MANITOBA PUBLIC UTILITIES BOARD

Re: MANITOBA HYDRO

GENERAL RATE APPLICATION

2012/13 AND 2013/14

Before Board Panel:

Regis Gosselin - Board Chairman

Raymond Lafond - Board Member

Larry Soldier - Board Member

HELD AT:

Public Utilities Board

400, 330 Portage Avenue

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--- Upon commencing at 9:02 a.m.

THE CHAIRPERSON: I believe that we're ready to commence today's proceedings. So good morning, everyone. I just want to take note of the fact that panel member Soldier has been here for at least a half an hour, patiently waiting for the rest of us to show up, as usual.

I believe that we have no administrative matters to address unless there -- I just noticed that we have a couple of new exhibits. So perhaps you would like to introduce them, Ms. Ramage.

(BRIEF PAUSE)

MR. PATTI RAMAGE: Yes, Manitoba Hydro has two (2) documents that it is filing just to assist the Board and parties to follow along with our final submission. One is a book of documents. It's just a compilation of documents we'll be referring to from the record. We -- that is Exhibit Manitoba Hydro 118.

--- EXHIBIT NO. MH-118: Book of documents

MR. PATTI RAMAGE: And the other is an outline of Manitoba Hydro's closing comments. And that is one nineteen (119).

--- EXHIBIT NO. MH-119: Outline of Manitoba Hydro's closing comments

THE CHAIRPERSON: I believe we're ready to proceed, so off to you --

MS. PATTI RAMAGE: Okay.

THE CHAIRPERSON: -- or back to you rather.

CLOSING SUBMISSIONS BY MANITOBA HYDRO:

MS. PATTI RAMAGE: Well, hunker down. Good morning, Mr. Chairman, Board member Lafond, Board member Soldier.

Manitoba Hydro filed its 2012/'13 and 2013/'14 General Rate Application on June 15th, 2012. Since that time, we've covered a lot of ground: to (2) rounds of Information Requests, totalling two thousand one hundred and forty-eight (2,148) questions; fifty-nine (59) pre-ask questions; a hundred and -- oh, I had a hundred and seventeen (117) -- a hundred and nineteen (119) Manitoba Hydro exhibits, including seventy-nine

(79) Undertakings; culminating in twenty-one (21) days of public hearings over the month of December and January.

We've definitely canvassed a very broad range of topics. Manitoba Hydro has made its best efforts to inform the Board of the considerations it took into account when developing these rate proposals, rate proposals that Manitoba Hydro submits balance the needs of ratepayers with the fiscal realities faced by the Corporation in fulfilling its mandate of providing Manitobans with safe, reliable, environmentally sustainable, and economic power.

Before commenting on the various issues that have been raised during the course of the hearing, I would first like to bring back into focus the essential components of Manitoba Hydro's General Rate Application. And I'll deal with the approvals sought in chronological order.

First, approval to maintain in base rates the 1 percent rate deferral that had originally formed part of the rates approved on an interim basis in Orders 30/'11 and 40/'11 and to include in 2012/'13 revenues the revenues already billed and collected on account of this 1 percent since April 1st, 2010. These reve -- revenues have been accumulating in a deferral account since the issuance of Order 5/'12, and $36 million to the end of '12/'13, and $14 million in 2013/'14.

Second is final approval of Orders 32/'12 and 34/'12, which orders approved, on an interim basis, a 2 percent increase effective April 1st, 2012. This represents $25 million in 2012/'13 and $26 million in 2013/'14.

Third, final approval of Order 116/'12 and 117/'12, which orders approved, on an interim basis a 2.5 percent increase effective Sep -- September 1st, 2012, for all domestic customer classes. This represents $20 million in 2012/'13 and $32 million in '13/'14.

Fourth, final approval of the requested 3.5 rate increase effective April 1st, 2013, which is projected to result in 48 -- $48 million in 2013/'14.

Fifth, Manitoba Hydro is seeking the PUB's endorsement of modifications to the terms and conditions of the SEP program and the curtailable rates program, as well as final approval of all the interim orders which have issued with respect to these programs, as identified in Manitoba Hydro's filing, together with any further interim orders that issue since the filing up to the date of the Board's final order in this GRA. Manitoba Hydro has provided a list of the curtailable rate program and SEP orders to date at the very back of its book of documents at Tab 16.

Finally, with respect to diesel, in Order 116/'12 the PUB approved a 6.5 percent interim rate increase on the full-cost portion of the real -- rate applicable to general service and government customers in the diesel zone. This increase is projected to provide two hundred thousand dollars ($200,000) in 2012/'13 and three hundred thousand dollars ($300,000) in 2013/'14. In total, there are eight (8) interim diesel orders identified in Manitoba Hydro's filing.

If MKO files the true copies of the settlement agreement prior to the issuance of the final order in this manner (sic), Manitoba Hydro requests these orders be approved as final. And here I'm referring to Order 17/'04, 46/'04, 159/'04, 176/'06, 1/'10, 134/'10, 1/'11, and 148/'11.

If, however, the true copies of the settlement agreement are not filed, Manitoba Hydro would request the Board's final approval of these interim orders be granted conditional upon the filing of the true copies of the settlement agreement.

In order to put the requested rate

approvals in context for the PUB, it's first useful to review the background of how we got to this point. A portion of the approvals requested in the current GRA stretch back to the previous GRA and the subsequent interim rate applications filed by Manitoba Hydro and the various interim orders that have been issued by the PUB since that time.

Manitoba Hydro filed a GRA with the PUB on December 1st of 2009 requesting a 2.9 percent increase effective April 1st, 2010, and a further 2.9 percent effective April 1st, 2011. Due to the length of the hearing process, the application for rate increases were dealt with by way of interim orders, with the PUB issuing Order 30/'10 on March 26, 2010, which improved an interim increase of 2.9 percent effective April 1st, 2010, and Order 40/'11 on March 30th, 2011, which approved a further in -- interim increase of 2 percent effective April 1st, 2011.

On January 17th, 2012, the PUB issued Order 5/'12, which approved, on a final basis, a 1.9 percent increase effective April 1st, 2010, and a 2 percent in -- rate increase effective April 1st, 2011. The impact of Order 5/'12 was essentially to reduce the April 1st, 2010, rate increase by 1 percent, which has been referred to in this application as the '1 percent rate rollback'.

In that order, the PUB also directed Manitoba Hydro to create a regulatory deferral account that would track the differences between the revenues pursuant to the interim rates and the rates finalized in Order 5/'12, together with accrued interest at Manitoba Hydro's short-term borrowing rate.

With respect to rate changes in light of this order, the Board stated -- and here I'm quoting page 28 of Order 5/'12:

> "Rather than requiring Manitoba Hydro to immediately reduce its rates, the Board orders that the rate differential between what was approved on an interim basis and what has now been finalized shall be quantified by Manitoba Hydro and remain as an interim rate, with its associated revenues being accumulated by customer class with accrued interest in the previously prescribed deferral account."

The PUB went on to explain that the reason for not immediately requiring rate decreases and refunds extend beyond the obvious administrative expense and inequities due to customer class changes. The PUB acknowledged that Manitoba Hydro would likely be seeking further rate increases effective April 1st, 2012, and it wanted to definitively understand Manitoba Hydro's intentions in that regard when considering its approach to what it termed a new interim rate and an accumulating deferral account.

On February 14th, 2012, Manitoba Hydro filed an application to review and vary Order 5/'12, which sought to have the directive in Order 5/'12 pertaining to the rate increase rollback of 1 percent rescinded and Manitoba Hydro's application for 2.9 percent effective April 1st, 2010, approved as final.

Manitoba Hydro alleged not only that the PUB had erred in its decision but also that new facts had arisen. Specifically, Manitoba Hydro's forecast of net income for the years 2011 and '12 and the subsequent two (2) test years -- that's the test years we're dealing with in this application -- that they had changed dramatically due to mild weather, below-normal precipitation, continuation of the economic downturn in US export markets, greater competition from alternative energy sources, as well as the impacts of Order 5/'12 itself.

The PUB issued Order 19/'12 on February

17th, 2012, which denied Manitoba Hydro's application and indicated that Man -- if Manitoba Hydro intended to seek a further general increase for the 2012/'13 fiscal year, that the disposition of revenues from the 1 percent rate rollback that was accumulating in the deferral account would be an issue for a determination at that time.

On March 30th, 2012, as contemplated in the previous orders of the Board, Manitoba Hydro filed an interim application with the PUB, seeking approval to include the $23 million accumulated in the deferral account to March 31st, 2012, in the 2011/'12 revenues to maintain the base rates approved by the PUB in Orders 30/'10 and 40/'11, as well as approval of an additional 3.5 percent rate increase effective April 1st, 2012.

As part of this application, Manitoba Hydro indicated that there was an urgent need for the rate increase, because the Corporation was experiencing much lower than forecast revenues, primarily due to the impact of continued low prices in the export markets, and warmer-than-normal winter weather impacting domestic revenues.

Despite the significant reduction in the financial outlook as projected in IFF11 and financial ratios that were lower than target levels, Manitoba Hydro proposed to maintain the rate increase requests at the 3.5 percent previously forecast for 2012/'13 and 2013/'14 to achieve the appropriate balance between customer sensitivity and financial integrity.

THE CHAIRPERSON: Could I interrupt you for a second, Ms. -- Ms. Ramage? I'm just wondering whether it would be better if we had a copy of your comments, because I think it would be easier for us to follow. I'm -- I'm writing notes as you go along, but I'm not move -- not moving quite fast enough. Is it -- is it already in the document, or...?

MS. PATTI RAMAGE: I think if you -- and perhaps I should have been going through the tabs as we went, but as we come up, you are going to -- I should have been telling you which slide to be on. But these slides will outline in notes each of the --

THE CHAIRPERSON: Okay. That would be --

MS. PATTI RAMAGE: -- each of the statements. And I have to admit, I didn't mark in my notes the first few slides, but I'm going to get there very quickly and -- and be able to have you turn the page with me.

MR. RAYMOND LAFOND: Yeah, however, I

think you were quoting some numbers. And, I mean, not having them in front of me, like, I'm not sure they're corresponding to IFF12 or the Exhibit 15 that was submitted by Mr. Warden.

MS. PATTI RAMAGE: I believe the numbers you'll see are -- they are consistent with, if you look to Tab 1 of Manitoba Hydro's book of documents, which is Ma -- Figure 3 from Manitoba Hydro's rebuttal evidence. And this is going to be a tab I will be referring to continuously throughout the process. And -- and that Figure 3 quotes some of the numbers. And if you're on tab -- page 5 -- or slide 5 of the outline, we should be able to follow the numbers.

In preparing the argument, we referenced, as I said, this Figure 3 from the rebuttal evidence. And I will put the caveat, and -- and I do want to note that this Figure 3 is identical to that in the rebuttal evidence with one (1) exception. And that is where we have put the interim rate increases of 2 percent April 1st, 2012, and 2.5 of September 1st, 2012. We -- in the rebuttal evidence they were referred to as a single number. For example, in 2013, it would say 45 million. We've broken it out so the Board has the benefit of the exact -- the -- the two

(2) numbers.

Throughout the hearing, we went through the evidence and there -- we looked at Mr. Warden's numbers, we looked at these numbers. Where -- if they aren't exactly the same, it's due to rounding errors. We had the people -- people back at the office check to see if -- because we were adding up to, for example, at one (1) point, I think it was 46 million instead of 45 million. And we had them check, and it was just rounding between the -- the -- depending on who did it.

So we looked to the rebuttal because this was a document that set everything out on one (1) page for the Board. So if that's of assistance, our hope was that we could use this Tab 1 and not have you having to flip around to different documents.

THE CHAIRPERSON: I think that would be very helpful. Thank you.

MS. PATTI RAMAGE: So Mr. Wiens advises me we're at Ta -- Tab 5 of the slides -- or slide 5 of the slides.

(BRIEF PAUSE)

MS. PATTI RAMAGE: I'm trying to remember which order I last described. I -- I think -- I'll -- I'll start with 32/'12, and that was the -- the

March 31st, and -- no, we've gone through that. I think we're up to -- okay, I'm going to start at 32/'12, and -- and hopefully we'll all follow this through.

And in Order 32/'12, and that was March 31st of 2012, the PUB denied Hydro's request to reinstate the 1 percent rollback and varied the rate increase proposal, approving an interim 2 percent increase effective April 1st, 2012, as opposed to the 3.5 percent sought by the Corporation. The PUB reasoned that the 2 percent interim rate increase would, quote:

> "Enhance the fiscal health of Manitoba Hydro while also balancing the impact on consumers."

End quote. And there I'm referring to page 7 of Order 32/'12.

The Board also stated that the final disposition of the deferral account and the 1 percent interim rate are matters best resolved through the upcoming GRA. And there I'm referring to page 3 of that Order.

On June 15th, 2012, Manitoba Hydro filed its 2012/'13 and 2013/'14 General Rate Application requesting reinstatement of the 1 percent rate rollback and inclusion of the revenues associated with the deferral account in the '12/'13 revenues; an interim rate increase of 2.5 effective April -- or September 1st, 2012, and the further 3.5 percent effective April 1st, 2013; along with the various other rate approvals I outlined earlier and won't repeat now. The June 15th application was based on the financial forecast in IFF11-2.

On July 20th, Manitoba Hydro files its submission with respect to the proposed interim rate increase of 2.5 percent effective September 1st, 2012, and additional material that was requested by the PUB to consider the application.

And Mr. Wiens has pointed out we're now at slide 6. As part of this submission, Manitoba Hydro indicated that it required the proposed interim rate increase and rate rollback reinstatement to maintain net income and the financial ratios in 2012/'13 at acceptable levels and to preserve the financial integrity of the Corporation.

Manitoba Hydro also indicated that the implementation of the 2.5 percent interim rate increase effective September 1st, 2012, would, together with the 2 percent interim rate increase approved by the PUB effective April 1st, 2012, produce a similar level of additional revenue in '12/'13 as would have been produced by a 3.5 percent increase, had it been approved as originally requested effective April 1st, 2012.

Manitoba Hydro continued to be of the view that this was the appropriate level of rate increases required in '12/'13, considering all relevant factors. Manitoba Hydro also replied a re -- provided a reply to the submissions of Intervenors on August 14th.

