included in Tab 19 of my Book of Documents, and the amendment that Mr. Warden will -- will make, the costs, that is the share of that $19 million annual cost, was to be allocated in

accordance with the synergies and benefits derived by each of the gas and electric segments, is that correct?

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

MR. BOB PETERS: And where we left off before the recess was the total synergies, as a result of Manitoba Hydro acquiring Centra shares was $16 million?

MR. WILLIE DERKSEN: Yes.

MR. BOB PETERS: And to the best, and recognizing it's not a precise science at this point, your suggestion is that 9 million of those synergies would fall on the Manitoba Hydro side of the ledger, and 7 million would fall on the Centra Gas side of the ledger?

MR. WILLIE DERKSEN: Yes that would be a -- a good approximation, yes.

MR. BOB PETERS: But you don't use that ratio in terms of who pays, how much of the sixteen (16) -- I'm sorry -- of who pays how much of the $19 million, do you?

MR. WILLIE DERKSEN: Well, Mr. Peters, obviously before the break Mr. Warden and I were on a little bit of a different pages with respect to the backing behind that allocation.

I had looked at it independently from a different perspective, and -- and I think -- well, I know that Mr. Warden has done the calculations and endorsed what the transfer should be, so we -- we'll have to defer to the calculations that he'll provide.

MR. BOB PETERS: All right. Then Mr. Warden?

MR. VINCE WARDEN: I should add though, nevertheless, looking at it from both approaches we did come up with the -- the same split of -- of synergies -- I'm sorry of the costs.

MR. BOB PETERS: All right. So no matter which methodology you used, you still came to a -- an agreement on how much of the $19 million is paid for by each of the two (2) utilities?

MR. VINCE WARDEN: Yes we did.

MR. BOB PETERS: And maybe then you can tell me, how you've calculated Centra's share to be $12 million, and the electric customer's share to be 7 million, Mr. Warden?

MR. VINCE WARDEN: Well, I think I indicated when we first talked about the reduction in the allocation to Centra, that there was some judgment involved. So, we looked, first at the no harm principle, we did look at the synergies that were being achieved within the electric side of the business, we -- we did calculate them to be slightly higher than the gas, based on the assumptions that we had.

And based on those assumptions we did determine that, in fact, electricity ratepayers could bear a larger proportion of the -- of the cost, the acquisition cost. Again, based on judgment, we came to agreement that an additional $3 million could be borne by electricity ratepayers and still keep them -- preserve the -- the no harm principle as far as electricity ratepayers were concerned.

So not all that scientific, but based on some judgment as to which electricity and gas ratepayers should bear the costs of -- of the -- of the acquisition.

MR. BOB PETERS: Maybe another high level question, Mr. Warden: If it comes down and push comes to shove or the crunch hits, and one (1) set of customers cannot, for whatever reason, be held harmless, however that's defined, if that can't be accommodated, which ratepayers would be -- should be harmed?

MR. VINCE WARDEN: Well, happily we don't have that situation. We're very confident in the total of the synergy number. As I've mentioned, we -- we consistently have come up with $16 million in total synergies.

We know that the rates are lower than they would otherwise be in Centra today than they -- than under the previous ownership. So there are synergies and benefits that far exceed the cost of -- of 19 million.

The difficulty we have is -- is how do we allocate those costs between electricity and gas ratepayers and really it's a -- it's a cost allocation issue that we, in our normal cost of service study that we have to contend with, is how costs are allocated to the different classes of customer.

So, this is a allocation between classes of customers at a very high level.

MR. BOB PETERS: Mr. Warden, I'm going to pin you down a little bit further; you didn't answer my question, maybe -- maybe -- maybe wisely so.

But if push came to shove, and one (1) of the customer bases would be harmed as a result of this acquisition, do you agree with me that it should be the Hydro ratepayers who should bear that harm because they entered into the transaction in the first place?

MR. VINCE WARDEN: I think, Mr. Peters, that is consistent with the previous order of this Board, that the risk and benefit should reside with the utility that initiated the transaction; that would be the electricity ratepayers.

So, in the event that there was a -- a net cost then -- then I do agree that electricity ratepayers should bear that cost, but fortunately we don't have to contend with that.

MR. BOB PETERS: Thank you for that answer, Mr. Warden. In the note 19 to Centra Exhibit number 12 as well as the other note to financial statement found at Tab 19 of the Book of Documents, I'd -- I had interpreted the explanation as to suggest that there was an allocation calculation, and what I'm hearing from your answer, sir, is that it wasn't so much an allocation, as it now is -- is a question of judgment; would that be correct?

MR. VINCE WARDEN: Yes. Judgment based on knowledge of where the synergies and benefits reside.

MR. BOB PETERS: So there's no particular specific allocation you can point the Board to that gave rise to that decision in the first instance, but rather it was based on the judgment that you've indicated has been exercised?

MR. VINCE WARDEN: There's no set formula that we can apply, and -- no, there is -- there is very much an element of judgment involved.

MR. BOB PETERS: Thank you, sir. And one last point, this $15.1 million synergy benefit, wherever it appears in the materials, Centra has now amended that, and says that that number could be reduced to 12 million;

would that be correct?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And that would apply to any and all answers to Information Requests, as well as financial statements, and IFF's; just a blanket take that down from 15.1, down to 12 million?

MR. VINCE WARDEN: As it pertains to the fiscal years 2004/05 forward, yes.

MR. BOB PETERS: Okay. And -- and you said as it pertains to '05 -- '04/'05 fiscal years going forward, you were referring to starting April 1st of 2005, correct?

MR. VINCE WARDEN: April 1st, 2004. Fiscal year '04/'05.

MR. BOB PETERS: All right. Yeah, you've got me again on that; to March 31st, 2005?

MR. VINCE WARDEN: Correct, yes.

MR. BOB PETERS: And that's the fiscal year -- that's the fiscal year in which the Corporation has received a rate increase commencing February 1st of '05?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And --

THE CHAIRPERSON: Just one (1) second, Mr. Peters or Mr. Warden, I think it might be just that the pace as you were working through it, but would you typify that twelve point one (12.1) as being a synergy savings; that's not correct, is it; it's just a definition thing. The twelve point one (12.1) is the corporate allocation, the amended corporate allocation?

MR. VINCE WARDEN: Yes, it is the corporate allocation --

THE CHAIRPERSON: It's not the synergy savings? That's what Mr. Peters said you said --

MR. VINCE WARDEN: I'm sorry, I -- I heard it as the -- as the --

THE CHAIRPERSON: It may be as I get older my --

MR. VINCE WARDEN: -- corporate allocation, but --

THE CHAIRPERSON: -- hearing goes, thanks.

MR. VINCE WARDEN: But it is definitely the corporate allocation, yes; the share of the corporate allocation.

MR. BOB PETERS: And Mr. Chairman, I'd indicate to you, I did not intend to refer to it as that, although I may have inappropriately, and in error. So I apologize to the witness, and you can look at that on the record and see if there's any corrections further needed.

THE CHAIRPERSON: If we have the tapes, Mr. Peters.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Warden, while the $15.1 million corporate allocation changes to a $12 million corporate allocation, there is no change in the revenue requirement being requested?

MR. VINCE WARDEN: That's correct.

MR. BOB PETERS: And the $15.1 million corporate allocation, which -- which now we'll try to remember to refer to as a $12 million corporate allocation, the first time that shows up on the financial statements would be for the fiscal year ending March 31st, '04?

MR. VINCE WARDEN: No, March 31st, '05.

MR. BOB PETERS: I can't seem to get that right, Mr. Warden; so -- just let me check.

THE CHAIRPERSON: Mr. Warden, I'm sure it's '04; I'm just looking at your own notes of the financial statement. It's hard with these fiscal and calendar years --

MR. VINCE WARDEN: Yeah.

THE CHAIRPERSON: -- and it's getting --

MR. VINCE WARDEN: Maybe I'm not hearing

correctly. I -- I thought -- well, Mr. Peters, could you ask the question again, I'm sorry. I thought you were referring to the first time the $12 million allocation appears on the financial statements of Hydro, and that is the fiscal year '04/'05.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: But you show --

MR. VINCE WARDEN: The 15 million would have appeared in '03/'04.

MR. BOB PETERS: All right, and -- and the previous years to that, Mr. Warden, there would have been nothing on the financial statements with --

MR. VINCE WARDEN: Well actually, I'm sorry, the '03/'04 and -- and '02/'03, both had $15 million in -- in the corporate allocation to Centra.

MR. BOB PETERS: Mr. Warden, without crunching any numbers, the February 1st rate increase that the Corporation was awarded in interim Order 13/05, was again premised on the Board supporting the corporate allocation amount, correct?

MR. VINCE WARDEN: Well, the corporate allocation amount was part of our filing that supported the request for an interim rate increase, yes.

MR. BOB PETERS: I'm looking back to Tab

2 of the Book of Documents that I prepared, in which a copy of Board Order 13/05 is provided, and on page 6 of that Order, there's a table prepared by the Board that shows a corporate allocation for the year ending March 31st of '05, in the amount of $15 million, correct?

MR. VINCE WARDEN: Correct.

(BRIEF PAUSE)

MR. BOB PETERS: And in the '04 actual column, if the net income before allocation is shown as $7 million in the 2004 fiscal year, correct?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And the point that was demonstrated in your Application was that applying a corporate allocation of approximately $15 million, results in a net loss for the year of $8 million?

MR. VINCE WARDEN: For the year --

MR. BOB PETERS: For the year ending 2004, that would be March 31.

MR. VINCE WARDEN: Yes, correct.

MR. BOB PETERS: And the purpose of the interim rate increase in Order 13/05, was going to ameliorate that net loss by approximately $3 million?

(BRIEF PAUSE)

MR. VINCE WARDEN: Yeah, I think we might have the years mixed up there again, Mr. Peters. It's really the '04/'05 fiscal year that was affected by the $3 million interim relief that was granted by this Board. The loss would have been $8 million, had it not been for that interim relief.

MR. BOB PETERS: You're correct, I have my years again transposed, and I apologize for that, Mr. Warden.

Looking again at the bottom of page 6, there's a two (2) line chart which shows what the net income or loss would have been without any rate increases, and you're showing an $8 million loss in the year ending March 31, 2005?

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

MR. BOB PETERS: And the rate increase allowed the Corporation to realize approximately $3 million of additional revenue, which would mean the net -- a net loss would be reduced by the $3 million, down to $5 million?

MR. VINCE WARDEN: Correct.

MR. BOB PETERS: And help me again, Mr. Warden, why is it that your -- your changing the allocation from fifteen (15) down to 12 million, doesn't apply to the year we've just exited?

MR. VINCE WARDEN: The year we've just exited being 2004/05?

MR. BOB PETERS: Yes, sir.

MR. VINCE WARDEN: It -- it does, we -- we will be reducing that corporate allocation down to $12 million for '04/'05.

MR. BOB PETERS: And that means that the net loss, with the rate increase that was granted, would be further reduced from a $5 million loss, down to a -- it's going to be a $2 million loss?

MR. VINCE WARDEN: Correct.

MR. BOB PETERS: Perhaps happily moving on to issues of capital structure, Panel Members --

THE CHAIRPERSON: Mr. Peters, just before you do. Mr. Warden, I don't think this one (1) tiny little point had been covered off.

A little bit earlier, not that long ago, you talked about in answering Mr. Peters' insistence in getting you to answer, were the final risks and rewards rested, and you said Hydro.

But you didn't just say risks, you also said rewards, and my question is this: if the situation changes and the synergies do develop in Centra that you were hoping to achieve, in short, will -- is the twelve point one (12.1) open for further re-evaluation in future years, one (1) way or another?

MR. VINCE WARDEN: Mr. Chairman, I -- I think I indicated that it would be good to fix that amount going forward. We know or at least our position is that we've already surpassed the point at which there is no harm.

So any additional synergies realized would be to the benefit of the respective ratepayers, be they electricity or gas. So Manitoba Hydro's proposal would be because it becomes even more judgment, as time goes on, is to fix that amount at $12 million gas, $7 million electric forever more.

THE CHAIRPERSON: Thank you, Mr. Warden, that was my understanding of the -- of what you were saying. You were basically saying at some point you'd -- you move on beyond the -- the amalgamation and fix some things?

MR. VINCE WARDEN: Yes.

THE CHAIRPERSON: Okay, Mr. Peters...?

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

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: I wanted to turn to the

issue of capital structure and, Mr. Rainkie, I thought that might have been one (1) of the areas you told Ms. Murphy earlier today that was under your bailiwick; have I remembered that correctly?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And under Westcoast ownership, the capital structure that was approved in Order 79/98, was a sixty decimal nine (60.9) debt and a thirty-nine decimal one (39.1) equity ratio; correct?

MR. DARREN RAINKIE: I don't have that in front of me, but I'll -- I'll take that subject to check, that sounds reasonable, Mr. Peters.

MR. BOB PETERS: Okay, I got that from page 66 of the Order, so if I'm wrong you'll tell me. And that was based, Mr. Rainkie, on the actual capital structure that existed within the utility?

MR. DARREN RAINKIE: Yes, a calculation based on -- that was a test year forecasted amount, so it was based on averaging basically the two (2) years during 1997 and 1998.

MR. BOB PETERS: When the shares of Centra were acquired by Manitoba Hydro, the capital structure was also approximately 61:39, Mr. Rainkie, would you agree?

MR. DARREN RAINKIE: Are you referring to the determination that was made for rate setting in the 2003/04 GRA, Mr. Peters, or some other calculation or a reference that you have?

MR. BOB PETERS: Let me ask it this way: Do you know if the -- if the capital structure had changed from when the Board last approved it, Mr. Rainkie, to when Centra's shares were acquired by Manitoba Hydro?

MR. WILLIE DERKSEN: Mr. Peters, could you repeat that question please? I'm sorry.

MR. BOB PETERS: Yes, Mr. Derksen, I was seeking confirmation that the debt equity levels of Centra at the time of acquisition by Manitoba Hydro would have been 61:39?

MR. WILLIE DERKSEN: It would have been something less than that because we had projected earnings for 1998 that would have contributed positively to the equity ratios which would have contributed to bringing up the equity percentage.

And what happened during 1998 was that there were some losses related to hedging activities, I believe, and so that would have deteriorated the debt equity ratio somewhat. I don't know. I can't give you a precise amount.

MR. BOB PETERS: And Mr. Derksen, do you

recall that at the 2003/'04 test year that was approved in Board Order 118/03 there was a return on rate base of 8.1 percent reflected on actual capital structure of 63:37?

MR. DARREN RAINKIE: The 2003/'04 approved I have the equity amount being about 39 percent and the debt being about 61 percent and I can confirm that the overall rate of return that was approved was 8.10 percent, Mr. Peters.

Once again, that was on forecast -- forecast capital structure as opposed to a notional amount.

MR. BOB PETERS: In the materials you have before the -- before the Board, I'm looking to Tab 38 of what I've put in my Book of Documents; you have Schedule -- Schedule 5.9.1 through to 5.9.3.

Mr. Rainkie, you have that?

MR. DARREN RAINKIE: I do.

MR. BOB PETERS: And that is where you put forward your calculation of the overall rate of return?

MR. DARREN RAINKIE: That's right. Based on the Board's methodology for rate setting purposes.