In Order 116/'12, dated August 29th of 2012, the PUB approved Manitoba Hydro's request for the interim 2.5 percent effective September 1st, 2012, and a 6.5 percent interim rate increase on the full-cost portion of the rate applicable to general service and government customers in the four (4) diesel communities.

In this order, the PUB found that it was necessary to gra -- grant the interim rate increases to protect and preserve the short-term financial status and stability of the Utility based on currently available information and financial projections and that all parties would have the further opportunity to test the submitted information as part of the GRA process.

Now, in accordance with Manitoba Hydro's normal annual planning cycle, IFF12 was approved by the Manitoba Hydro Elecri -- Electric board in late November of 2012 and was filed with the PUB and Intervenors as Exhibit 9 in this proceeding. IFF12 provided all parties to the GRA with the most current financial outlook of Manitoba Hydro so that the PUB has the most current financial projections in which to base its decisions.

So with that and -- I admit, fairly lengthy background in mind, I'd like to move to discuss the reasons for the rate increase. And here we're at slide 8. And I think this will become much easier to follow along now.

While there have been a number of interim rate application and orders leading up to the 2012/'13 and '13/'14 GRA proceeding, and while there have been various forecasts provided to the PUB over this period of time as conditions and projections have changed and the various planning cycles of Manitoba Hydro have been completed, I would submit to the PUB that the reasons for the rate increases that Manitoba Hydro has sought over the time frame have remained consistent.

Simply stated, the rate increase

requests have been designed to ensure that the financial health of the Utility is maintained and to ensure that ratepayers will continue to enjoy rate stability and predictability over the long term. And while there have been twenty-one (21) days of public hearings to review GRA material in detail and allow interested parties to test the need for rate increases, in Manitoba Hydro's view, there has been no credible information provided to the PUB to refute the requirements for the rate increases proposed by Manitoba Hydro.

As well, the forecasts and considerations that resulted in the PUB finding that it was in the public interest to grant the 2.5 percent increase for September 1st, 2012, have not changed significantly in IFF12 and continue to be valid. These same reasons were equally valid with respect to the rate increases being sought in this application.

In Tab 2 of the application, the response to PUB/Manitoba Hydro First Round 61A, and pages 11 to 14 of Manitoba Hydro's rebuttal evidence.

In the -- in those documents, the Corporation outlined five (5) primary justifications for the proposed increases. These can be summarized, and they are included in Tab -- in slide 9 of Manitoba

Hydro's outline.

First, to avoid incurring losses on operations.

Second, to limit the extent to which financial ratios are projected to deteriorate, and to maintain the financial and credit rating integrity of Manitoba Hydro.

Third, to compensate for reduced prices for non-firm electricity sales in the -- in the export market.

Fourth, to recognize that Manitoba Hydro's infrastructure is aging, and that increased costs are necessary to maintain that infrastructure in a safe and reliable manner.

And fifth, to provide customers with rate stability and predictability and to avoid the need for much higher rate increases.

I'll now go through each of these justifications in order to outline why they are important considerations for the PUB in determining the public interest and providing final approval to the rate requests of Manitoba Hydro. I'll also briefly address how Manitoba Hydro has constrained growth in operating, maintenance, and administrative costs to ensure that rate increases are kept to a minimum necessary to ensure the safe, reliable, and economic surf -- service to ratepayers.

If you could turn to slide 10, first I'm going to deal with the justification related to avoiding incurring losses on operations. And if you could also turn to Tab 1 of the book of documents, it might be -- assist in following along.

At Tab 1, Manitoba Hydro has provided a table that summarizes the actual electric operations net income for the past five (5) years and the projected net income for the 2012/'13 and 2013/'14 test years from IFF12, as well as the impacts of the reinstatement of the 1 percent rate rollback, the interim rate increases that have been implemented in '12/'13, and the proposed rate increase in '13/'14.

This table, as I've indicated, is consistent with Figure 3 that was provided at page 12 of Manitoba Hydro's rebuttal evidence, with the exception, as I indicated, that we have broken up the -- the April 1st, 2012, and September 1st, 2012, interim rate increases.

At the commencement of the hearing, Mr. Warden had indicated at pages 441 to 443 of the transcript that the contractual arrangement with NCN with respect to Wuskwatim Power Limited Partnership, or

WL -- PLP, was under review and that, based on the current status of the negotiations, it was likely that the contractual arrangements would change such that there would be no attribution of projected loss from WPLP to NCN in 2012/'13 or 2013/'14. By letter dated February 22nd, 20 -- of this year, Manitoba Hydro advised the PUB and Intervenors that negotiations are still ongoing with NCN, and it now appears unlikely that the agreement will be reached this year.

On this basis, the financial projections in IFF12 continue to represent the best information with respect to Manitoba Hydro's financial outlook. And at this time Manitoba Hydro intends to reflect the non-controlling interest amount in net income in the test years.

If the parties are successful in renegotiating the contractual arrangement prior to the issuance of the PUB's order, Manitoba Hydro will advise the PUB forthwith, and reflect any revised arrangement in future IFFs. IFF12 is the best information at this time.

Now, as noted in Tab 1 of the book of documents, the cumulative impact of the 1 percent rate rollback reinstatement is $36 million to the end of 2012/'13, and the impacts of the interim increases total $45 million. That's $25 million related to the April 1st, 2012, increase and $20 million related to the September 1st interim rate increase. So there's a total net impact of $81 million in '12/'13.

In that same tab, you'll see the impact of increases total $58 million. That would be $26 million related to the April 1st, 2012, interim rate increase and $32 million for the September 1st, 2012, interim rate increase. And the impact of the proposed 3.5 percent rate increase is -- effective April 1st is $48 million, for a total impact of $120 million in the 2013/'14 test year. Together, these impacts of the rate increases total approximately $200 million for the two (2) test years. These impacts were outlined by Mr. Warden at transcript page 443.

Based on the update of water flow conditions and the various other assumptions that form part of IFF12, and assuming that both the 1 percent rate rollback is reinstated in '12/'13 and the interim and proposed rate increases are -- are approved, Manitoba Hydro is projecting net income from the electric operations of 53 million in 2012/'13 and 60 million in '13/'14. You'll also note, from Tab 1 of the book of documents, that these projected net income levels are considerably lower than the actual net income of 62 million that was achieved in '11 and '12 and the average net income level of the previous four (4) years of approximately $223 million.

Manitoba Hydro has recently published its financial results and quarterly report for the period ending December 31st, 2012. This report shows a consolidated loss of $38 million for the first nine (9) months of the 2012/'13 fiscal year. And I should have you turn the page to slide 11 at this point.

That $38 million loss compares to consolidated net income in the first nine (9) months of $29 million for the previous fisc -- fiscal year. The consolidated net loss of $38 million was comprised of a $24 million loss in the electricity sector and a $14 million loss in the natural gas sector. The net income in the electricity sector for the same nine (9) month period in the previous fiscal year was $48 million.

The $24 million loss in the electricity sector includes the impacts of the two (2) interim rate increases in '12/'13 and an $8 million non-controlling interest attributed to NCN with respect to the WPLP losses, but excludes any consideration of reinstatement of the 1 percent rate rollback which continues to be accumulated in the associated deferral account. The amount accumulated in the deferral account as of

December 31st, 2012, is $32.1 million.

On February 25th, 2013, Mr. Rainkie provided the PUB with the most up-to-date information available regarding Manitoba Hydro's financial outlook for the remainder of the '12/'13 fiscal year. And this can be found at transcript page 5,697. And I'm quoting here:

"We also took a quick look, a high-level look, at our expected results for '12/'13. And with some of the colder weather that we've experienced in the last month, it looks like we -- we may come close to our projected net income. I think it was 53 million, if I was not mistaken, for '12/'13."

Mr. Rainkie went on to caution that while you can rely on IFF12 as a reasonable forecast of Manitoba Hydro's net income for electric operations, it might be slightly lower once we review all our provision and accruals at year end. And that caution is found at transcript page 5,698.

I can't emphasize enough that the $53 million in projected income for 2012/'13 assumes approval of the 1 percent rate rollback and approval of the April 1st, 2012, and September 1st, 2012, interim rate increases. Without those rate increases that have been approved on the interim basis, the reinstatement of -- and the reinstatement of the 1 percent rollback and the further proposed increase of 3.5 on April 1st, 2013, Manitoba Hydro is projected to incur losses on electric operations of $28 million in '12/'13 and $59 million in '13/14.

In Manitoba Hydro's respectful submission, allowing the electric utility to incur losses on its operations is not in the best interest of electricity ratepayers and could result in the requirement for substantially higher rate increases in the future. As evidenced by IFF12, the current financial need for rate relief remains urgent. Simply put, negative or threadbare net income places Manitoba Hydro in a chini -- challenging financial position that could impair the financial health of the Utility. The situation is certainly not in the public interest and unto itself would be sufficient reason to grant Manitoba Hydro their requested rate relief.

Before I move on, I did want to address Mr. Lafond's question regarding the use of the term IFS -- 'IFRS related' in the December 31st, 2012, quarterly report. Mr. Rainkie addressed this terminology at transcript page 509 and said that we used the term IFS -- 'IFRS related'. When we use that, we're meaning the overhead changes under Canadian GAAP that are directionally consistent with IFRS and -- and will not have to be unwound upon the operation of IFRS. As it relates to the Q3 quarterly report, we're talking about overhead and pension changes in the 2012/'13 year.

And if you could turn to slide 12, I'll deal with the second justification for Manitoba Hydro's rate increase. And that's to limit the extent to which financial ratios are projected to detet -- to deteriorate and to maintain the financial and credit rating integrity of Manitoba Hydro.

Manitoba Hydro's rate proposals are developed considering the future financial position of the Corporation, the forecasts of revenues and expenses, and the maintenance of reasonable financial targets, including ensuring that there is adequate level of retained earnings to protect against the risks that are faced by the Corporation.

As has been discussed during the hearing, Manitoba Hydro has three (3) primary financial targets that guide its revenue requirement decision-making: First, to maintain a minimum debt equity of 75/25, recognizing that it may not be possible to maintain this ratio during years of major investment in generation and transmission. Second is to maintain minimum annual gross interest coverage ratio of greater than one point two (1.2). And third is to maintain a capital coverage ratio of greater than one point two (1.2), excepting new man -- new major generation and transmission.

The evidence on the record clearly demonstrates that since the previous GRA, there has been a serious der -- deterioration in the financial outlook of Manitoba Hydro, as measured by its financial ratios. The deterioration in the projected financial ratios of Manitoba Hydro during the test years warrants serious consideration.

In IFF12, the electric operations debt-to-equity ratio is projected to meet the 25 percent target in 2012/'13, and to deteriorate to 22 percent in '13/'14. The interest coverage ratio is projected to be 1.09 percent in '12/'13 and 1.1 percent in '13/'14. The capital coverage ratio is projected to be 1.09 in '12/'13 and .89 in '13/'14, respectively. This assumes that the PUB approves the rate relief requested in its entirety.

Absent the proposed rate increases, the debt-equity ratio is projected to deteriorate to -- to

24 percent in '12/'13 and 21 percent in '13/'14. The interest coverage ratio is projected to deteriorate to .95 percent and .9 percent in '12/'13 and '13/'14. And the capital coverage ratio is projected to be .9 percent and .67 percent in '12/'13 and '13/'14, respectively.

Oh, I'm sorry. I've been saying percentages. And as Mr. Rainkie has pointed out to me, they are ratios, not percentages. It's what happens when I wing it and leave the script.

Manitoba Hydro is very concerned about the potential for the deterioration of its interest coverage ratio below one (1) -- below one (1), given that this indicates that the Utility is required to incur more debt in order to fund its interest payments to bond holders. To do so would send a negative signal to bond holders and credit rating agencies and could have negative consequences for the credit ratings of the Province of Manitoba and Manitoba Hydro itself. It would be especially troublesome to have an interest coverage ratio below one (1) when water conditions in the province are above average.

Manitoba Hydro's response to CAC/Manitoba Hydro 1-6 -- and here I'd suggest we turn to -- over to slide 14 now. That -- that IR response provides significant insight and a -- and a number of direct quotes from credit rating agency reports regarding the importance of Manitoba Hydro's financial ratios to the credit rating of the Province of Manitoba.

This Information Request has been repr -- reproduced at Tab 2 of Manitoba Hydro's book of documents. And I'm not going to review this information here but would encourage the Board members to read it.

In the past, the PUB has clearly accepted and agreed with Manitoba Hydro's evidence regarding the importance of the Corporation's financial performance on the credit ratings and the financing costs of the province and of Manitoba Hydro.

The following PUB findings from Order 116/'08 are instructive. And I'm quoting.

> "The three (3) measures of financial health and stability -- debt to equity, interest coverage, and capital coverage -- are taken seriously by debt rating agencies and others. And while the ratios may not be expected to be maintained throughout the whole forecast period due to the effects of expanded

capital program, they still remain important."

And that's at page 127 of that order. The order also says:

"It is the Board's understanding that rating agencies look predo -- prominently at Manitoba Hydro's financial strength in assessing the credit rating of the province. A weakening of the financial strength of Manitoba Hydro would not be viewed favourably by those credit rating agencies and may have implications impacting the credit rating of the province, making provincial borrowing more expensive. Such a development would not be in the public interest."

And there I'm quoting from page 130 of that Board order. Manitoba Hydro submits that the PUB's conclusion is as important today, if not more so, than it was when it was written in 2008. Certainly with Manitoba Hydro's debt representing approximately one-third (1/3) of the province's debt, it is in the public interest for Manitoba Hydro to be able to independently service that debt.

Manitoba Hydro is also concerned about the deterioration of its capital coverage ratios to levels below one (1), given that the purpose of this target is to measure the ability of the Utility to generate cash in order to fund sustaining capital expenditures from current cashflow from operations. A capital coverage ratio of less than one (1) indicates that the Utility is required to borrow more debt in order to fund its sustaining capital expenditures.

And now if we could go -- we're going to go back a page to slide 13.

The longer-term forecast, as presented in IFF12, further reinforces the need to implement the requested rate increases in their entirety. Even with the proposed increases in the test years, the reinstatement of the 1 percent rollback, and the indicative rate increases in the IFF12 of 3.95 percent per year, the electric operations retained earnings are projected to remain relatively flat to '21/'22, and the electric operations equity ratio is projected to decrease by 10 percent by '21/'22.

Oh, I'm sorry. Mr. Rainkie says I misspoke and said it was decreasing by. It's decrease to 10 percent by '21/'22.