MR. BOB PETERS: All right. In your answer, is that a qualification, Mr. Rainkie, or an indication that this is done under a rate base rate of return methodology which is a methodology that you're hoping to get away from?

MR. DARREN RAINKIE: That's right. These calculations are part of our rate base rate of return calculations. They're not what is embedded in our proposed revenue requirement, but -- but trying to provide the comparator in terms of rate base rate of return and how this calculation's been done in the past.

As Mr. Warden alluded to in his direct evidence, the way that we're looking at the debt to equity ratio in terms of for management purposes is -- is quite a bit different than how this calculation has been performed historically.

MR. BOB PETERS: All right. Well, let's just explore that then, Mr. Rainkie. What you've shown here under Tab 38 in Schedules 5.9.2, for example, is a forecast capital structure with a 67:32 debt equity ratio?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And that's based on, again, a -- a forecast of actual capital structure?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: When you indicated that you're now calculating the capital structure differently than what had been done in past years, your new calculation brings a debt equity ratio of, was it 84:16 that Mr. Warden shared with us in his direct evidence?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And it's the 84:16 ratio that also underpins your rate request; would you agree with that?

MR. DARREN RAINKIE: Yes, I would. That's one of the factors that the senior management and Board of Directors looked at in -- in proposing the 2 1/2 -- the 2 1/2 percent rate increases.

MR. BOB PETERS: And when you say that, Mr. Rainkie, one (1) of the reasons Mr. Warden is -- you want to migrate from what you calculate as an 84:16 debt equity ratio, to a 75:25 debt equity ratio?

MR. DARREN RAINKIE: Correct.

MR. BOB PETERS: Can you tell the Board why you want to go to 75:25 debt equity ratio?

MR. VINCE WARDEN: Well the -- the 75:25 debt equity ratio mirrors the financial targets on the electricity side of the business. This makes it consistent for both electricity and gas ratepayers to achieve that level of debt to equity, which is considered prudent for a Crown corporation.

MR. BOB PETERS: Sorry, in -- in that

answer, Mr. Warden, you want to get to 75:25, because that's really what the parent Company debt equity ratio is?

MR. VINCE WARDEN: It's consistent with the financial targets of the parent Company, yes.

(BRIEF PAUSE)

MR. BOB PETERS: I'm not sure if I -- how to interpret your answer, Mr. Warden. It's consistent because it's the same numbers, but is it consistent because that's the strategy of the Corporation, is to move the two (2) utilities to the same debt equity ratio?

MR. VINCE WARDEN: Yes, the consolidated -- that is the consolidated results of the Corporation are -- are judged based on progress towards the attainment of our long term -- short and long term financial targets. So, we have rating agencies that look at Manitoba Hydro's consolidated results.

And it is appropriate, in our view, that all subsidiaries contribute an equal amount towards the attainment of those targets, and that they should be the same.

MR. BOB PETERS: Well, Mr. Warden, when Manitoba Hydro acquired Centra's shares and that the last

GRA, I think Mr. Derksen or Mr. Rainkie had told the Board that a 61:39 debt equity structure was approved, correct?

MR. VINCE WARDEN: Approved for purposes of -- I'm not -- I'm sorry, could you just elaborate?

MR. BOB PETERS: Approve for rate -- approve for rate setting purposes?

MR. VINCE WARDEN: Well, the 61:39 was only calculated to support a rate of return methodology, which as we said many times, we don't support. We would -- we -- we prefer the -- the cost of service approach.

But inasmuch as we were compelled to file, based on a rate of return methodology, we did -- it was necessary for us to emulate what that capital structure would be under the previous -- somewhere to the previous ownership.

As much as we didn't agree with it, we still filed on that basis to show the difference between rate base rate of return and cost of service.

MR. BOB PETERS: Wouldn't another financial target for Centra be the 60:40 debt equity ratio that was approximately used by the prior owner?

MR. VINCE WARDEN: But there's no reason for a Crown corporation to attain that level of equity. It's been determined that Manitoba Hydro's appropriate capital structure is 75:25.

We have rating agencies that agree that that is the appropriate structure. We -- we know that structure provides for all risks that the Corporation faces. So 75:25, in our view, is appropriate and it is consistent with the debt equity ratios of other Crown owned utilities in Canada.

MR. BOB PETERS: So, if you were to calculate the -- the debt to equity ratio under a rate base rate of return methodology, Mr. Derksen, you would do it as you did on Schedule 5.9.2 for the '06 test year?

MR. WILLIE DERKSEN: Yes, I think this -- this is the proper Application, a rate base rate of return; that as Mr. Warden mentioned that's not what we're asking for. So, you have to distinguish between the purpose of the calculation.

MR. BOB PETERS: And let's just take that one (1) step at a time, Mr. Rainkie. The calculation that Centra is urging on the Board is to not include in the calculation the approximate $120 million of share capital that -- that exists, correct?

MR. DARREN RAINKIE: That's correct. That share capital is backed by debt at Manitoba Hydro corporate, so it's not available for a rate stability fund is simply how I look at it.

MR. BOB PETERS: Well, what you're telling the Board is that under a cost of service methodology the decision on how to finance Manitoba Hydro's share capital will dilute the ratio?

MR. DARREN RAINKIE: Well, I think we're looking at the reality of the world. I mean, we can -- we can look in the -- in the text book and say, how do you apply rate base rate of return or we can look at the combined financial statements for Manitoba Hydro and say, is there money there for a rate -- for a rate stabilization fund or not?

And simply in the calculation there isn't. And that's how -- why we're taking the cost of service perspective, as you take a theoretical approach or you can look at the reality of the world and for a Crown owned utility there's no shareholder to go to to get extra money.

So, I think we have to begin to realize the reality of the world when we're setting rates in this proceeding.

MR. BOB PETERS: And the reality, Mr. Rainkie, is the decision made on how to finance that share capital was made by Manitoba Hydro?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And was that to the

benefit of the Centra gas shareholders?

MR. DARREN RAINKIE: Mr. Peters, I'm not sure what -- what you're asking.

MR. BOB PETERS: As I understood your rebuttal, and I had a note here, page 18, line 19, Manitoba Hydro includes the debt incurred to buy Centra in the calculation of the debt equity; is that right?

MR. DARREN RAINKIE: Well --

MR. BOB PETERS: Or did you simply remove the -- the share capital?

MR. DARREN RAINKIE: I think it's better to say that we've -- we've removed the share capital because it's backed by debt at the Manitoba Hydro corporate level.

MR. BOB PETERS: Does it amount to the same thing?

(BRIEF PAUSE)

MR. VINCE WARDEN: If we included the share capital, the 251 million, as debt, which it really is, the ratio would go from 84:16 to 88:12.

We've chosen not to do that. But that is a -- another way of looking at that share capital. It's really the underlying debt -- it's -- it's not share --

it's not equity. It is debt that financed that purchase.

And if the $251 million was considered as debt, the debt ratio would -- would increase.

MR. BOB PETERS: Thank you, Mr. Warden. I just wasn't clear whether in doing the calculation to get to 84:16 you added the debt into the calculation or did you remove the share capital from the equation?

MR. VINCE WARDEN: We simply removed the share capital from the calculation. So, it's the -- the calculation is long-term debt plus short-term debt over retained earnings -- sorry, debt plus retained earnings.

THE CHAIRPERSON: Mr. Warden, what you're saying then is, when you're looking at -- you're looking through Centra's actually corporate balance sheet to the overall economic impact on Hydro?

MR. VINCE WARDEN: We are. Yes.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: When you do that Mr. -- Mr. Warden, does that mean that you are, in essence, including the debt on Centra's books?

MR. VINCE WARDEN: No. We're just excluding the share capital from -- from Centra's books for purposes of the debt equity calculation and we are, as the Chairman indicated, we're looking past the balance sheet of Centra to look at how that share capital was financed.