The equity ratio is projected to show

improvement following the in-service of Keeyask and Conawapa and returns to the target of 25 percent by 2031/'32.

In IFF12, interest coverage ratios are forecasted to be lower than the target for the first thirteen (13) years of the forecast. In the longer term, interest coverage is projected to return to the 1.2 percent target level following the Conawapa generation in-service in '25/'26 and grows thereafter. Capital coverage is below target for the first four (4) years of the forecast. Then projected cashflows are sufficient to enable this target to be met in the remaining years of the forecast.

Tab 3 of Manitoba Hydro's do -- book of documents provides a summary of Manitoba Hydro's key financial targets and the projections over the twenty (20) year period of IFF12. And those were all provided on the record in Exhibit 12, pages 11 through 14. So we've -- that's Mr. Warden's presentation. And we've repro -- reproduced that for you at -- at tab 3.

MR. RAYMOND LAFOND: Mr. Warden's presentation is Exhibit 15, right, not 12?

MR. PATTI RAMAGE: Oh, I'm -- if I said 12, I meant 15.

Maintaining reasonable financial ratios

are in the best interests of the customers, as it reduces the need for borrowing and the additional financing cost that must be borne by future customers, which serves to reduce the pressure on future rates and provides more financing flexibility in the event of adverse circumstances. In Manitoba Hydro's submission, the final approvals of all of the proposed rate increases are necessary in order to accomplish the objective of maintaining reasonable financial ratios during the test years.

And now if I could have you turn forward to slide 15, I'm going to deal with the third justification Manitoba Hydro has presented, and that's to compensate for the reduced prices for non-firm electricity sales on the export market. And I'm also going to be referring to Tab 1 of the book of documents. Everyone's going to have Tab 1 memorized by the time I'm done today.

Here you'll note that there's been a significant reduction in the net extraprovincial revenues over the last five (5) years from levels well inex of -- excess of $300 million in '07/'08 to a level around $100 million in '11/'12. This reduction is primarily due to low export prices and is projected to continue into the 2012/'13 and '13/'14 test years, where the projected next -- net extraprovincial revenues are $97 million and $62 million, respectively.

In IF -- IFF11-2 there was a reduction in the forecast net extraprovincial revenues of $4 billion, as compared to IFF10-2 over the twenty (20) year period to 2031/'32. In IFF12 there's a further reduction in forecast net ext -- extraprovincial revenues of $2.9 billion, as compared to IFF11-2 over the twenty (20) year period to 2031/'32. This amounts to a total reduction of $6.9 billion over the twenty (20) year period.

The reductions in net extraprovincial revenues will have a significant negative impact on the net income and financial ratios of Manitoba Hydro in the test years. While there may be some partial offsets, such as lower -- lower financing costs, the reality is there are no other offsets that are of the same magnitude as the substantial reduction in export revenues.

Now, I should be clear here: Manitoba Hydro is not seeking rate increases in this application that would fully compensate for reductions in net extraprovincial revenues over the last two (2) integrated financial forecasts. Rather, it has proposed rate increases that balance the financial integrity of the Corporation with the customers' sensitivity to rate increases.

However, lower export prices are a financial reality that the Corporation is facing. And it's important from a rate stability perspective to recognize the dramatic reduction in net extraprovincial revenues into customer rates on a gradual basis over time. Manitoba Hydro's position is that the pro -- proposed increases are necessary in order to achieve that objective.

Now, turning to slide 16, the fourth primary justification for Manitoba Hydro's rate increase was to recognize that Manitoba Hydro's infrastructure is aging and that increased costs are necessary to maintain that infrastructure in a safe and reliable manner.

In Appendix 5.6 of its application, Manitoba Hydro explained that similar to other utilities in North America, Manitoba Hydro's generation, tans -- transmission, and distribution assets have reached an age where their overall condition is placing greater risk on reliable electric service. Many components of the electric system were installed many decades ago during the urban and rural electrification period, and some assets have been in service for more than seventy (70) years.

Historically, reliability performance of Manitoba Hydro's electris -- electrical system has been excellent. Recently, however, system reliability performance has begun to degrade, and asset condition is a con -- contributing factor. Evidence of reliability degradation is that the average number of annual customer outages has increased by 20 percent -- one point seven (1.7) versus one point four (1.4) -- over the past three (3) years. And the average duration of an outage increased by over 30 percent, from two point four (2.4) hours versus formerly one point eight (1.8) hours.

While Manitoba Hydro continues to be ranked amongst the best utilities for system reliability, we will not be able to retain that distinction if we don't invest in the infrastructure maintenance that's required.

In terms of Manitoba Hydro's ability to accommodate new load growth, thirty-seven (37) of ninety-seven (97) dis -- distribution stations in the City of Winnipeg are being operated beyond their technical limitations, with that number increasing at a rate of two (2) per year. A further twenty (20) stations are within 20 percent of their maximum capabilities, suggesting severe limitations to providing electricity service to expanding residential subdivisions or large business developments. Eight (8) stations are at least sixty (60) years old. Public safety is becoming an increasing concern as the number of streetlight standards and manholes are beginning to fail at greater rates.

The availability of Manitoba Hydro's generating usion -- units has also declined with a significant deterioration and availability of units along the Winnipeg river system due to age of equipment, unknown failure modes, and deferral of capital projects.

If we could go to slide 17. The PUB heard compelling evidence from both Mr. Hall and Mr. Morin regarding some of the diligent ef -- efforts underway at Manitoba Hydro to address the aging infrastructure issue. The maintenance of Manitoba Hydro's existing assets is essential to the province, its citizens, and all ratepayers. And Manitoba Hydro submits that it is in the public interest for it to have sufficient revenues to fund such expenditures.

I will address asset management in greater detail when dealing with CAC's comments, but I can't resist giving you a bit of a sneak preview. I can tell you that Manitoba Hydro had an asset management system in place long before CAC produced evidence on the topic in the 2008 GRA.

Given the state of Manitoba Hydro's assets, over the next twenty (20) years, substantial increases in capital investment and maintenance budgets incremental to approved levels is required to upgrade aging distribution and generation infrastructure to avoid large-scale and long-duration outages. As noted in Appendix 40, Manitoba Hydro's report on distribution asset condition dated November 9th of 2012 -- and here I'm referring to page 24 of that report:

> "The critical asset funding gap is estimated to be $1.15 billion over the next twenty (20) years. If -- if this gap was evenly funded over the next twenty (20) years, the anticipated annual incremental funding requirement would be in the order of $57.5 million per year. These expenditures will be made at today's higher cost, and it's important that rates are increased gradually to provide the funds necessary to make the necessary

expenditures to contin -- to continue
to provide safe and reliable service.
Manitoba Hydro cannot and it will not
allow safety and reliability of the
system to be compromised. This is
our fundamental mandate."

And if we could go to slide 18. I'll deal with the fifth justification Manitoba Hydro provided, and that's to provide customers with rate stability and predictability and to avoid the need for much higher rate increases in the future.

The proposed rate increases are in keeping with Manitoba Hydro's approach to implement regular and modest rate increases to ensure the maintenance of an adequate financial structure. A sufficient level of equity allows the Corporation to withstand wisks -- risks and uncertainties inherent in its operations and to address adverse financial consequences outside of its control and, in doing so, promote rate stability and avoid the need for a large or sudden rate increase in the future.

In summary, taken as a whole, IFF12 and the material that has been provided during the current rate proceeding have demonstrated that largely due to significant reductions in export revenues, the financial outlook for Manitoba Hydro Electric operations has seriously deteriorated since 2010 and the GR proce -- GRA proceeding that we -- we found ourselves in at that time.

Despite the deterioration in the financial outlook and projected financial ratios that are lower than target levels, Manitoba Hydro is propos -- proposing to maintain rate increases at the 3.5 percent level previously forecast for '12/'13 and '13/'14 to achieve the appropriate balance between customers' sensitivity and financial integrity.

This is clearly not the time to dispose of the 1 percent rate rollback as a refund to customers or to consider deferring rate increases to the future that are required today. Rather, it's in the public interest, both from a financial integrity perspective and a future rate stability perspective, to approve the rate increase request of Manitoba Hydro, including the 1 percent rate rollback, in its entirety. We need to implement rate increases today. To defer these rate increases will only result in the need for larger rate increases in the future.

Now, if we could move forward to slide 20. I'd like to turn to the issue of Manitoba Hydro's operating, maintenance, and administrative costs.

While Manitoba Hydro has proposed what it believes are the minimum rate increases necessary to preserve financial integrity and rate stability, it continues to ensure that the Corporation's OM&A costs are only those necessary to maintain safe, reliable, and efficient service to its customers.

In delivery of this service, Manitoba Hydro has experienced increases in OM&A costs as a result of significant cost pressures on key inputs, including wages and salaries, fuel, and other commodities. The in-service of the Wuskwatim Generating Station, along with the impact of accounting changes, were also key drivers resulting in higher operating expenditures. These costs and business pressures have been discussed throughout the proceeding, in the application, and through responses to Information Requests and in the rebuttal evidence.

As indicated at page 21 of Manitoba Hydro Exhibit 15 and discussed at transcript page 454, salaries, overtime, and benefits make up 77 percent of OM&A expense. The increase in wages and salaries, approximately 5 percent per year over the past four (4) years, is primarily due to negotiated contract settlements reflecting competitive pressures in the market in -- in order to attract and retain skilled employees in the increasingly competitive energy sector. Mr. Warden discussed these pressures at transcript page 458.

Manitoba Hydro has also experienced an increase in EV -- EFTs over the same period. However, the increase is primarily attributable to the growth in Manitoba Hydro's capital program, including new generation and transmission development projects such as Bipole 3 and Point du Bois and, to a lesser degree, operational support for various in -- initiatives, including the in-serve -- in-service of the Wuskwatim Generating Station and the meter compliance program. And that can be found at Manitoba -- or, PUB/Manitoba Hydro First Round 64E.

The increase in benefit costs reflects higher pension costs due to the amortization of investment fund losses, higher vacation expense due to the increase in the number of days accrued, and higher extended healthcare benefits due to negotiated coverage enhancements. According to information provided by Blue Cross, health are -- healthcare costs are increasing annually at the range of 8 to 10 percent, including prescription drugs. In addition, beginning in '11/'12, the reduction in the discount rate on pension and other benefit obligations is also contributing to higher benefit costs. And here, I'm referring to the evidence provided in Manitoba Hydro rebuttal evidence at page 11.

Manitoba Hydro's commodity costs have also increased at rates higher than inflation. At that same page 11 of its rebuttal evidence, Manitoba Hydro provided information from Statistics Canada indicating that the price of commodities such as mineral fuels, non-ferrous metals, wire, cables, and ferrous metals have increased at a rate ranging between 6 percent and 97 percent between January of 2009 and December of 2011.

Changes in accounting practices -- and I should get you to turn the page to slide 21 here. Changes to accounting practices and policies have also resulted in an annual increase to OM&A costs of $78 million since 2008/'09. These accounting changes were provided in Exhibit -- Manitoba Hydro Exhibit 55 at page 13 and are reproduced at Tab 4 of Manitoba Hydro's book of documents.

The changes include -- and I'll list four (4) of them -- 1) changes to Manitoba Hydro's overhead capitalization practices to reflect industry trends to move way from full-cost accounting and provide consistency with other Canadian utilities.

That accounts for $58 million.

I note these changes were fully endorsed by Manitoba Hydro's auditors, Ernst & Young, as evidenced in Manitoba Hydro Exhibit 78, which is an email from Ernst & Young to Mr. Warden, which indicates that, and I quote:

> "As a result of this change in approach, Manitoba Hydro's overhead capitalization methodology is more consistent with the approach most companies employ and most other utilities."

End quote. Ernst & Young also states that Manitoba Hydro's former full-costing methodology was, quote:

> "At the end of the -- at the extreme end of costing methodologies."

End quote. And that, "We," quote, "fully supported the shift in methodology," end quote. A copy of Manitoba Hydro Exhibit 78 can be found at Tab -- Tab 5 of the book of documents.

The second accounting change is the reduction in the discount rate on pension and other benefits to reflect industry trends to calculate rates in accordance with recent guidelines from the Canadian

Institute of Actuaries and lower interest rates in general. That accounts for $10 million.

The third accounting change relates to accounting class -- reclassifications, and that is $6 million.

And, finally, the fourth accounting change is the change in Canadian accounting star -- standards with respect to intangible assets; and that's $4 million.

Manitoba Hydro continues to maintain a number of cost-constraint initiatives, including restrictions on external hiring, out-of-province travel, overtime, and reductions in community sponsorships and donations. Cost savings have also been achieved as a result of centralization of staff at both 360 Portage and 820 Taylor, resulting in lower facility lease costs, maintenance and property services, as well as energy efficiencies in the new building.

Manitoba Hydro has also engaged in continuous process improvement activities to gain operational efficiencies and continuously improve productivity in managing its resources and op -- and controlling its expenditures. Process improvements include automa -- automation, utilization and coordination of resources, and reviews of work procedures, including standardized work practices. And here, for my authority, I refer to rebuttal evidence at page 11.

And if we could turn to slide 22. In order to demonstrate its success in constraining OM&A costs, Manitoba Hydro provided an -- an analysis of the average annual increase in OM&A costs, including cost projections forecast in IFF12. This analysis is reproduced at tab 6 of the book of documents. It was provided at page 19 of Manitoba Hydro Exhibit 15.

This analysis demonstrates that Manitoba Hydro has limited increases in OM&A costs to an average annual increase of 1.68 percent net of accounting changes and that the incremental costs associated with the in-service of the Wuskwatim Generating Station over the period 2009/'10 through '13/'14.

This is below the average annual increase in Canadian CPI of 1.82 percent over the same period. It's also of note that the 1.68 percent is achieved at a time when increased costs are being incurred to maintain an aging infrastructure, and customer numbers are growing at an average rate of five thousand dollars ($5,000) per year -- five thousand (5,000) customers per year. It's a good thing I have people to whisper to me on either side. The reference for that five thousand (5,000) customers can be found at transcript page 451.

It's also important to recognize that CPI is a general measure of the cost changes of a standard basket of goods to a general consumer. CPI is generally not reflective of the cost inputs of a business like Manitoba Hydro, which consists mainly of wages, benefits, fuel, materials, and contractor services. The cost of these business inputs has risen at a much higher rate than CPI since the last GRA, as evidenced by the indices, such as average weekly earnings, industrial price indices, and raw material prices.

CAC's assertion that Manitoba Hydro's achievement of maintaining OM&A at or near inflation is not enough -- that that's not enough completely fails to recognize this critical point.

MIPUG had indicated at page 6-4 of their written final argument that OM&A costs had grown by 3 percent -- by a 3 percent annual increase after adjusting for accounting changes in Wuskwatim. However, this analysis is strums -- strategically selective in that it extends to a period of time where Manitoba Hydro filled a number of vacancies that occurred in the prior year and hired a number of additional trainees to address anticipated higher attrition rates. But the analysis didn't go back further to those previous years. The -- that evidence came out in the 2010 GRA.

Finally, with respect to OM&A, Manitoba Hydro is very concerned with the number of recommendations which entail hiring third-party consultants for the purpose of reviewing work performed by the professionals in the employee of the Corporation. Despite repeated concerns repar -- regarding operating costs, there appears to have been little recognition in the costs associated with these type of recommendations.

I'd now like to turn to the recommendations of Intervenors.

THE CHAIRPERSON: Ms. Ramage, I -- while the panel is relaxing and hearing -- listening to your -- to your discourse --

MR. PATTI RAMAGE: M-hm.

THE CHAIRPERSON: -- I'm concerned about your voice and so on. So I'll wait for a signal from you to let me know when you need a break, okay.

MR. PATTI RAMAGE: Thank you very much. I -- I will let you know. What we are going to do is

Ms. Fernandes -- I forgot -- I kind of jumped right in this morning without... Ms. Fernandes is going to take over for a piece.

So I'm also concerned that the Board is going to get tired of hearing from us, because this is a little dry.

THE CHAIRPERSON: You are dealing with some accountants here. We're kind of used to that. I would say that -- let's -- let's go -- let's go on for a while. I'd just say let's aim for a break around 10:30 or so. Okay.

MS. PATTI RAMAGE: That would be perfect, and it -- we may well line up with the switch to Ms. Fernandes too. But as I say, I want to make sure the Board gets its breaks too, so...

I wanted to turn to Manitoba Hydro's reply to the recommendations of Intervenors with respect to the rate increases in the test years. And here it's -- we're at slide 25, and I'm dealing with MIPUG's rate proposal.

Mr. Hacault has alleged that Manitoba Hydro's rate proposals are based on changes in accounting policies. Manitoba Hydro can demonstrate this is not the case. Mr. Hacault, on behalf of MIPUG, makes the statement that:

"Manitoba Hydro's accounting changes represent in excess of 10 -- of 10 percent rate pressure on domestic rates each year."

And here I'm referring to page 1-3 of MIPUG's final argument. I'd add that Mr. Hacault also made the point early on in his argument that we should be focussing on the two (2) test years on the Man -- on those two (2) test years. Manitoba Hydro agrees with that sentiment.

Ironically, MIPUG appears to have abandoned this principle in -- in their analysis leading to the statement that Manitoba Hydro's accounting changes represents in excess of 10 percent rate pressure on domestic rates each year. In making this assertion, Mr. Hacault has relied on Manitoba Hydro Exhibit 55, which is produced at Tab 4 of Manitoba Hydro's book of documents.

Mr. Hacault referenced accounting changes in excess of $137 million per year. And if we turn to Tab 4 and we look at page 2 of 13 of that document, you'll see $137 million at the bottom of the page under the year 2015. And that $137 million included IFRS changes, and it's outside the test years and it's -- in that it's in 2014/'15.

MIPUG has conveniently ignored that the $113 million decrease in depreciation and amortization expense that -- they've conveniently ignored, if you turn the next page, I should -- you'll see that they -- we've ignored $113 million decrease in depreciation and amortization expense. And that's at page 3.

This gives us a net amount of $24 million, or 1.8 percent of revenue requirement; a far cry from the 10 percent and very close to the range that Mr. Hacault referred to at transcript page 5,905 as not being such a huge issue. And it is, in fact, merely a percent or something which Mr. Hacault said, at transcript page 5,958, is something that we can deal with.

If we actually look at the test years and apply the same logic, you'll see at page 1 of Tab 4 -- I think we're looking at page 2 actually -- that the total OM&A accounting changes are 75 and $78 million in the test years, and that page 3 -- depreciation offsets on page 3 are 40 and $44 million respectively, for a net impact of 35 and $34 million. These financial reporting changes are hardly driving the rate increases, as claimed by MIPUG.

(BRIEF PAUSE)

MS. PATTI RAMAGE: In their final arguments, both MIPUG and CAC recommended the following with respect to Manitoba Hydro's rate proposals for the test years:

1) that the accumulated balance in the deferral account related to the 1 percent rate rollback directed in Order 5/'12 be returned to cus -- to customers.

Second, that the rates for '12/'13 and '13/'14 be finalized at the current levels approved on an interim basis as at September 1st, 2012, including the reinstatement of the 1 percent rate rollback approved in rates effective April 1st, 2012, and that the 3.5 percent rate increase effective April 1st, 2013, be denied.

In order to justify these alternatives -- alternative rate proposals, MIPUG has recommended that the PUB make -- PUB make two (2) adjustments in Manitoba Hydro's 2012/'13 and 2013/'14 revenue requirements for rate-setting purposes.

Here, if we go to slide 26, we outline that increased -- MIPUG's position is that increased overheads capitalized by 56 million and 58 million in 2012/'13 and 2013/'14 respectively will reduce OM -- OM&A costs by corresponding amounts.

They also remec -- recommended to remove net salvage from depreciation rates, effective April 1st, 2012, with an estimated reduction of depreciation expense of approximately $60 million in each of the test years.

And finally, they remec -- recommended removing the long-term debt associated with the new generation projects that are not yet in service from the calculation of the debt-to-equity ratio for rate-setting purposes.

In recommending increasing overheads capitalized by between 56 and $58 million in the test years, MIPUG is essentially requesting the PUB return to the overhead capitalization practices of Manitoba Hydro prior to 2008/'09 for rate-setting purposes some five (5) years ago.

Historically, electric utilities apply the full-cost accounting approach under Canadian GAAP, whereby common overhead charges, such as depreciation on head office buildings, were included in the cost of capital items. However, the interpretation and application of Canadian GAAP by utilities has changed over the years such there's been -- that there has been a reduction in the general and indirect overheads that are -- are being capitalized today as compared to the past.

As explained in response to PUB/Manitoba Hydro First Round 79A and PUB/Manitoba Hydro Second Round 52A, the overhead capitalization changes implemented today by Manitoba Hydro recognize industry trends to move away from full-cost accounting and, as a result, are designed to make Manitoba Hydro's practices more consistent with those of other Canadian electric utilities.

One has to as: If these policies are just and reasonable in other jurisdictions for the purpose of rate setting, why would they not be reasonable here? The policies are fully compliant with Canadian GAAP and have been fully endorsed by Manitoba Hydro's external auditors, as was evidenced by the information provided in Manitoba Hydro Exhibit 78. And I previously referenced the email communication between Ernst & Young and Mr. Warden that's found at Tab 5 of the book of documents.

Page 13 of Tab 4 of Manitoba Hydro's book of documents provides a summary of the overhead accounting changes for the period of 2009/'10 to 2013/'14. On pages 96 and 97 of Order 116/'08, the PUB expressed concern over the aggressive deferral and capitalization of operating costs under the full-cost accounting approach that was previously employed by Manitoba Hydro and recommended, at page -- in paragraph 2 at page 340, that the Corporation consider the early adoption of less-aggressive IFRS overhead capitalization practices.

In this context, the PUB was using the term 'less aggressive' to mean capitalizing less overhead costs. During cross-examination of Mr. Bowman, Manitoba Hydro walked through the reduction to cost capitalized since 2000 -- '08/'09, as ex -- as set out in Manitoba Hydro Exhibit 55, and compared it to the information which the Board referenced in Order 5/'12 - that is, information filed during the course of the 2010 GRA.

What is evident from this exchange what can be -- which can be found at transcript page 5,554, is that the PUB was well aware of Manitoba Hydro's intention to reduce the amount of overhead being capitalized. It did not take exception to these overhead capitalization changes for rate-setting purposes and, if anything, expressed the concern that even with these changes, Manitoba Hydro's capitalization practices were overly aggressive.

MIPUG attempted to minimize the significance of the PUB's acceptance of the changes on the basis that the PUB characterize the changes as being for the purpose of -- of transitioning to IFRS and that IFRS has been deferred. The fact is, the Board was well aware that IFRS was not going to be implemented during the test years in the 2010 GRA.

With this knowledge, the PUB reiterated its concerns from Order 116/'08 about the po -- potential for aggressive deferral and capitalization of operating costs which could burden fur -- future ratepayers. And that reference can be found at page 85 of Order 99/'11.

The PUB wasn't talking about IFRS. They were talking about Manitoba Hydro's accounting policies in place at that time. Further, the PUB did not take exception to those -- these overhead capitalization changes for rate-setting purposes in Order 5/'12, the final order resulting from the 2010 GRA. Tab 8 in Manitoba Hydro's book of documents contains the relevant excerpts from these orders.

MIPUG's view that the changes to overhead capitalization practices are inconsistent with Manitoba Hydro's projected increases in capital spending in the future is flawed and appears to be based on the misunderstanding that the changes are somehow resulting in direct capital costs being expensed as operating costs. This is not the case.

In pages 3 to 5 of Appendix 5.6 of the application, and in response to PUB/Manitoba Hydro First Round 44A and PUB/Manitoba Hydro First Round 79A, Manitoba Hydro described the nature of the costs that are being expensed under current industry practices as being sunk costs; that is, building depreciation and IT infrastructure costs or costs which do not vary directly based on the level of capital activity - for example, executive costs.

Without a direct relationship to a capital asset, these costs are more closely linked to current operations. And as such, it is appropriate from a rate-setting purpose -- or perspective that they be borne by current ratepayers that derive the majority of the benefit of these expenditures.

On transcript page 5,353, Mr. Bowman contends that, quote:

> "On a full-cost basis, you would look through your ledger of costs and clu -- conclude which are fundamentally supporting the capital program, and capitalize those."

End quote. That is exactly the process that Manitoba Hydro went through to identify costs that are not fundamentally supporting the capital program and, as such, do not fluctuate from year to year based on changes in Manitoba Hydro's capital spending.

It's also interesting to note that at transcript page 5,354 Mr. Bowman indicates he is accepting of the change that is being made in the 2012/'13 year to remove depreciation expense on common buildings as an item of overhead capitalized. Given that depreciation is a carrying cost of common assets, logic dictates that property taxes and interest on common assets and motor vehicles should be removed from overhead capitalized as well.

Manitoba Hydro implemented these very changes in 2009/'10 and 2010/'11. In fact, the removal of depreciation, interest, and property taxes on common assets and -- and motor vehicles from overhead capitalized represents over $28.5 million, or approximately 50 percent of the reductions to overhead capitalized that Manitoba Hydro has implemented in the last five (5) years.

As such, it's very puzzling why Mr. Bowman would recommend an increase to overhead -- overheads capitalized of between 56 and 58 million in the test years when the logical extension of his own testimony dictates elsewise -- otherwise.

The evidence is clear. MIPUG's recommendation to return to the overhead capitalization practices employed by Manitoba Hydro prior to 2008/'09 are inconsistent with current Canadian electric utility practices, they're inconsistent with past findings and recommendations of this Board, and they ignore information that was provided by Manitoba Hydro during the GRA proceeding that explains the reasons for the changes to overhead capitalization pol -- practices.

Manitoba Hydro does not support a recommendation to return to the previous overhead practices when the more recent changes have clearly been accepted for rate-making purposes by the PUB. MIPUG's recommendation should be rejected.

The detailed arguments with respect to the overhead capitalization policies, just for the record, can be found in Section 2.1.1 to 2.1.3 and on pages 2 to 6 of Manitoba Hydro's rebuttal evidence.

Moving to slide 27. As was outlined in Appendix 5.7 of the original application, the depreciation study that was reviewed as part of this GRA was different than previous depreciation studies. In addition to the normal update of service lives, this depreciation study also involved an assessment of IFRS-compliant depreciation practices and methodologies, given that Manitoba Hydro will be required to implement IFRS. Due to the deferral of IFRS, the implementation of the depreciation rates resulting from the current study will accomplished in two (2) phases.

In the first phase, Manitoba Hydro implemented the updated service lives and new asset component groupings effective April 1st, 2011. In the second phase, Manitoba Hydro plans to implement IFRS-compliant depreciation rates upon the adoption of IFRS, which will include a change in the depreciation methodol -- methodology to the Equal Life Group and the removal of asset retirement costs from depreciation rates.

Now, I'll -- I'll address the Equal Life Group methodology later in the argument, but right now I wanted to address the removal of asset retirement costs from depreciation rates, at is -- as it is a matter that has been raised by MIPUG as an issue for consideration during the test years.

And we're at slide 28 now. MIPUG is recommending that Manitoba Hydro remove net salvage costs from electric depreciation rates under Canadian GAAP commencing in the 2012/'13 test year. MIPUG's rationale is that the provision for net salvage is a discretionary concept that is not a precise calculation of asset removal cost and that it does not recognize the future value of developed sites for generating stations or transmission lines.

Including net salvage costs in depreciation rates is a regulatory construct that promotes intergenerational equity for ratepayers and is permitted under Canadian GAAP, consistent with the recognition of rate-regulated assets and liabilities.

Manitoba Hydro is planning to retain net salvage costs in electric depreciation rates until the adoption of IFRS. Manito -- Manitoba Hydro's proposal to change its practices with the implementation of IFRS is driven by the fact that rate-regulated accounts are not currently permitted under IFRS. Under IFRS, the future cost to retire and salvage assets will become a co -- a cost of the replacement asset.

Mr. Bowman asserts that the net -- net salvage is a concept of putting aside some money because some day I might have to remove a pole, and I'd sure like to have a place to charge the cost that isn't called capital or operating. Those comments do not reflect the intent behind including such costs in depreciation rates.

Mr. Bowman also states, You don't start putting away 10 percent just because 10 percent seems like a good number. Manitoba Hydro contends that although the exact timing of when physical plant assets may be replaced or retired may not be known, there is no doubt that ultimately each plant asset will be replaced or retired, and upon such date, costs will be incurred to remove the asset from operation.