And it was -- because it was 100 percent financed by debt we've simply removed that from the -- from the debt equity calculation.

We could have, as I indicated earlier, we could have considered that to be debt which would have the impact of increasing the debt equity ratio from eighty-four (84) to eighty-eight (88).

MR. BOB PETERS: All right. So, the answer to my question of whether its -- it amounts to the same when you -- whether you remove share capital or add that amount as additional debt, it -- it's not the same, it makes four (4) points difference in the -- on each side of the ratio?

MR. VINCE WARDEN: It does.

(BRIEF PAUSE)

MR. BOB PETERS: Would you agree with me, Mr. Warden, that by -- by calculating the debt equity ratio as you have, by excluding the share capital because it's financed with 100 percent by debt, that that drives the debt equity ratio away from the 72:25 target?

MR. VINCE WARDEN: Well, it -- it

definitely changes from -- including -- including the share capital in that calculation as -- as a component of equity would result in a 63:37 ratio which, as I indicated in my -- in my direct, that would be not the correct way of looking at it.

MR. BOB PETERS: I appreciate your answer to the Chairman's question about looking past Centra's financial statements, but why should Centra's capital structure for rate setting purposes be influenced by how the parent financed the acquisition?

(BRIEF PAUSE)

MR. VINCE WARDEN: Because as Mr. Rainkie indicated, it reflects reality; that those are -- that is the situation today.

MR. BOB PETERS: And I'll accept the reality of how you financed it and I think I asked you a hypothetical some -- not too long ago, that if Hydro brought in the piggy bank, I think were my words, and paid cash for this acquisition, that would then have a different impact on the capital structure under your calculation; would you agree?

MR. VINCE WARDEN: No. Because there's still a cost to that cash that would have to be borne by ratepayers and we -- we'd be at the same place as we are today.

MR. BOB PETERS: You'd assume you'd have to borrow that to have the cash on hand; is that what you're saying?

MR. VINCE WARDEN: Well, in as much as we do borrow to finance new -- new capital construction, if we displaced that with -- with cash for another purpose then we would just have to borrow that much more.

MR. BOB PETERS: So, you don't accept my premise that hypothetically you could have been sitting here in a cash position to make this acquisition and you didn't have to purchase -- or do it by 100 percent debt?

MR. VINCE WARDEN: No. Manitoba Hydro is never in a cash position.

MR. BOB PETERS: But, that's the reality of Manitoba Hydro, how it chooses to finance itself?

MR. VINCE WARDEN: Because it's the optimum way to -- to finance our operations.

MR. BOB PETERS: Can you -- can you go further on this, Mr. Rainkie or Mr. Warden, under West Coast ownership, was the determination of capital structure for Centra for rate setting purposes influenced by the debt on West Coast's books?

MR. DARREN RAINKIE: No, it wasn't

because Centra was a stand alone company that put out its own debt issues and all of its debt was included on its own financial statement.

But to the extent that we recognize things like the parental guarantee, we're already going past the corporate shell of Centra Gas Manitoba Inc. so why do we have to keep within the corporate shell for rate setting purposes where we can -- you know, it's convenient to recognize other benefits, well, why isn't it the same way when we go to look at rate setting?

Are we, you know -- are we constrained by the corporate walls of a legal shell?

MR. BOB PETERS: Good questions, Mr. Rainkie. And I'm sure some day they'll be answered, perhaps by the Board.

But, Mr. Rainkie, if you can wax philosophical on this then; if a third party looks at the financial integrity of Centra on a stand alone basis, would they consider the share capital to be debt or equity?

MR. VINCE WARDEN: If a rating agency picked up the financial statements of Centra, they would consider share capital; if they had no other knowledge, if they didn't know -- under -- understand the underlying transaction that -- that financed that share capital, if they simply looked at the stand alone financial statements as Mr. Matwichuk did, they would come to the same conclusion.

And I don't disagree with the arithmetic. It would come to 63:37 debt equity.

However, anybody that knows Centra, knows that it was acquired by a Crown corporation. The first -- first time, and I think what anybody that does come to that conclusion of the 63:37 ignores or chooses to ignore the unique circumstances of -- of the acquisition.

Never before, in the history that I'm aware of, of any acquisition in Canada, has there ever been a Crown owned utility acquire an investor owned company. So, we have to look at this -- at the unique circumstances and make some adjustment for that.

So, a knowledgeable person would not come to the conclusion that the share capital should be included in the debt equity calculation.

MR. BOB PETERS: In the calculation that you've presented to the Board, Mr. Warden, why didn't you come forward with an 88:12 debt equity ratio as calculated by -- including the debt, as opposed to excluding the share capital?

MR. VINCE WARDEN: Well, there are certainly some within the Company that advocate that we should do that. As a matter of fact that's probably the purest way of calculating that ratio. However, we didn't.

I think a debt equity ratio, to a certain extent, is how you define it. We do, for example, include capital non-refundable -- refundable capital contributions in our calculation, which rating agencies don't do, so that we quite often see differences between the published ratio that we have in our financial statements in our annual report, compared to what you might see in a rating report.

And you even see differences in the calculation between rating agencies. So, whenever you do have such a calculation, it is important that it is defined.

We've chosen for the purpose of this Application to exclude share capital from that -- from that formula. But it's perfectly legitimate too, should we -- you know the other -- the other calculation including share capital as -- as debt, is -- is also a legitimate calculation.

MR. BOB PETERS: But it's a matter of now judgment that the Corporation has used as to how it should be calculated today and this day forward?

MR. VINCE WARDEN: Yes, for consistency

purposes we will be using the definition as we've -- as we've outlined in this -- outlined in this Application.

MR. BOB PETERS: All right. Turning to the cost of capital, Mr. Rainkie, can you just briefly tell the Board how the cost of debt is determined?

MR. DARREN RAINKIE: There's two (2) portions to that; long term debt and short term debt.

On the long term debt front, we do for -- once again, for a rate base rate of return purposes we do a thirteen (13) month weighted average calculation of the embedded cost of all of the debt issues. And then on the terms of the short term debt forecast, we do a forecast of what we expect short term debt rates to be in the forward test years, including the Provincial guarantee fee.

The long term debt calculation includes the Provincial guarantee fee as well.

MR. BOB PETERS: You strive to represent the average cost of debt over a thirteen (13) month average on that basis?

MR. DARREN RAINKIE: That's right; under the rate base rate of return calculations.

MR. BOB PETERS: And you say that the debt guarantee fee, that's .95 percent is included in the calculation?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And Centra gets the flow through rate that the Province of Manitoba affords the parent company; is that correct?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And, Mr. Rainkie, under a rate base rate of return methodology, the -- the cost of equity is to compensate the investors for their ownership interest in the -- in the Utility?

MR. DARREN RAINKIE: That's right. It's to compensate the investors for their risk in the investment that they have with the Utility.

MR. BOB PETERS: Just before I get there, Mr. Rainkie, I see here in my notes that on Tab 37 of the Book of Documents I put in a couple of schedules, Schedule 5.8.2, and then for the next test year 5.8.3 And this just demonstrates the specific debt issues and the thirteen (13) month calculation on account of the debt; is that correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And although I don't see it off hand, you're telling the Board that the -- the debt guarantee fee is embedded in those amounts?

MR. DARREN RAINKIE: If you look at line 31, where we're actually looking at the financing costs, it says provincial guarantee fee, I'm looking at the schedule 5.8.2, on line 31 there's roughly $2.4 million included there, Mr. Peters. That -- that would be an example of where we've included that in the calculation.

MR. BOB PETERS: And is there any Provincial debt guarantee fee on the short term debt?