The purpose of including net salvage costs in deprecian -- depreciation rates is to promote fairness in rate-making by ensuring that the current ratepayers benefiting from the respective assets are bearing some of the costs of removing those assets from operations when the assets are at the end of their useful life.

Further, Manitoba Hydro doesn't agree with MIPUG's assertion that the provision for net salvage does not recomme -- does not recognize the future value of developing sites for generations -- generating stations or transmission lines. The provision is based on a percentage of the original cost of the asset. And as discussed during the hearing at transcript page 1,959, the percentage is not increased on an annual basis for inflation or updated for estimates of future removal cost.

In the example provided in the hearing, if Point du Bois cost $100 million in 1911, the te --

the 10 percent salvage factor would recover $10 million over the life of the asset towards removing the Point du Bois asset from service. In today's dollars, the cost of -- to remove Point du Bois from service or to replace cer -- certain aspects of Point du Bois would far exceed the $10 million, which demonstrates that the salvage factor recognized that there continues to be future value in developing sites despite replacing the asset itself.

Overall, the inclusion of a provision for net salvage costs in depreciation rates provides a measure of intergenerational equity. While on its own Manitoba Hydro would not favour the removal of net salvage from depreciation rates upon transition to IFRS, we do recognize that the removal of net salvage cost provides an offset against some of the other costs of transition to IFRS and thus is an exupt -- is an acceptable tradeoff in order to mitigate the impacts of IFRS for ratepayers.

Manitoba Hydro is of the view that it should maintain net salvage under Canadian GAAP while it considers its options with respect to IFRS conversion and the potential for an interim or a final standard that per -- permits the recognition of rate-regulated assets and liabilities.

It's important to recognize that as part of the first phase of implementation of the depreciation study, Manitoba Hydro has already made significant reductions to depreciation expense through the change of asset surfa -- service lifes. As set out in page 3 of -- of Exhibit 55 -- and that's Tab 4 of our book of documents -- these reductions amount to $40 million in 2012/'13, and $44 million in '13/'14. Before making any further significant reduction in depreciation expense, Manitoba Hydro believes it would be prudent to understand the full implications of IFRS and rate-regulated accounting.

Manitoba Hydro is also concerned that the policy of net salvage under Canadian GAAP may be construed as a change in accounting policy, requiring a retroactive reinstatement -- or restatement of Manitoba Hydro's financial statements. This was discussed at transcript page 1,751.

Manitoba Hydro doesn't support MIPUG and CAC's recommendation for an early adoption of the removal of net salvage from depreciation rates, as to do so would impair intergenera -- intergenerational equity, may have to be treated as a retrospective change in accounting pol -- policy, and may jeopardize Manitoba Hydro's ability to carry forward asset net book values on transition to IFRS.

Manitoba Hydro is appropriately managing the collective package of accounting policy changes in a way that will minimize rate impacts to customers and avoid the need for large rate increases in the future.

THE CHAIRPERSON: Can I just ask a few questions and perhaps give you a break, Ms. Ramage, in relation to the statements you just made in respect of the change in accounting pol -- you know, the -- if we effect a change to net salvage immediately, it may have to be treated as a retrospective change in accounting policy. And also you go on to say it might jeopardize Man -- Manitoba Hydro's ability to carry forward asset net book values on transition to IFRS. I'm reading directly from -- from the overhead here.

Mr. Rainkie, could you -- could you extrapolate? Could you give us more information about what -- what's being said here, please?

MR. DARREN RAINKIE: In both items, Mr. Chair, or just the last one, the --

THE CHAIRPERSON: Both items.

MR. DARREN RAINKIE: Both items. What we're -- maybe I'll start with the second one first, and then I'll get back to the -- to the first one.

As I noted at some point during these

proceedings, one of the exemptive relief that the International Board did provide to Canadian rate-regulated entities in moving to IFRS is that we would not have to go back and restate all of our plant records and for all of the different practices that we've had over the years -- decades -- in Canada. And that's a very important thing to -- it's a very important elective exemption which we're going to take.

So we really don't want to do anything at this point that would impair our ability to do that because we're able to drag the net book value over on -- on transition to IFRS. So certainly, that's a very big concern for us. If any other change would have -- would -- would make us go back and have to restate how would that interact with that -- that exemption that we've been granted.

Also, right now we have not segregated out a cumulative impact of net salvage value as a rate-regulated asset in our accounting statements. It's been smushed together with depreciation over the -- over the decades. I think it would even be impossible for us to really even try to break that out.

So that leaves us with this difficulty, I suppose, with our auditors, in terms of if it hasn't been classified as a rate-regulated liability in the past and we were to get a directive of the Board, is it something we could do on a prospective basis, or is it something that we would have to go back and restate.

So there's uncertainty about -- about this. It's not quite as black and white as was implied by the Intervenors on Monday.

MS. PATTI RAMAGE: Noticing it's 10:30, it might be a good time for a break, because I'm not as close to handing off the mic to Ms. Fernandes as I had hoped.

THE CHAIRPERSON: Okay. Okay. Let's take a ten (10) minute break. Thank you.

--- Upon recessing at 10:28 a.m.

--- Upon resuming at 10:42 a.m.

MS. PATTI RAMAGE: Ready? Before I move to MIPUG's recommended adjustments to the debt-to-equity ratio calculation, I should comment on the cashflow implications of MIPUG's recommendations. And this is slide 29.

While MIPUG's recommendations appear on face value to be simply accounting adjustments for rate-setting purposes, these recommendations adversely impact Manitoba Hydro's cashflow. The cashflow difficulty with these proposals was highlighted by the undertaking requested by the PUB at transcript page 5,401. That -- that undertaking asked for interest in -- and capital coverage ratio implications arising out of MIPUG's recommendations.

In MIPUG Exhibit 10, which is reproduced at Tab 9 of Manitoba Hydro's book of documents, it is apparent that over the five (5) year period to 2017, MIPUG's proposals would reduce Manitoba Hydro's cashflow by nearly $243 million. All other things being equal, this deficit would need to be financed with additional debt or with future rate increases.

And if you turn to slide 30. MIPUG has recommended that Manitoba Hydro should revise the debt-equity ratio calculation by removing the long-term debt associated with new generation projects that are not yet in service. The proposed calculation is theoretical in nature and could result in the PUB having a very different assessment of the financial position of the Corporation than any other user of the financial statements.

To that end, Mr. Bowman himself acknowledged on page 5,664 of the transcript that the proposed adjusted equity ratio is a notional calculation, that it does not reflect the actual amount of the debt issued by Manitoba Hydro. He acknowledged that Manitoba Hydro will need to report its actual debt-equity ratio in its audited financial statements. And he acknowledged that credit-rating agencies will use the actual debt-to-equity ratio as reported in the audited financial statements.

Given that one (1) of the purposes of regulation is to ensure the financial integrity of the Utility for the benefit of the ratepayer, having such a theoretical calculation that reflects only a portion of the Corporation's debt leverage is potentially confusing and misleading.

And we'll turn to slide 31. I'd like to briefly address MIPUG's assertion that the level of reserves and annual contribution to reserves that Manitoba Hydro requires could be reduced because of a decrease in the projected cost of a five (5) year drought to $1.6 billion in IFF12.

In making this assertion, MIPUG is ignoring a number of facts. First, MIPUG is comparing the cost of a five (5) year drought in IFF12 to that of a similar drought in IFF09. Manitoba Hydro adopted its current equity ratio target of 25 percent in 1995. Since that time, the cost of a five (5) year drought has increased, but there was no upward adju --

adjustment of the debt-to-equity ratio target to compensate for that increased cost, nor should it be decreased as a result of the decreasing cost of a drought.

Second, the 25 percent equity target is designed to pro -- protect Manitoba Hydro from all its risks, not only drought risk. There are a number of other risks, such as infrastructure risks, interest rate risks, and foreign exchange risks, to name a few. Manitoba Hydro notes that it faces a number of different types of infrastructure risk, and infrastructure risk is much broader than the risk of losing Bipoles 1 and 2 for an extended duration. Natural disasters such as fire, tornados, ice storm, are real concerns and have caused significant damage in the past. For example, at page 600 of the transcript, Mr. Cormie describes the recent fire at Jenpeg which caused a complete shutdown and physical damage in excess of $10 million, which could take up -- up to a couple of years to repair.

Third, in addition to business risk, there are also financial risks associated with the increased level of leverage and higher rate -- and higher rate increases -- the rate increases forecast in IFF12. MIPUG has ignored the higher level of financial risks.

Fourth, MIPUG has emphasized that the emphasis -- emphasized that the $1.6 billion cost of drought is a differential cost and not the projected losses associated with a five (5) year drought. While this is true, if one closely examines the five (5) year drought scenario that has been provided in Manitoba Hydro Exhibit 38 -- and that's included in Tab 10 of the book of documents. And if you look at Tab 10, one can see that Manitoba Hydro -- what page are we? At page -- it's 2 of 2. The second page in. Oh, I'm sorry, it's page 2 of 7 that's included in Tab 10.

(BRIEF PAUSE)

MS. PATTI RAMAGE: Okay, I just wanted to make sure I was at the right one. It's page 2 of 7 that is actually four (4) pages in on that tab.

You can see that Manitoba Hydro experiences a significant loss in each and every year of this scenario until '21/'22. While the Corporation benefits from a lower value of -- value of export losses and lower-cost power purchases related to drought in a per -- in a period of low export prices, the Corporation's ability to recover from the cost of drought in the absence of rate assistance from customers is also dis -- diminished due to lower subsequent net export -- extraprovincial revenues.

This is demonstrated by the delay in returning to the $2.5 billion level of retained earnings until the end of the forecast period in 2031/'32 in the drought scenario. I note that the $2.5 billion retained earnings is reached by '24/'25, or nine (9) years following the final drought year in the IFF09 scenario, compared to '29/'30, or eleven (11) years following the final drought year in the IFF12 scenario. Were it not for the higher indicative projected rate increases in IFF12 compared to IFF09, this recovery would otherwise occur several years later.

If the Corporation were to experience an additional period of low water flows or one (1) of the other risks identified in -- within this time frame, Manitoba Hydro would be very limited in its capacity to shield ratepayers from the significant rate increases that may be required. This is contrary to the objective of stable rates that MIPUG advocates.

Now turning to slide 32 --

THE CHAIRPERSON: Could I ask you a question in relation to slide 31? There's a statement that I found to be dissonant, and I'm thinking -- I'm looking at the third bullet:

"There are financial risks associated with an increased level of leverage, agreed, and higher rate increases forecast in IFF12."

Now, what exactly is meant there?

(BRIEF PAUSE)

THE CHAIRPERSON: And -- and thus...

(BRIEF PAUSE)

MS. PATTI RAMAGE: Yeah, Mr. Rainkie has confirmed, I think I have the right answer. And that's -- it -- it's to demonstrate that the IFF is very sensitive to the rate increases and the importance of that 3.95 percent that's in there. And I note that that -- at IFF09 it -- it wasn't a 3.95 percent increase that was forecast at that time.

MR. RAYMOND LAFOND: The way I read that was level of leverage and higher interest rate increases than forecast in IFF12. I mean, you're -- you've got to tie interest to the leverage aspect.

(BRIEF PAUSE)

MS. PATTI RAMAGE: I -- I think the intention there was two (2) separate things, but...

THE CHAIRPERSON: Right. But -- but I think -- I agree with panel member Lafond that this is -- the formulation he suggested is probably the right approach? I think -- I just wanted to clear up...

(BRIEF PAUSE)

MS. PATTI RAMAGE: Yeah, I'm -- I'm a little concerned. I'm not sure I can -- I can answer Mr. Lafond's question without --

THE CHAIRPERSON: Okay. It's just that -- it jumped up at me right away when I read it. It doesn't -- it didn't seem to make any sense. So I just -- based on what we saw, a 1 percent increase in -- in interest rates had a $700 million impact. And I think that's what is meant here, and I just wanted to confirm that with you. Impact -- yeah, that's right, impact over ten (10) years.

MS. PATTI RAMAGE: Okay. I think -- I think that's, true what you're saying. But what hasn't been done is quantified what the 1 percent decrease in a rate would do to the same forecast. And we don't have that sensitivity.

MR. RAYMOND LAFOND: So you will clarify this statement later on?

MR. PATTI RAMAGE: Maybe after the break we can clarify it so I can have a chance to speak to Mr. Rainkie.

(BRIEF PAUSE)

MR. PATTI RAMAGE: Turning to slide 32. Mr. Hacault argues that retaining the 1 percent deferral undermines the conclusions in Order 5/'12. I've already walked through the PUB's orders leading up to this GRA, and I'd simply remind the PUB of the following findings.

In Order 5/'12 the PUB said:

> "Rather than requiring Manitoba Hydro to immediately reduce its rates, the Board orders that the rate differential between what was approved on an interim basis and what has now been finalized shall be quantified by Manitoba Hydro and remain as an interim rate, with its

associated revenues being accumulated by customer class with accrued interest in the previously described deferral account."

And then in Order 32/'12 the PUB stated that:

"The final disposition of the deferral account and the 1 percent interim rates are matters best resolved through the upcoming GRA."

Clearly, the PUB's intentions with respect to the 1 pen -- percent deferral have not been undermined, because the PUB wanted to wait until this GRA to determine what its intentions would be.

And at slide 33, we're dealing with MIPUG's exception to the treatment afforded the general service large class with respect to interim rate schedules approved effective September 1st, 2012.

To recap, Order 116/'12 approved a 2.5 percent interim rate increase for all domestic customers effective September 1st, 2012. Immediately upon issuance of Order 116/'12, Manitoba Hydro filed rate schedules which would yield an increase -- would yield an increase in revenues of 2.5 percent from each customer class. However, due to the rate design associated with some classes, the percented in -- increase of each component of the rate was not necessarily 2.5 percent.

For example, the residential class Manitoba Hydro -- for the residential class, Manitoba Hydro proposed to recover the entire 2.5 percent increase in the energy charge and propose no change to the basic monthly charge. This meant that the residential charge would increase by 2.7 percent, with no change to the basic monthly charge. As Mr. Wiens noted at transcript page 2,675, while this was consistent with past practice, the Board did not agree with the rate schedules and provided additional direction.