MR. DARREN RAINKIE: Yes, Mr. Peters, that rate of 4.35 percent that's quoted there beside the 7.45 percent, includes the Provincial guarantee fee.

MR. BOB PETERS: Turning, as I tried to before, Mr. Rainkie, to the cost of equity, at Tab 35 of the Book of Documents, we get to the formula that you had referenced in earlier answers to me today; is that correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And what we've done here in Tab 35 is simply take an extract from your Application as to how you would calculate, under a rate base rate of return, what the revised ROE would be for the '05/'06 test year?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: If I understand the calculation that you've done, Mr. Rainkie, based on the current formula, the return on equity would be reduced to 9.26 percent, from the previous 9.56 percent.

MR. DARREN RAINKIE: That's correct.
MR. BOB PETERS: And to what do you attribute this reduction in the ROE?
MR. DARREN RAINKIE: Basically a reduction in the forward looking long Canada Bond yield expectation.
MR. BOB PETERS: And the Board had established parameters in assessing the appropriateness of the formula, as to the long Canada yield range, is that -- is that right, Mr. Rainkie?
MR. DARREN RAINKIE: Yes, my recollection is that it would operate in a range of 6 percent to 10 percent. I know the bottom end of the range, but I might be forgetting the appropriate top end of the range; I'm sure you have it, Mr. Peters.
MR. BOB PETERS: Well that was 8 percent plus or minus two hundred (200) basis points?
MR. DARREN RAINKIE: So, 6 percent to 10 percent.
MR. BOB PETERS: So, you -- you know the bottom, Mr. Rainkie, because that's the one (1) that's hit home first, correct?
MR. DARREN RAINKIE: That's correct.
MR. BOB PETERS: And because it's hit the bottom, and because you told the Board we could spend a

couple of days and a quarter of a million dollars setting a new number, the Corporation hasn't come forward to revise the return on equity amount?

MR. DARREN RAINKIE: The practical person in me has wrestled with the theoretical person in me and has won the day.

MR. BOB PETERS: And the practical person says even though the parameters that were set by the Board as many as ten (10) years ago have now -- would -- would normally trigger a review, the Corporation has opted not to come in for a review on this matter?

MR. DARREN RAINKIE: yes, because we're only providing these -- these calculations for comparison purposes, we didn't see through going -- you know going through the expense to update them.

I -- I do take some comfort in the -- the fact that other regulatory boards have either recently adopted a formula methodology or reviewed theirs, and pretty much haven't changed the parameters. And most of those formulas were put in place around the same time that ours was; if not earlier.

MR. BOB PETERS: The current yield of the Long Canada Forecast that you provided is 5.54 percent; have I read that correctly, Mr. Rainkie?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And the range that the Board had talked about being plus or minus two hundred (200) basis points of 8 percent range, that was set, was it back in '94?

MR. DARREN RAINKIE: Yes, I think it was part of the 1995 test year, it was --

MR. BOB PETERS: And does the Corporation have any knowledge as to what -- what's happened to that Long Canada Forecast, since you've used -- it looks here like you've used November trading days, November of '04?

MR. DARREN RAINKIE: This -- this particular formula relies on the London consensus forecast, and I think the last version that I looked at, had come down twenty-five (25) basis points since this was prepared.

The problem is, is that you also have to look at the spread between the ten (10) and the thirty (30) year bond yields, and that can move around as well; so I'm not sure what the net between those two (2) components of the calculation would be at this point.

MR. BOB PETERS: So, you haven't updated this formula based on more current information?

MR. DARREN RAINKIE: No, the Board's determination was that we would do this calculation in November, and I guess, in my words, to eliminate game playing it would be done consistently, each time we wouldn't pick a month and look at that month and say well is it up or is it down?

In fact, we asked several years ago to go to October because we filed our Rate Application earlier in the year, and we wanted some certainty with respect to this -- this amount before we filed it so we didn't have to revise the calculations.

And the Board said that it would prefer to stay in November; I think, to eliminate, kind of, the judgment and the game playing. But the whole purpose of the formulate in the first place is to put an established formula in place that people can understand and work with, rather than going all over the place and looking at changes here and looking at changes there.

So, I think that -- that was my understanding of why the Board said, no, we're going to stay firm on the November time-frame.

MR. BOB PETERS: The Board was looking at a rate base rate of return request only, Mr. Rainkie, what is Centra's view on whether the formula, as you've calculated it and worked it through, provides a reasonable result?

MR. DARREN RAINKIE: In reference to the other rate of return formulas for -- for the other

Boards, BCUC, the OEB, the AUB, the NEB, I think it's providing a reasonable -- reasonable number.

What's concerning me a bit is that if -- if you want to take the theoretical approach of rate base rate of return that our capital -- our equity percentage, now, is down to thirty-three (33), and I -- I think that the fair rate of return would be more around 10 percent at a 33 percent equity ratio.

The -- the rule of thumb is that for every 1 percent decrease in the equity ratio, there should be about a ten (10) basis point increase in the rate of return.

But, you know, once again, we -- we were doing this calculation for comparative purposes so we didn't see the value in -- in undertaking that type of expert opinion in terms of what the -- what the new refresh number might look -- look like.

But I do take comfort in -- in the -- the numbers that I see coming out of the other formulas from the other jurisdictions.

MR. BOB PETERS: You told the Board, Mr. Rainkie, in PUB/CENTRA-21 found at Tab 36 of the book of documents, that the formula was based on a 60:40 capital structure way back when it was -- when it was arranged; correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And now Centra's capital structure is -- is something less than 60:40, and depending on how it's calculated it'll determine how much less it is; correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: Is it Centra's view that a higher ROE should be sought as its risks have increased, or have its risks decreased?

MR. DARREN RAINKIE: Well, since we set the 9.56 percent ROE in the 2003/04 GRA I don't -- I don't think there's been an appreciable change in our -- in our risk profile. So I think if we were okay with it then, we should be okay with it now.

The problem is is that when we came before the Board in 2003/04, and we applied the rate base rate of return methodology, we had our equity ratio of around 39 percent.

Now, if we -- if we do the regulatory calculation, as distinct from Mr. Warden's financial analysis calculation, we're coming down to 33 percent, and at 33 percent I think that 9.26 percent is -- theoretically is probably low.

But given that we're not here looking for a return on equity, once again, I don't see the -- the reason to incur the cost, and hurt the Board's head in terms of going through all of these theoretical gyrations in terms of calculating rate of return in capital structure.

MR. BOB PETERS: There would simply be a notional capital structure provided, Mr. Rainkie?

MR. DARREN RAINKIE: Well, interesting that you mention that because we've been looking for that in three (3) previous test years. And usually when the rate of return formulas are applied, at the same time, the Boards calculate the capital structure.

Like, usually a rate of return formula goes hand in hand with a notional capital structure amount because you can't look at one in isolation. The -- the fair rate of return is based on the operational and the financial risks of the Company.

The more debt you have and the move leverage you're using the greater the financial risks. So the greater the -- the return equity that would be expected from an investor. So that's why in other jurisdictions they've -- they've -- they've coupled the two (2) hand in hand and they specify a certain notional equity percentage to go along with the -- with the -- with the return formula.

And it gets us out of trying to look at

the financial statement and do an actual calculation of capital structure which can be difficult, depending on the circumstances.

As you mentioned before, some -- some corporations -- Centra, in the past, was a stand alone corporation that had its own debt.

Other Corporations are structured differently. There might be a -- a separate corporation that's the Utility, but some of the debt might be at the parent level. So, you -- you have so many different combinations and permutations in a -- in a world where utilities have taken over other utilities, that I think notional capital structure makes a lot of sense.

MR. BOB PETERS: And what's the appropriate notional capital structure then, in light of what Mr. Warden told the Board before, is it 60:40 or is it 75:25?

MR. DARREN RAINKIE: Well, this is -- this is where we get into the question of, do you want to apply a theoretical regulatory methodology that's designed for a private corporation, and if you're asking that question, at 9.26 percent I would say 40 percent equity structure; equity ratio.

If we want to use a cost of service methodology, and judgment in terms of moving towards financial targets, then Mr. Warden has indicated that 75:25 is the appropriate way to go.

But I can't see creating a third methodology here, you know, and saying, well let's take rate base rate of return, let's -- let's suggest it here and there and see how it works, because I'm not sure what the regulatory methodology is at that point. It's neither a cost of service, or rate base rate of return, and so -- you know, I really don't see the value in that exercise.

MR. BOB PETERS: From that answer, Mr. Rainkie, and given the ownership of the gas utility, is there a need for the risk premium inherent in these ROE, calculations even needed?

MR. DARREN RAINKIE: Well let me answer that question with a question, a rhetorical question. If -- if you're not going to calculate a rate of return based on the -- the principals that have been established, what are we doing; why would we go to calculated rate base, why would we go to calculate a rate of return? I don't think there is the -- a fair rate of return for a Crown corporation.

If you don't use the principals of risk, then how do you go about calculating it; what are you using? I mean, then you're just using judgment anyway, so why not move to the cost of service methodology and look at management's proposal as opposed to trying to get yet a third set of theoretical calculations involved.

MR. BOB PETERS: Well maybe back to -- I'm not sure if it was the hybrid, Mr. Rainkie, but on Tab 38 of the Book of Documents, there was a calculation made on return on rate base for the '05/'06 test year, found at -- I'm sorry 5.9.2.

And if I look at this on an overall basis in terms of return on rate base, Mr. Rainkie, the 11.8 million is the equity return, correct?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And the balance is on account of finance costs, or interest charges, however you calculate them?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And in a previous question when I had suggested that if you add up the return that's shown on -- on Schedule 5.9.2, on line 14 in the far right hand column number 4, you talked about $30 million total return, correct?

MR. DARREN RAINKIE: That's correct. I also indicated to you earlier today that on top of that, you would have to add a million dollars of interest on inventory and common assets, but I'm not sure that's important to where you're going.

MR. BOB PETERS: All right. You keep reminding me of that, and I appreciate that, Mr. Rainkie. Well, where I'm going then is that in -- over and above this rate base rate of return calculation, the request that's before the Board right now requests an additional amount in the -- in the magnitude of $12 million from the gas ratepayer; would you agree with that?

MR. DARREN RAINKIE: No, I think that's where we're getting a little off base, because we have to go back to Schedule 3.0.0, Mr. Peters. Column 1 is what we're asking for in terms of our total revenue requirement, and it includes a net income of, I think, around $1.8 million in '05/'06.

MR. BOB PETERS: Just to interrupt you, Mr. Rainkie, we're back to Tab 13 of the Book of Documents, okay.

MR. DARREN RAINKIE: I think I can remember the numbers, I'm not sure I have to even go there anymore. But we're not asking for, in that year, the corporate allocation plus a return on equity; we're asking for the corporate allocation, plus $2 million of net income.

And in the second test year we're asking for the corporate allocation plus about $12 million in net income, but that hasn't -- that $12 million in the second test year has not been derived by using the rate of return formula; that has been derived in terms of senior management and the Board of Director's judgment on putting some equity in the kitty for the future.

So, it's unfortunate there are so many numbers in this rate case that -- that are, kind of, roughly the same but -- but those are two (2) very different ways of coming up to a similar number.

But I don't look at it as a double rate of return because there are two (2) issues here. One, we have to figure out what the proper allocation of the acquisition and integration costs are, and that's what the corporate allocation takes care of.

Once we have that dealt with, then the next issue is, how much equity should we have in Centra Gas Manitoba, and how fast should we build that equity. And that's where you start getting into the judgment about how much net income you would want to build into rates in any particular test year.

So -- so hopefully that's clear. If -- If we can't get this clear, Mr. Peters, we're not going to go too far down the road.

MR. BOB PETERS: Well, I think we've -- we've come a long ways, Mr. Rainkie, from -- from where we may have been earlier today. But you will acknowledge that the -- that the Intervenor evidence from Mr. Matwichuk doesn't separate those two (2) issues and deal with the allocation of acquisition costs separate from how much equity is needed within the Corporation?

MR. DARREN RAINKIE: Yes, I think Mr. Matwichuk looks at it as one (1) issue, and I looked at it as two (2) different, distinct issues.

MR. BOB PETERS: And probably that's a good summary of -- of where we've come to, Mr. Rainkie.

I'd like to move with you to the depreciation and amortization matters, and without checking my notes, Mr. Derksen, is this -- is this one of your areas?

MR. WILLIE DERKSEN: Yes, it is.

MR. BOB PETERS: Can you remind the Board of what the depreciation expense represents?

MR. WILLIE DERKSEN: The depreciation expense represents the annual charge into income, if you like, of the cost of the assets that are acquired in order to service the customers of Centra Gas.

So, if, for example, we buy an asset or -- or construct an asset for a million dollars and it has a ten (10) year service life, we would charge 1/10th of that $1 million into expense each year -- to depreciation expense each year for the ten (10) year period.

MR. BOB PETERS: And while Mr. Rainkie and Mr. Warden and I were crossing swords earlier on the differences between rate base rate of return and cost of service methodology; is this happily an area where the method of regulation doesn't really matter to what the depreciation expense will be?

MR. WILLIE DERKSEN: I would agree with that, yes.

MR. BOB PETERS: All right. So it's the same under either methodology?

MR. WILLIE DERKSEN: Yes, it is. And I think that shows up in our comparative schedules as well.

MR. BOB PETERS: You were referencing Tab 13 where depreciation and amortization is shown on Schedule 3.0.0 being no different in either of the test years, under either of the methodologies looked at?

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

MR. BOB PETERS: And I see at Tab 27 of the book of documents, that I've put before you, a copy of Schedule 4.9.3 and 4.9.4 being the depreciation expense for the two (2) test years.

Would you agree with me, Mr. Derksen, that the -- between these two (2) years there's relatively no difference in the depreciation expense?

MR. WILLIE DERKSEN: Yes. That's correct. Now, one thing I should mention, this is the depreciation expense on the assets that Centra owns. There's also a further component of depreciation expense charged to Centra based upon the assets that are owned by Manitoba Hydro and shared between the two (2) utilities.

MR. BOB PETERS: Okay. Since you asked, if you turn to Tab 26 of the Book of Documents you'll see Schedules 4.8.3 and 4.8.4. What you're telling the Board is to be mindful of line item number 11 which is depreciation on common assets?

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

MR. BOB PETERS: And what you're telling the Board is that Manitoba Hydro will buy an asset and it will be used between the two (2) Utilities, and a share of the depreciation gets charged to each of the Utilities?

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

MR. BOB PETERS: And on a net basis -- I -- I think I saw a schematic somewhere, or maybe it was confusing at the time, but you were showing the Board that sometimes Centra also buys an asset that is shared with the parent company for which there has to be a reverse allocation done?

MR. WILLIE DERKSEN: Yes. That primarily

represents the assets that pre-existed in Centra prior to Hydro acquiring it. And some of those assets are used jointly in both operations so there is a charge from Centra to Manitoba Hydro for pooling, and that those pooled costs are then subsequently reallocated to each of the Utilities.

MR. BOB PETERS: And what you show on line 11 of Schedule 4.8.3 and 4.8.4, found at Tab 26, is a net number?

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

MR. BOB PETERS: A net number that Centra has to pay as a result of its share of the depreciation on assets purchased by the parent?