Manitoba Hydro's understanding of that additional direction is set out in a letter to the PUB, dated August 31st, 2012, a copy of which can be found in MIPUG's book of documents, which is Manitoba Hydro -- or MIPUG Exhibit 6, and it's at Tab 10. It's been included in Manitoba Hydro's own book of documents at Tab 11.

Mr. Wiens summarized the PUB's direction at transcript page 2,675. They did not want to see any increase in energy charges over and above the 2.5 percent; that -- that Manitoba Hydro could request increases in demand charges up to 2.5 percent but no increase in basic monthly charges. Mr. Wiens went on to confirm that this ultimately reduced the amount recovered for the residential class by seven hundred and thirty thousand dollars ($730,000), or what amounts to a 2.3 percent increase.

MIPUG is seeking an adjustment to the September 2012 interim rates for the general service large class so as to reduce the rate increase applicable to that class to 2.3 percent. And here we're at slide 34. As noted by Mr. Wiens at transcript page 2,697, the result would be a decrease in revenue collected by Manitoba Hydro of five hundred and one thousand, six hundred and fifty-five dollars ($501,655).

Manitoba Hydro does not believe it is logical to reduce revenues in one (1) class simply 'cause -- because one (1) component of another class's rate structure was not increased by the Board.

The fact is, Manitoba Hydro applied for a 2.5 percent increase effective September 1st. The parties were afforded the opportunity to make submissions on the rate application. And the Board rendered its decision to approve a 2.5 percent increase. That the Board's clarification resulted in less revenue than originally contemplated being collected from one (1) customer class is not in and of itself a basis to reduce the approved increase for all classes.

What we have here is a relatively minor departure from the historic pure, across the board class revenue increase. But the impact on the GSL cost per kilowatt hour is less than point zero-zero-seven (.007) cents per kilowatt hour. As such, Manitoba Hydro submits it's not necessary to make any further adjustments.

And now if we go to slide 36.

(BRIEF PAUSE)

MS. PATTI RAMAGE: CAC's rate proposals mirror those of MIPUG's. They -- they argue that the proposed rates should be reduced on account of alleged failures to manage assets in an optimal fashion, the need to fund Wuskwatim imback -- impacts, and the alleged failure to manage energy efficiency initiatives in a reasonable manner. It's unclear, however, how the -- how CAC quantified these alleged failures and turned them into the need to deny Manitoba Hydro's proposed rate increases.

Dealing with the asset management issue, CAC argues that Hydro is clearly behind the curve, in terms of good asset management practice and reporting as compared to other jurisdictions in Canada. Manitoba Hydro disagrees with this assertion.

Based on Manitoba Hydro's historical performance and asset replacement rates, it is evident aggressive replacement of these assets prior to the end of their serviceable lives was not required, resulting in the deferral of hundreds of millions of capital expenditures which would have been passed on to ratepayers. However, due to the timing and magnitude of the original installation of distribution assets, the existing replacen -- replacement rates are no longer adequate and will need to be increased. This was discussed in Manitoba Hydro's application at Appendix 5.6, 'Aging Infrastructure', at page 2.

Manitoba Hydro has continually improved its level of asset -- of asset assessments and long-term capital planning in an effort to maximize asset life seg -- cycles and associated operating costs. To have allocated additional resources for assessing assets earlier in the asset's life or replacing them at a time when they were still in reasonable condition would not have added value to the Corporation or its ratepayers.

Contrary to MIPUG's assertion that there is an inconsistency between the extension of service lives and the need for asset replacement, the opposite is true, as demonstrated when you consider that the assets in need of replacement were installed post-World War II and have performed well beyond their original estimated life. Manitoba Hydro now needs to replace those assets, and it is also appropriate then to reevaluate those lives based on this experience.

Power supply and transmission business units have both implemented comprehensive reliability-centred maintenance, or RCM programs, more than a decade ago, as referenced in Manitoba Hydro's response to CAC/Manitoba Hydro Second Round 15A. These programs acknowledge the risks associated with particular categories of assets and establish maintenance plans to deliver the desirable level of reliability. Thorough reliability studies based on asset failures are part of these programs.

As discussed in Manitoba Hydro's response to PUB/Manitoba Hydro First Round 82B, Manitoba Hydro has taken various steps to enhance the sophistication and accuracy of assessing the condition of its generation, transmission, and distribution assets. I can provide five (5) quick examples.

1) Implementation of the asset investment planning software and processes to facilitate twenty (20) year capital planning for aging generation asset rehabilitation or replacement based on asset condition.

A second example: use of an equipment health-rating methodology for eight (8) significant equipment categories at fourteen (14) hydraulic generating stations.

A third example: conducting an example of all outages and maintenance issues to identify the root cause of the failure.

Another example: undertaking a detailed study of three (3) critical transmission asset categories: transmission lines, substation transformers, and breakers.

And finally, completion of the distribution asset condition report, detailing the condition of eight (8) critical distribution asset categories. As noted in Exhibit 98, the transmission asset condition report is near completion and will be filed following internal reviews. In Exhibit 92, we learn that the report for the generation assets is expected to be completed by December 31st, 2013.

Prioritization of the overall capital portfolio considers safety; reliability; customer requirements; compliance with regulation; environmental and financial impacts, including risk deferral. Varying methods of priortor -- prioritization are used by the business units to assist the executive in making decisions for the allocation of capital dollars and resources.

And turning to slide 37. CAC's rate proposal is premised on the notion that ratepayers should not be required to bear the burden of the impacts of Wuskwatim coming into service and the drop in export revenues in the opportunity market. Instead, Manitoba Hydro should be required to seek internal efficiencies to make up for these costs, which CAC attributes to forecasting errors.

As Mr. Warden stated at the outset of the hearing, Manitoba Hydro does not apologize in any way for its forecasts. And that can be found at transcript page 438. Forecasts are always prepared with the best information at the time the forecasts were put together.

The changes that have been occurring in the energy market over the past four (4) years have been described as game changers. CAC hasn't produced any evidence suggesting there is anyone who had the predictive ability to have forecast a 41.7 percent drop in extraprovincial revenues or a 54.3 percent drop in the cost of natural gas to supply the Manitoba market.

It's interesting that Mr. Dunsky agreed with Mr. Warden and indicates at transcript page 4,261 that -- and I'm quoting:

"The more we have to look into the future, the greater the risk of us getting it wrong is. Again, it's no criticism of forecasters. Things happen, you know. Sudden, worldwide economic crises happen, and we can't forecast them."

While Manitoba Hydro disagrees with CAC's suggestion that the need for -- the -- the need for the proposed rate increases is a result of the Corporation's poor forecasting, it does agree that it is reasonable to expect that the Corporation do its part to limit costs before seeking rate increases.

As I had previously outlined, Mr. Warden provided evidence of the steps Manitoba Hydro has taken to constrain costs. These included hiring and overtime restrictions, reductions to sponsorships and donations, and leveraging technology. Manitoba Hydro has succeeded in limiting increases in OM&A expense to 1.68 percent per annum, which is less than the rate of inflation. But as noted by Mr. Thomson, there are limits to what can be achieved, and he said, "You can't cut your way to prosperity." That would be found at transcript page 313.

As he -- further stated by Mr. Thomson, quote:

> "You cannot operate a utility of the geographic scope of Manitoba Hydro without people, and labour represents the Corporation's largest operating cost, at 77 percent."

End quote. When storms hit like the one experienced last Thanksgiving, ratepayers are not prepared to hear that staff have been cut or overtime has been restricted. There have, in fact, been hiring and overtime restrictions, but we have to manage these restrition -- restrictions so that we continue to keep the lights on.

Mr. Thomson testified that to meet the material changes in our operating cost structure, we need to -- we need to examine whether there are things we do that our customers don't really value. That exercise is underway. Contrary to CAC's submission, Manitoba Hydro is controlling its cost -- costs aggressively.

Now, I'm turning to slide 38. And with respect to Wuskwatim, it is correct that capital costs escalated from the estimate of 1 billion in -- in the capital expenditure forecast '03 to an in-service cost of 1.7 --7 billion in CEF12. It's also correct to note that many industry sectors in North America experienced similar unforseen capital cost increases, driven to a large degree by the impact of concurrent massive international investment in infrastructure. This was discussed at transcript page 1,423 and also in Manitoba Hydro Exhibit 91.

It was also discussed by Mr. Warden when he referenced the article 'Sticker Shock' in his testimony in this hearing. That article was filed in a previous GRA, the 2008 GRA, as Exhibit 10.

The concerns regarding the cost impacts of Wuskwatim appeared to be premised on the mistaken assumption that Wuskwatim is not needed for domestic load in 2013. Mr. Cormie was -- corrected this misunderstanding at transcript page 2,339 of the record where he said:

"Had we not built it, we would have been short this year. And subsequent

events, such as the addition of wind
generation, has created surpluses
that have -- have created the
surpluses that are shown. But we
need -- we need Wuskwatim this year
to serve domestic load."

Further in its rebuttal evidence, to demonstrate the need for Wuskwatim -- and here I'm referring to pages 39 to 40 in that rebuttal evidence -- Manitoba Hydro clarified that:

"To respond appropriately to the
question of whether Wuskwatim was in
fact required as a new resource to
serve Manitoba, the removal of
Wuskwatim, as well as wind, from the
supply/demand table is required prior
to conducting such analysis.
Removing these generation resources
results in a persistent shortfall
starting at 2011/'12, as shown in the
table provided in Manitoba Hydro's
response to MIPUG/Manitoba Hydro
Second Round 16B. These shortfalls
would be filled by the Wuskwatim
Generating Station."

CAC's argument that Wuskwatim is somehow a burden on ratepayers fails to recognize that Wuskwatim was constructed to serve the demand generated by those very same ratepayers. It is of note that Mr. Bowman did not agree with Mr. Williams's assessment of Wuskwatim. And here he said, and I'm quoting:

"I'm not here even saying that it was a bad decision to proceed with it. I think -- [or] I -- I think, given the information at the time, people had a -- a sensible reasoning that led to make them the -- the -- to make the decisions. And, actually, in hindsight I think you'd have to do some very different analysis than has been done to -- to come to any other conclusion."

And that's at transcript page 5,618. Mr. Bowman went on to say at transcript page 5,619:

"Just to go back to where I was suggesting. That doesn't mean Wuskwatim was a bad decision to proceed with, because it -- it has provided some other benefits, even to date, that -- that can't be ignored.

> And that -- that would be -- need to be considered if you were to seriously do with -- without analysis."

Anything constructed in 2010, is going to have a higher unit cost than something built in the '60s or '70s. But Manitoba Hydro's mandate is to serve the load, and Wuskwatim facilitates that purpose. As acknowledged by Mr. Bowman, the decision to proceed with Wuskwatim project was based on the best available information at the time the decision was made, after having received all necessary regulatory and environmental approvals. As provided in Manitoba Hydro's response to PUB/Manitoba Hydro Second Round 23B, at the time, the Wuskwatim project was considered to be a viable, economic alternative by the Clean Environment Commission and the Manitoba Hydro Electric Board.

Now to slide 39. As indicated in Manitoba Hydro Exhibit 91, which is Tab 12 in the book of documents, Manitoba Hydro undertook regular process reviews during the pre-construction and construction phases of the Wuskwatim project. The outcomes of these reviews were used to adapt the planning and construction processes for the Wuskwatim project to control project scope, schedule, and budget.

The process reviews continue to be applied to the Keeyask and Conowata -- Conawapa projects planning, construction, and cost-estimating processes, to receive the same type of benefits.

Two (2) of the most significant differences from the period in which the last Hydro project was developed -- that is, Limestone -- to the period in which Wuskwatim Generating Station was developed, were the Wuskwa -- were that the Wuskwatim project is the first project which Manitoba Hydro has engaged in a partnership framework, and the -- and that there has been a significant incr -- significant increase in the degree of rigour required environmentally, as compared to the past. Both the Canadian Environmental Assessment Act and the Environment Act of Manitoba came into existence after the Limestone Generating Station.

A related effect was, as this was new legislation, there was no experience by the federal and provincial regulators in Manitoba, which added another dimension to th scope and scheduling. Experience gained from the pre-construction and construction phases of the Wuskwatim project are outlined in Manitoba Hydro Exhibit 91. This experience is being implemented in the Keeyask and Conawapa projects.

Lessons learned are going to affect the scope, schedule, and budgets of those projects. We provided seven (7) examples of the lessons learned:

The cost -- 1. The cost of doing business in today's business and regulatory environment have increased significantly due to the requirement to have available more engineering and environmental information earlier in the pre-construction process in order to support process and informational needs for both the partnership framework and the regulatory requirements.

2. Considerable time is required with regulators and affected communities to ensure the project scope is well drafted, understood, and agreed by all the relevant parties. Early inputs from these stakeholders will assist in defining and maintaining scope, schedule, and budget for the project.

3. Preparation and endorsement of agreements to define development arrangements and adverse effects are time consuming and difficult to schedule, taking much longer than anticipated. Timing needs to be managed carefully, with engineering, regulatory, and compur -- and procurement processes.

4. Moving supporting infrastructure

design and construction activities such as those for access roads and camps out of the generation project and into separate earlier projects helps protect an in-service date and reduces construction relay -- delay risk.

5. New approaches to contract frameworks, for example, tarbet -- target price contracts approve alignment with prevailing market conditions and help to manage risks associated with certain aspects of the major project; attract contractor interest and provide incentives for the contractor performance.

6. Market research on craft labour and heavy construction improves the recruitment and retention of craft labour workers to major northern project sites and allows for customizing contracting strategies for particular work projects -- work packages associated with the projects.

7. The design and construction of camps have evolved significantly to provide craft workers with remote site living conditions that are on par with those of other major proje -- project sites across Canada, improving craft labour recruitment, retention and productivity.

Contrary to CAC's assertion and final

argument that project capital cost estimate changes should align with the North American economic downturn, it is clear from Manitoba Hydro Exhibit 91 that project cost increase drivers relate to the global demand for commodities and labour due to significant worldwide infrastructure investment.

The recent updates to the Keeyask and Conawapa total project costs are the results of re-estimates that incorporate experiences from the Wuskwatim project. This includes updates to labour, material, and equipment rates, as well as updates to the assumed labour productivity.

Mr. Bowman acknowledged on page 5,683 of the transcript the benefits of embarking on the construction of Wuskwatim after a twenty (20) year hiatus following Limestone. And here I'm quoting.

"And, as Manitoba Hydro said, we can sit here today and say Wuskwatim's a $1.6 billion project, which sounds pretty big, but it's only 200 megawatts. And I would not fault Manitoba Hydro for saying, Before we get to the big stuff, having not one -- done one of these for almost -- for twenty (20) years -- or -- or not set off on building a project for twenty (20) years and the environment is changing, let's take one that got a lower risk because it's a much smaller one and let's learn our way to do the big projects.

And I -- I take with some sincerity their -- their concerns about having learned a lot from Wuskwatim and that there will be ver -- and that will be very beneficial for Conawapa and Keeyask."

CAC's argument that Manitoba Hydro should somehow be penalized in the form of lower rate increases for having proceeded with Wuskwatim and not having foreseen the worldwide economic downturn is flawed both in its premise and its result.

Wuskwatim is needed for domestic purposes in 2013. And no evidence has been presented suggesting a better alternative was ignored. Wuskwatim has been built. It has been placed in service, and it's generating power for the benefit of Manitobans.

As such, it's fair that the cost be included in Manitoba Hydro's revenue requirement and included in rates. It's not fair to defer these costs to future ratepayers.

And now to slide 40. One (1) of the issues that arose during the course of the hearing and was addressed by CAC in its argument was the appropriate treatment of the accumulated depreciation variance that -- that was calculated as part of Mr. Kennedy's depreciation study.

This variance was inappropriately -- inappropriately described as a refund during the hearing. And Manitoba Hydro would like to ensure that its position is clear on this point.

By its nature, depreciation is an accounting estimate which is subject to periodic revision as calculated as part of the Corporation's depreciation studies based on the best information that is available at the time.

Given the very long lives of Manitoba Hydro's property, plant, and equipment assets, positive and negative variances will build up in accumulated depreciation over time. These variances are incorporated on a go-forward basis by way of new depreciation rates each time a depreciation study is performed.

Typically, the studies are performed every five (5) years to assess the requirement for a change in depreciation rates based on updated retirement history and technological or operational changes to those components since the last study.

Changes in assumptions and service lives are not to be considered errors that should be collected or refund to prior customers as the information supporting the latest assumptions did not exist at the time of the previous studies.

Such changes are supported by new information that is to be dealt with on a prospective basis through the calculation of a revised depreciation rate, the purpose of which is to ensure that the remaining undepreciated capital cost of an asset is recovered over its expected remaining service life.

On page 5,275 of the transcript, Mr. Bowman agreed with Manitoba Hydro's assessment and said that the accumulated depreciation variance is not something to be refun -- refunded as he states that, quote:

> "I've been quite clear that I don't sit here saying a depreciation surplus is a refundable balance or is something that should be credited back to anybody."

End quote.

In Mr. Bowman's pre-filed testimony -- and here I'm referring to page 4-13, and oral evidence on behalf of MIPUG at transcript pages 5,631 through 5,632, Mr. Bowman accepted the proposed treatment of the accumulated depreciation variance as recommended by Hydro.

And if we turn the page, the 594 million variance that has accumulated over a long period of time using depreciation rates that were based on previous studies, it -- it's accumulated over a long period of time using those depreciation rates.

On pages 3,335 to 3,336 of the transcript, Mr. Kennedy clarifies that the variance is nothing more than a theoretical calculation and/or an interim step of a two (2) part calculation. To paraphrase Mr. Kennedy, step 1, which is typical for any company that has just updated his depreciation rate, is to determine an updated depreciation rate by taking the present day net book value of an asset and amortize that net -- that net book value over the remaining life of the asset.

In this case, Manitoba Hydro has taken a second step of presenting what the net book -- what the netbook value would have looked like had we applied the new depreciation rates since the acquisition of the asset. This is how the variance is determined. The new depreciation rate will effectively amortize the variance over the remaining service life of the asset, and at the end of the day, you will derive the same annual depreciation rate or expense as you had performed in step 1.

On pages 337 -- 3,337 through 3,339 of the transcript, Mr. Kennedy provides an example that explains the two (2) step process, and Manitoba Hydro would encourage the Board and any interest -- interested parties to review this example to assist with their understanding of what the variance represents.

Notably, this perspective approach is the recommended accounting treatment by the Canadian and International accounting standards in preparing financial statements where the goal is to present fairly the financial position of an entity.

And now it's slide 42. Consistent with Manitoba Hydro's systematic and rational approach to rate making, Manitoba Hydro prefers an approach to handling the variance that recognizes the long-term nature of the assets and the fact that depreciation estimates will continue to change over time as new information becomes available in the future. In this depreciation study, as in the past, the approach has been to amortize positive or negative variances over the remaining life of the accounts to which they pertain, which is consistent with the objective of maintaining rate stability for customers.

CAC alludes to a shorter amortization period than recommended by Manitoba Hydro but offers no specific recommendation. If the net variance in accumulated depreciation was to be amortized over a shorter period of time, revenue requirements could be reduced during the time frame of the amortization. But a significant increase in revenue requirement would be experienced when the net surplus was depleted. Such a treatment would contribute to rate volatility for customers which would be compounded if circumstances changed such that it becomes necessary to shorten asset lives in the future depreciation study.

Manitoba Hydro notes that as demonstrated in figure 1 on page 9 of Manitoba Hydro's rebuttal evidence, approxil -- approximately 60 percent of the amortization of this variance will be completed after twenty-three (23) years, and the vast majority, 90 percent, of the amortization of the variance is expected to be complete in forty (40) years.

Amortizing the variance over the

remaining life of the accounts to which they pertain is consistent with the past regulatory practice, recognizes the long-term nature of the assets to which it relates, and is consistent with the objective of rate stability for customers.

Very briefly, I'd like to deal with GAC's rate proposals, or Green Action Committee. Manitoba Hydro notes that GAC supports the rate increases sought by the Corporation. GAC acknowledges the increases are just and reasonable. They agree there is need to invest in infrastructure, and they accept that the drop in export prices due to the decline in opportunity export sales has a negative impact on the financial position of the Corporation.

GAC also advocates for a further 1 percent per year for the next three (3) years to add $41 million to the revenue requirement to be used for the purposes of DSM. Ms. Fernandes will deal with that proposal when she addresses DSM matters. That will be later in the argument, but I've asked Ms. Fernandes to deal with Manitoba Hydro's rate programs at this point in the argument.

So I'm going to take a break. You're going to -- you get a break from my voice, and I'm going to ask Mr. -- Ms. Fernandes to address the curtailable rate program, and the other specific rate programs being dealt with in Manitoba Hydro's application.

MS. ODETTE FERNANDES: Thank you. Good morning, Mr. Chairman, Board member Lafond, and Board member Soldier. I will be starting out at slide 44.

Manitoba Hydro's General Rate Application sets out proposed changes to the curtailable rates, terms and conditions, and the most recent status report on the program. The CRP has been in existence since the mid 1990s, providing benefits to both Manitoba Hydro and participating customers.

For Manitoba Hydro, the value is greatest during peak times, as that is when Manitoba Hydro's capacity surplus is most vulnerable. For customers, the benefit comes via the way of a monthly credit regardless of whether curtailable load has been called upon or not. The program to date has been a win/win for both Manitoba Hydro and the customers.

Over the years, the curtailable rate program has undergone several changes, the last being in April 2005. For the Corporation, CRP load serves two (2) general purposes. The first is to minimize disruption to firm load in the event of a contingency or disturbance. The second is to maintain a sufficient level of planning and operating reserves to maintain reliable operation of the bulk electric system and compliance of NERC reliability standards.

Customers wishing to partake in the curtailable rates program must provide a minimum of 5 megawatts of curtailable load. And now I've moved on to slide 4 -- 45.

They currently can select from four (4) different curtailable options -- Option A, Option C, Option R, and Option E -- each of which have different notice period provisions and differences in the number and duration of curtailment.

Pursuant to the terms and conditions per the CRP, customers must curtail their load when requested by Manitoba Hydro. In exchange for doing so, customers receive a monthly credit on their bill. To date, there are only three (3) customers on the program, which accounts for a total contracted curtailable load of 230 megawatts. During the 2011/'12 fiscal year, a total of $5.8 million was credited to these customers on their bills. And that is discussed at Appendix 10.5, page 6, of Manitoba Hydro's application.

I've now moved on to slide 46. Manitoba Hydro is proposing several changes to the curtailable rate program terms and conditions. These are listed in Tab 10 of the application. The most significant changes are: number 1, the elim -- elimination of Option C and CE; number 2, the reduction of the overall subscription cap.

In this revised condition, the current Option R cap of the 100 megawatts would be reduced to 50 megawatts, and the current Option A and C combined cap of 230 megawatts would be reduced to either 180 megawatts for Option A load, assuming that the Option C load converts to Option A, or 150 megawatt reduction for Option A load if Option C load switches to firm service.

And the third major change is a change to the defined peak and off-peak period hours to be consistent with the current MISO definitions.

Now on to slide 47. Mr. Cormie gave evidence detailing the reasons behind these changes at transcript pages 2,466 and then again at 2,470 to 2,477. And he noted that Manitoba Hydro has entered into a contingency reserve sharing arrangement with MISO effective January 1st, 2010, that reduced Manitoba Hydro's requirement for contingency reserves. Therefore, Manitoba Hydro no longer needs as much Option A load.

With respect to the elimination of Option C, this option is rarely used. Therefore, it makes no sense to pay for something that has no value. The one (1) hour notice period to curtail is too long, resulting in Manitoba Hydro seeking another means to deal with contingency.

Further to this evidence, Manitoba Hydro has also clearly outline -- outlined its reasons for reducing current subscription limits to these curtailable rate program load options in its response to Information Requests, which we've inserted into Tab 13 of Manitoba Hydro's book of documents and then again at pages 40 through 43 of its rebuttal evidence, which we've reproduced at Tab 14 of Manitoba Hydro's book of documents.

In essence, the current subscription level of curtailable ro -- curtailable rate program load meets Manitoba Hydro's near-term contingency reserve obligation requirements and its reliability needs. As explained on page 40 of Manitoba Hydro Exhibit 8, recent capacity auction clearing prices have averaged below .1 percent of the marginal value of capacity used to establish CRP rates. Given the current low market prices for capacity, it is simply not affordable for Manitoba Hydro to sign up for additional CRP load.

Mr. Bowman, on behalf of MIPUG, recommends that the PUB reject Manitoba Hydro's proposed cap reductions, with Mr. Bowm -- Bowman providing his reasons in his pre-filed evidence. His arguments for retaining the present caps were to recognize long-term value, as customers have invested facilities to participate in the program; in order to assign value to CRP, based on long-term export market prices; and because of the alleged lack of other industrial rate options offered to Manitoba Hydro -- offered by Manitoba Hydro.

On to slide 48. Manitoba Hydro recognizes the amount of investment customers have provided to participate in the program, which is why the caps are not being reduced lower than the amount of curtailable load currently subscribed. The Option C customer, although subscribed for 31 megawatts of curtailable load, has been operating roughly at or below their prote -- projected firm level for the last two (2) years, thereby providing no load to curtail. But even at that, Manitoba Hydro is allowing the customer the option of switching their curtailable load to Option A.

Although Manitoba Hydro has offered 100

megawatts of Option R load since this option was made available in 2005, only 50 megawatts of Option R load has ever been subscribed. So the reduction of the caps and elimination of Option C should have no impact on existing customers.

Manitoba Hydro recognizes that the reduction in the global subscription cap means that new customers will not be able to avail themselves of the discounts offered by the program. However, expanding participation at this time does not provide benefits to Manitoba Hydro and other ratepayers commensurate with the program discounts.

In their final argument, MIPUG stated:

> "MIPUG is not expecting handouts, but if there can be situations such as curtailable programs which are a win for the company and a win for Hydro, why shouldn't we investigate them?"

And that's found at transcript page 5,995.

MISO's recent voluntary capacity auction prices cleared at an average price below one-tenth (1/10) of a cent per kilowatt month. And this depressed capacity price market represents less than .1 percent of the marginal value of capacity used to establish CRP rates. And that was indicated on page 40 of Manitoba Hydro's rebuttal. Therefore, signing up additional curtailable rate program load at this time would resemble a handout.

As explained in Tab 13 and 14 of Manitoba Hydro's book of documents and by Mr. Cormie on page 2,718 of the transcript, the current market prices for capacity are very, very low. But Manitoba Hydro expects that the value will increase. MIPUG questions why Manitoba Hydro would seek to cap the program to current subscription levels, given the expectation capacity markets will improve.

Quite simply, current market prices are low relative to the discounts offered in the CRP. The quote cited by Mr. Hacault in his final submission, which is from Mr. Cormie at transcript page 2,718, did indicate an expectation that the market would improve but did not suggest it would be immediately or soon. At such time that market conditions improve to a level that can be re-balanced -- that can re-balance the win/win nature of the CRP, Manitoba Hydro could consider increasing the caps to the program.

In addition to its concern with the proposed reduction of the curtailable rate program subscription caps, MIPUG asserts that there are very few rate programs available for industrial load customers. MIPUG is now recommending that the Board direct Manitoba Hydro to investigate other rate options for large industrial customers.

Manitoba Hydro is now and has always been open to discussion with all its industrial customers regarding other approaches that could be taken to find mutual benefits and does not require a directive to do so.

Moving on to slide 49. I would now like to comment briefly on MIPUG Exhibit 11, which compares the industrial rates offered in other jurisdictions to those offered by Manitoba Hydro, noting in particular that the utility Entergy in Louisiana offers an electrochemical energy intensive rate.

This appears to be a load retention rate. Typically, utilities offer this type of rate when they have actual or potential excess capacity and major loads which have serious options to continued service from that utility. In this situation, the utility is better off to accept a reduced rate that recovers at least some of the fixed costs, rather than losing the sale altogether, should a customer relocate or take alternative service.

Such offerings are usually made for a

limited period of time. And this appears to be the case in Louisiana, as the rate has been closed to new customers since 2008 and offered in limited amounts to existing customers, thereby limiting the value of comparison to other utilities.

Unlike Entergy and some other utilities, Manitoba Hydro does not have excess capacity for which it is unable to find a market and, therefore, does not have to discount rates for load retention.

Manitoba Hydro is also very concerned with statements made in MIPUG's argument which suggest that export-energy-related benefits can be realized from having all types of CRP load. This is not factually correct.