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

MR. BOB PETERS: When was the last depreciation study done, Mr. Derksen?

MR. WILLIE DERKSEN: We reviewed it at the last GRA in 2003/04, the new rates went into -- were -- were implemented in April of 2002.

MR. BOB PETERS: In light of those dates, you can remind the Board, Mr. Derksen, that you implemented new depreciation rates in advance of the depreciation study having been approved, and the new rates approved by this Board?

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

MR. BOB PETERS: And are your depreciation studies done by an external consultant?

MR. WILLIE DERKSEN: Yes, Centra has -- Centra has always used an external consultant, and a participative approach, but the recommendations are done by the external consultant.

MR. BOB PETERS: And that continues under Manitoba Hydro's ownership?

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

MR. BOB PETERS: Mr. Derksen, has there been any changes in the depreciation rates used in this application compared to those in the last time that it came before the Board, and those rates are found, I think at Tab 27 of the Book of Documents.

MR. WILLIE DERKSEN: No the rates are the same.

MR. BOB PETERS: Back to the issue of common assets, I see on Tab 28 of the Book of Documents, you have a schedule of the common assets acquired by each of the utilities, and then you go through a process of allocating the depreciation on those back to the utility that, I suppose, got the benefit from -- from the use of them?

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

MR. BOB PETERS: Are all common assets now purchased by Manitoba Hydro, or does Centra still acquire new common assets?

MR. WILLIE DERKSEN: All of them are now being purchased by Manitoba Hydro.

(BRIEF PAUSE)

MR. BOB PETERS: Assets purchased by Centra prior to the purchase of its shares by Manitoba Hydro remain on Centra's books?

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

MR. BOB PETERS: When it comes to depreciation itself, Mr. Derksen, are there different depreciation rates as between the two (2) Utilities for the same asset?

MR. WILLIE DERKSEN: With respect to common assets, I believe that we've harmonized all of the underlying links of services between the utilities, but there may be some differences in depreciation rates due to differences in net book value; is there an unrecovered gains or losses on each of the utilities?

MR. BOB PETERS: I'm sorry, could you -- could you repeat that?

MR. WILLIE DERKSEN: Yes, in utility accounting practice, it's typical that gains or losses be maintained in the accumulated depreciation account of the Utility, and those gains and losses are accumulated and dealt with in -- in calculating the subsequent depreciation rates.

So to the extent that Hydro and Centra had different accumulations of gains or losses, there may be different depreciation rates that flow from that, even though the underlying length of service of the assets is the same.

So, for example, we -- we choose a five (5) year period for computers under both Centra and for Hydro, but there may be some differences in the unamortized gains or losses resulting in a -- in a slightly different depreciation rate between the two (2) companies.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Derksen, in terms of amortization expense, I think at Tab 30 of the book of documents you'll find a continuity schedule, additions and retirements since 2003/04, and it's provided for each of the two (2) test years, that is Schedule 4.10.3 and

4.10.4; do you have that?

MR. WILLIE DERKSEN: Yes, sir. I have that.

MR. BOB PETERS: And in -- are there any expenses if they're deferred charges on this schedule that have come here by way of the parent Company?

Any that have been allocated over to the gas company from the parent Company?

MR. WILLIE DERKSEN: Well, on this schedule, the demand side management would be an allocation, if you like, from the parent Company since it's -- the demand side program is managed on an integrated basis.

As well, I suppose, all of the additions for general rate applications represents workforce costs from the integrated workforce and, as such, really are allocations from the parent Company as well.

Oh, I'm sorry, on general rate applications, they're just the external costs. I'm corrected on that. So, they are costs paid to third-parties. But demand side management would, in fact, include some internal cost allocations because it's done consistently between the way the electric treats demand side and the way Centra proposes to treat demand side management.

So, it is the only one that would have an allocation of costs from the parent company.

MR. BOB PETERS: Just to address the GRA costs first, those are -- those are costs paid out to third- parties is what you've said?

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

MR. BOB PETERS: No -- no internal costs?

MR. WILLIE DERKSEN: There are no internal costs here, that's right.

MR. BOB PETERS: Are the internal costs expensed in the period in which they're incurred?

MR. WILLIE DERKSEN: Yes, they are.

MR. BOB PETERS: And in terms of the DSM expenditures, I see that there's a $2.5 million addition down at line 48 on account of demand side management; that's an allocation that's been made as a result of Manitoba Hydro's overall demand side management program; is that correct?

MR. WILLIE DERKSEN: Yes, that's correct. That's the amount that, in -- in preparation of the IFF, was proposed to be spent on gas DSM.

MR. BOB PETERS: And because I'm not going to remember to ask the third Panel, Mr. -- Mr. Derksen, has this number changed as a result of the additional DSM filing the Company has made?

MR. WILLIE DERKSEN: The number in the Application hasn't changed, but I believe that the amount the Company proposes to spend will have changed.

MR. BOB PETERS: Okay. I'm confused by that answer.

The Company's going to spend more than $2.5 million in the first test year on account of demand side management; is that your understanding?

MR. WILLIE DERKSEN: That is the proposal that it has, yes, that more than $2.5 million will be spent. I believe that's what the materials that have been forwarded as part of this proceeding have indicated.

But we're not updating our Application is -- is my point.

MR. BOB PETERS: Okay. And what impact does your not updating your Application have?

MR. WILLIE DERKSEN: It means that the costs would be -- the actual -- to the extent that the costs were greater and more amounts were amortized during the test year periods, the income would be lower in Centra than what would be shown in the IFF and in this Application.

MR. BOB PETERS: You don't get to carry it forward to the next period, you would -- you would essentially have to pay for that out of -- out of the test year revenues?

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

MR. BOB PETERS: And is the amortization of the DSM expenditures based on a fifteen (15) year amortization?

MR. WILLIE DERKSEN: That's what the proposal is, yes.

MR. BOB PETERS: And even if I turn to Schedule 4.10.4, even if the demand side management expenses are higher than what's shown, the amortization amount will remain the same. So, one-fifteenth (1/15) of the difference that isn't captured in the -- in the amortization would be covered out of current revenues?

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

MR. BOB PETERS: Not to steal the thunder from the third Panel, Mr. Derksen, but why would you be amortizing demand side management over a fifteen (15) year period?

MR. WILLIE DERKSEN: The underlying lives of the acids that are thought to -- to be acquired as part of the demand side management program, I think they have an estimated life something in excess of fifteen (15) years, and so Centra has chosen fifteen (15) years as a conservative approach to amortization and a consistent approach with how electric DSM costs are being amortized.

MR. BOB PETERS: Derksen, Municipal Income Taxes and Other Taxes is a schedule found on Schedule 4.11.0 and I've included that schedule at Tab 31 of the Book of Documents. Can you confirm for the Board that the municipal taxes are those levied against Centra's plant and facilities?

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

MR. BOB PETERS: And are these actual taxes that Centra now has to pay, or are these payments in lieu of taxes.

MR. WILLIE DERKSEN: These are still taxes that Centra has to pay.

MR. BOB PETERS: Is Centra exempt from paying any -- any such taxes?

MR. WILLIE DERKSEN: Not that I'm aware of.

MR. BOB PETERS: Can you tell the Board what the capital tax represents?

MR. WILLIE DERKSEN: Yes, the capital tax is a levy that the province charges to corporations and it's based upon the capital that's employed in the Corporation.

MR. BOB PETERS: Would there be a

correlation here that if the working capital allowance increases, there would also be a corresponding increase in the Corporation capital tax?

MR. WILLIE DERKSEN: Yes, that would be correct. The working capital allowance is an average for the year, and the corporate capital tax is levied based upon the year end financial statements, so there are -- it wouldn't be a perfect correlation, but broadly speaking, yes.

MR. BOB PETERS: Does this amount shown in schedule 4.11.0 reflect the increased working capital allowance and the Corporation capital tax that would be exigible?

MR. WILLIE DERKSEN: The -- the increase in working capital allowance -- from which point are you -- are you referring to?

MR. BOB PETERS: Well, if we -- if we look through your last approved amount you're applying to increase the working capital allowance, and has that increase reflected -- been -- sorry, has that increase in working capital allowance caused a -- an increase in the Corporation capital tax?

MR. WILLIE DERKSEN: Yes it has, but again, as I said, not to the same extent one might consider. I think a large component of our working capital allowance is based upon gas in storage, and the gas in storage, I think at year end, doesn't go up as much as the average gas in storage does, the average being the amount that would be -- its impact on working capital.

MR. BOB PETERS: And looking at the income tax line, what you're showing the Board here is that there's a one (1) time tax liability, and you show it at the bottom third of the page, that is being retired over a period of thirty (30) years; is that correct?

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

MR. BOB PETERS: And so, on line 32 there's an amortization of $1.8 million a year in the principal amount of that one (1) time tax liability; is that correct?

MR. WILLIE DERKSEN: Yes.

MR. BOB PETERS: And the carrying costs on that -- on that average balance is -- is shown in line 33 and in the first test year it's approximately $3.4 million.

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

MR. BOB PETERS: Is there something perverse in paying principal of 1.8 million a year and interest of twice that?

MR. WILLIE DERKSEN: Well, when you first take out a mortgage, it's much more perverse than that, and this is typically like that, so this is what happens.

MR. BOB PETERS: So, there's no -- there's no opportunity for you to finance or pay that off in a -- in a way that would attract fewer carrying costs?

MR. WILLIE DERKSEN: Well, the only way to do that would be to lower the time that it -- the duration of the amortization. You know, if you have a five (5) year loan, the amount of interest relative to the total payments is much lower than if you have a thirty (30) year loan, and this represents a thirty (30) year loan.

MR. BOB PETERS: So, one (1) way or the other the amount would be the same at the end of the day in terms of what you'd have to pay for interest?

MR. WILLIE DERKSEN: I -- I think financially speaking, yes. If I paid -- if I paid it down quicker then I'd be out of pocket -- that would be the consumers would be out of pocket that amount of money earlier, and they would have to finance that through their own borrowings, or -- or cash that they otherwise would have.

So at the end of the day other than there being a -- a rate differential between the rate that we can borrow at, and the rates that they can borrow at, the interest costs would be the same, or the total cost would be the same.

MR. BOB PETERS: When this matter was last before the Board, Mr. Derksen, I guess the option was to -- to pay it down quicker, and increase the rates to do so, or to spread it out and not increase the rates; isn't that what it came down to?

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

MR. BOB PETERS: I think in a previous question, Mr. Derksen, you've confirmed that Centra doesn't raise it's own debt, does it?

MR. WILLIE DERKSEN: No. The debt is raised through the Province and Manitoba Hydro.

MR. BOB PETERS: And how is the credit rating established for Centra?

MR. VINCE WARDEN: It -- it isn't actually. There's -- there is no stand alone credit rating for Centra.

MR. BOB PETERS: If there's no stand alone credit rating for Centra, Mr. Warden, what you're telling the Board is it -- it gets the benefit of whatever Manitoba Hydro's credit rating is?

MR. VINCE WARDEN: In the provinces, yes.

MR. BOB PETERS: In Tab 36 of the Book of Documents that you have in front of you is an extract from PUB/CENTRA-21 and just help me out on this, there's an attachment to it and it's a report by DBRS, have you located that?

(BRIEF PAUSE)

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

MR. BOB PETERS: Mr. Warden, if there's no stand alone credit rating for the gas utility, can you explain to the Board why then you need a 75:25 debt equity ratio?

MR. VINCE WARDEN: Well the -- the 75:25 debt equity ratio really isn't to satisfy credit rating agencies, although it does do that. It is more to provide for the risks the utility faces, the risk faced by Centra are judged to be similar than -- than the risk faced by -- by Manitoba Hydro Electric.

And in the determination of the Board of Manitoba Hydro 75:25 was the appropriate ratio to strive for over time.

(BRIEF PAUSE)

MR. BOB PETERS: Has Centra attempted to

quantify those risks through analysis and report?
MR. VINCE WARDEN: Well we do have a -- a corporate risk management process and -- and report that is -- that is prepared on a regular basis and presented to the Board of Manitoba Hydro. That report does include the risks of Centra as well.
MR. BOB PETERS: Does it break out Centra's risks separately?
MR. VINCE WARDEN: Yes, it does.
MR. BOB PETERS: What would be the largest uninsured risk that the gas Utility has?
MR. VINCE WARDEN: The risk would be an infrastructure type risk, offhand I don't remember the -- the quantum of that, but the risk would be related to a loss of some critical component of the gas delivery system.
MR. BOB PETERS: Subject to my checking, that -- that report has not been filed in these proceedings has it?
MR. VINCE WARDEN: I believe it has, yes.
MR. BOB PETERS: Was it --
MR. VINCE WARDEN: I'm sorry, not in part of these proceedings, it would have been filed as part of the electricity proceedings.
MR. BOB PETERS: That's what I was

thinking out of the other hat. Could you, for the benefit of these proceedings then, Mr. Warden, through your counsel, undertake to provide the Board with -- with that document outlining the risks of the gas utility?

MR. VINCE WARDEN: Yes, we can file the same report that was filed with the -- as part of the electricity GRA. I believe there was some parts of that report removed for sensitivity purposes, security purposes, and we'll look at what was filed and file the same document, if that's acceptable?

MR. BOB PETERS: I -- I think that's acceptable at this point. I don't know that anything further will turn on it, Mr. Warden, but, that would be a good starting point in any event. Thank you.

--- UNDERTAKING NO. 7: Centra to provide Board the document outlining the risks of the gas utility.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Just to conclude in this area of finance expense, am I reading the DBRS report correctly when I come to the conclusion that the rating for the Province of Manitoba, including Hydro and Centra, is the better or same as what it was when West

Coast Energy owned the gas Utility?

(BRIEF PAUSE)

MR. DARREN RAINKIE: Yes, I -- I think when you look at the rating history that's on the top of the page you're referring to as you go through --

MR. BOB PETERS: Excuse me, but Mr. Rainkie, that would be page 3 of 8 that you're looking at?

MR. DARREN RAINKIE: That's what I was looking at yes, Mr. Peters.

MR. BOB PETERS: Thank you.

MR. DARREN RAINKIE: That it has continued on, but I think if you look under rating update, the first line is really the -- the clincher in that, it says, it's really just a flow through of the rating of the Province of Manitoba.

MR. BOB PETERS: So you're not reading much into it, Mr. Rainkie, that the balance sheet may not be as strong as it was when West Coast owned it, and yet the DBRS rating is -- is as strong or stronger than when West Coast owned it?

MR. DARREN RAINKIE: That -- that's correct. The small size of the centre utility in relation to the Province's rating; it -- it's simply just a flow through Mr. -- Mr. Peters. It's -- I don't think it's reflecting any changes on Centra's balance sheet, it's just recognizing the debt guarantee of the Province, more than anything.

MR. BOB PETERS: All right. With that question and answer, Mr. Chairman and Board Members, and recognizing the hour, I suggest that might be an appropriate time -- this might be an appropriate time to adjourn for the day.

And then tomorrow I will hopefully quickly conclude on cost of operations matters and then get into some of the capital and safety issues that I have questions on.

THE CHAIRPERSON: Thank you Mr. Peters. We will stand down now. Thank you.

(PANEL RETIRES)

--- Upon adjourning at 4:02 p.m.

Certified Correct,

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Carol Wilkinson, Ms.