As explained on page 2 of Appendix 10.5, Option R curtailable load allows Manitoba Hydro to meet reserve obligations, thereby freeing up hydro generation for market transactions in the opportunity energy and capacity markets.

Option A curtailable loads in -- increases the amount of capacity for sale in the firm export markets but does not influence the dispatch of Manitoba Hydro generation, nor does it free up Manitoba Hydro generation for additional energy sales. Therefore, Option A load is of lesser economic value to

Manitoba Hydro.

No party at the proceeding raised any significant concerns with the proposal to eliminate Option C and CE or the proposed change in the defined hours of the program.

Manitoba Hydro has fully explained its reasons for the requested changes to the CRP. It is open to discussing other possible rate options with large industrial customers, as in the past, with a view to identifying mutually beneficial alternative rate options. Manitoba Hydro is requesting the PUB to endorse the requested modification to the terms and conditions of the curtailable rate program.

I will now move on to the surplus energy program. And that would start at slide 51.

(BRIEF PAUSE)

MS. ODETTE FERNANDES: Manitoba Hydro's application outlines several proposed changes to the SEP terms and conditions at Appendix 10.6 and includes the most recent status report on the program located at Appendix 10.7. The surplus energy program has been in place as a temporary rate offering since 2000, with various sunset dates that have been extended by application of Manitoba Hydro and approval by the PUB from time to time over the years since. This program is made available to qualifying customers who wish to designate their load as interruptible. SEP is of mutual benefit to both Manitoba Hydro and its customers. This revenue-neutral program offers customers choice and access to surplus energy at prices similar to those paid by opportunity export customers.

To obtain the benefits of the program, customers need to have sufficient flexibility in their operations to take advantage of lower price periods. For Manitoba Hydro, the benefit comes from the ability to market excess capacity to domestic customers as similar to opportunity export prices and, in times of excess water availability, to market surplus that would otherwise go unsold.

Moving on to slide 52. The SEP consists of three (3) options. Option 1 is available to industrial loads whose monthly demands is 1000 kVA or greater. Under this option, custer -- customers may only designate 25 percent of their load as interruptible.

Option 2 is available to heating load customers, and Option 3 to customers with intermittent industrial load. Both Options 2 and 3 customers must have an onsite alternate backup energy source to provide power in the event the surplus energy is not available or should they find SEP prices too high.

SEP prices, as determined by Manitoba Hydro power traders, are revised each week for the following Monday to Sunday period and are submitted to the PUB approval. And that is on slide 53.

The rates are set for three (3) pricing periods: peak, shoulder, and off peak, which hours differ from summer season to winter season. Manitoba Hydro's application proposes that the SEP be made a permanent rate offering, that Option 1 customers be allowed to have different reference demand for each of the three (3) pricing periods, and that the requirement for an engineer to seal the weekly SEP rates filed with the PUB be discontinued.

Counsel for the PUB raised a concern over the removal of the engineer's seal on the weekly SEP rates, and this discussion occurred at transcript page 2,504 to 2,512. Manitoba Hydro contends that it is unnecessary and inappropriate to require an engineer to seal the weekly rates filed with the PUB.

As outlined in Manitoba Hydro Exhibit Number 64, the preparation of the SEP rates is not supervide -- supervised by an engineer, nor is the schedule and engineering document. SEP rate schedules are based on near-term project -- projections of power prices which do not involve the practice of engineering. Sealing such a document is considered by Manitoba Hydro engineers to be a contradiction to the Association of Professional Engineers and Geoscientists of the Province of Manitoba's code of ethics.

Intervenors themselves did not express concerns with any of the changes being proposed by Manitoba Hydro with respect to the SEP. Manitoba Hydro takes responsibility for the accuracy and integrity of the SEP rates information, as it does for all information it files with the PUB.

It is Manitoba Hydro's expectation that the weekly SEP rates will continue to be filed under the usual process, with the exclusion of the engineer's seal. And Manitoba Hydro is requesting that the PUB endorse the requested modification to the terms and conditions of the surplus energy program as requested.

Now, moving on to slide 55. I'm moving into the area of diesel rates.

MR. ANTOINE HACAULT: Sorry to interject. I just wanted to note for the record if I leave, it's just because of conflict of scheduling. So I may be leaving, and I'll be back about a quarter to

2:00, because there's something I couldn't move.

THE CHAIRPERSON: Thank you, Mr. Hacault.

(BRIEF PAUSE)

MS. ODETTE FERNANDES: As reviewed in Manitoba High's -- Hydro's application and in oral evidence, Manitoba Hydro serves four (4) remote communities which are far from the provincial grid and which must be served by local diesel generation and distribution systems. The four (4) communities are Shamattawa, Tadoule Lake, Brochet, and Lac Brochet.

The Corporation serves approximately seven hundred and forty (740) customers in these communities, of which approximately 75 percent are residential, 15 percent are general service non-government, and 10 percent are government or First Nation education accounts.

For fiscal year 2012/'13, total sales in these communities were forecast to be 13.5 million kilowatt hours, which is equivalent to about one-sixteenth (1/16) of 1 percent of Manitoba Hydro's sales to all domestic customers.

Now, turning to slide 56. Costs to

serve the diesel communities are much higher than costs to serve customers from the grid, and this is due to the isolation of the communities, the small population served, and the cost of facilities and fuel. For the 2011/'12 year, the total costs, excluding capital costs, to provide service is estimated at 53.5 cents per kilowatt hour. And this was at Appendix 11.1, page 3.

Only government customers, a category which also includes the First Nation education accounts, pay rate intended to recover the full cost of providing them service. For residential and general service non-government customers, the rates charged recover only a small part of the cost to provide that service. This is depicted in the schedules to Appendix 11.1 of the application.

Residential rates for all usage are identical to rates charged to grid customers and, hence, recover only about 12 percent of their cost of service. Residential customers are limited to a 60 amp service, which is sufficient to cover all requirements other than electrical heat, which is not a permitted use.

General service non-government customers do not have service level restrictions but have access to grid rates for only the first 2,000 kilowatt hours per month of usage. Beyond that 2,000 kilowatt hour per month, a significantly higher rate applies, and that's thirty-seven point three (37.3) cents per kilowatt hour.

This rate was used to recover the estimated full variable cost of providing service but since January 2011, it recovers only about two-thirds (2/3) of that cost. Overall rates changed to general service non-government accounts recover about 42 percent of their cost to serve.

Costs not recovered from residential and general service non-government rates are recovered from two (2) sources; either a surcharge applied to the rate for government customers, and Manitoba Hydro, by extension, its ratepayers.

As noted earlier - moving on to slide 57 - grid rates apply to all residential usage, and to general service non-government usage up to the 2,000 kilowatt hours per month. This covers 68 percent of all usage in the diesel communities.

Longstanding practice at Manitoba Hydro, and supported by PUB orders, is that rates for this usage are equivalent to grid rates for the same class of customers, and change whenever grid rates change.

General service non-government usage in excess of 2,000 kilowatt hours per month represent some 16 percent of all usage in the diesel communities. Government and First Nation education accounts for a further 16 percent of total usage. Manitoba Hydro is not proposing any change to these rates for April 1st, 2013.

As noted by Mr. Wiens at transcript page 2,543, Manitoba Hydro's intentions with respect to a further Application for diesel rates will be communicated to the PUB as soon as they are known.

Manitoba Hydro did apply for, and implement effective September 1st, 2012, an increase of 6.5 percent to the rates of -- applying to the general service non-government usage in excess of 2,00 kilowatt hours per month. And now I'm on slide 58.

The 6.5 percent applies to all government usage. The rate increase was approved on an interim basis in Orders 116/'12 and 117/'12. No Intervenor has suggested that these rates should to be approved. Manitoba Hydro acknowledge -- acknowledges that these rates are subsidized by other Manitoba Hydro general consumers to a greater relative extent than any other class of service.

But Manitoba Hydro takes the position

that in the circumstances the rates are fair and reasonable for the following reasons. Number 1, Board Order 148/'11 approved the extension of equivalent to grid rates for all residential used within a 60 amp service limitation.

Number 2, Board Order 134/'10 set the rate for general service non-government usage in excess of 2,000 kilowatt hours per month at thirty-five (35) cents per kilowatt hour, and thereby establish the precedent for recovering less than the cost of service from this usage.

The current -- the current interim rate is 6.5 percent higher, that being thirty-seven point three (37.3) cents per kilowatt hour, and this increase was designed to equal the cumulative increases to grid rates since Order 134/'10 was issued. Manitoba Hydro takes the position that this is a reasonable tradeoff to recognize the intent of Order 134/'10, as well as cost increases since that time.

And finally, Manitoba Hydro argues that the rates are fair and reasonable because the interim approved rate for government customers and First Nation education accounts is two dollars and twenty-seven cents ($2.27) per kilowatt hour, which incorporates the full operating cost of providing service at an amount equal to one dollar and sixty-eight cents ($1.68) per kilowatt hour to subsidize the provision of service to the classes served at grid rates, or otherwise below cost.

This rate does not fully cover the full cost of the subsidies. It does not co -- recover even the same share of subsidies provided for in the indicative rates filed in Appendix 11.1, that would require a unit surcharge of a dollar ninety-five ($1.95), and a full government rate of two dollars and fifty-four cents ($2.54). Nevertheless, by any measure, two dollars and twenty-seven cents ($2.27) is a very high rate, and in the interest of customer sensitivity, Manitoba Hydro asks that no further changes be made to this rate.

This brings me to a truly unique aspect of diesel rates, which you can see at slide 59, where we show a list of the diesel orders implemented on an interim basis since 2004. Manitoba Hydro's application requested that the PUB give final approval to all outstanding interim diesel orders. Yet, until Manitoba Hydro and Canada are in the possession of true copies of the settlement agreement, the condition in the agreements are not final. Hence, there exists a remote possibility the agreement could be unwound.

As noted in response to PUB/Manitoba Hydro Second Round 104B, if all the conditions in the agreement are not met, theoretically it could result in the unwinding of the provisions of the settlement agreement, including return of a significant capital contributions paid. In this unlikely event, Manitoba Hydro would not want rates designed on the basis that capital contributions have been received, to have already been finalized.

The Board has reviewed this matter on a number of occasions over the years, and Intervenors and the parties to the settlement agreement have had an opportunity to comment on the various interim rate proposals in this and other proceedings.

And I'm now on slide 60. Manitoba Hydro is of the view that there is no need for a further process in this matter, and recommends that the PUB approve these eight (8) orders as final, subject to the filing of true copies of the settlement agreement.

Manitoba Hydro notes that in Order 134/10, the Board indicated that it would be helpful to obtain the consents of all parties to the agreement, as well as CAC, in ord -- in seeking an order to confirm all the interim diesel orders. As indicated at transcript page 2,525 of the transcript, there has been some reluctance by the parties to provide such a consent. As Ms. Ramage noted, Canada has shown a general reluctance, although it hasn't refused to sign; CAC would like to see the agreements first; MKO has not responded.

It's Manitoba Hydro's position that the PUB doesn't need anyone's consent to exercise its jurisdiction. Mr. Peters asked, at transcript page 2,526, whether Manitoba Hydro's position was that this hearing is the time for any party to raise any objections or concerns, and failing that, the Board could adjudicate on the issue, to which Ms. Ramage replied, "That's correct."

As we have seen, no party has raised an objection or concern about fil -- finalizing the interim orders. It continues to be Manitoba Hydro's position that there is no need for further process, other than the Board's own delimer -- deliberations, to finalize the interim orders, which Order, Manitoba Hydro requests, be expressly made subject to receipt of the true copies of the settlement agreement.

THE CHAIRPERSON: Before you move on to another topic, I do have a -- I guess something that I would like to address with you.

You will recall when we discussed this

earlier this week, we indicated that we had agreed that, before we accepted a late hour submission from -- from MKO, we would need a letter from them advising us as to what -- what's causing the hold up with respect to the signed agreements.

I just want to clear something up, because the -- the submission that was received from MKO, the late hour submission, made reference to the fact that -- and I quote from this -- this document on page 2:

> "It is MKO's understanding that Manitoba Hydro has been provided with electron -- electronic copies of the agreement as executed in counterpart, and has been advised of the nature of the -- of the administrative matters and the effect of these matters on the final steps in respect of the agreement."

And I just want to clarify that point.

Could you advise this panel of what -- what the issue is? What -- what's the hold up? If you are aware of the -- the nature of the administrative matters, and the effect of those matters?

MS. ODETTE FERNANDES: The only thing

that Manitoba Hydro is aware of is that we understand that there may -- may be some compensation related issues between AANDC and MKO. It has -- it doesn't involve Manitoba Hydro. We don't know the details of that compensation issue, but we don't believe that the administrative matters that are being discussed are related to or arise from the settlement agreement. So, we are at a loss as to why the true copies of the settlement agreement haven't been provided to Manitoba Hydro or this Board.

THE CHAIRPERSON: But you have received copies of the electronic versions of the co -- of the documents, have you?

MS. ODETTE FERNANDES: This goes back to the long history. Mr. Anderson provided electronic PDF copies of the agreement, and then some Board counsel resolutions and inde -- certificates of independent legal advice, however, some of the originals were missing and couldn't be located.

So Mr. Anderson -- the parties discussed it, and Mr. Anderson was to go back and obtain affidavits because the -- the bands in some of these diesel communities have changed. So he -- so he was to go back and get affidavits swearing that the PDF copies that we had were actually copies of the original.

And once he had all that in order we were supposed to receive true copies of all the documents. But I believe we were provided with three (3) copies of affidavits, but we still have not seen one (1) copy of it, which Mr. Anderson indicated he did have, but we haven't seen it yet.

THE CHAIRPERSON: Okay. I notice you were looking at the clock. I guess you're going to undertake another topic. And is it your preference that we stand down now, and then resume after lunch?

MS. ODETTE FERNANDES: We can -- we can stand down. I believe Mrs. Ramage was going to take over from here, so this may be a good --

MR. PATTI RAMAGE: I was going to say this is probably a perfect time to stand down because what we've done is we've -- how we structured the argument was the first half of the argument dealt with all the issues that actually occurred in the test years and that were part of the application.

And the second half of the argument, and we're more than halfway but not much, I'm a little disappointed on how fast we're moving, is dealing with all matters outside DSM and all matters outside of the test year.

So it's a perfect time to have a break

because now we're going to move into matters that we would say, quite frankly, if we had to right now and I got hit by a bus, we're done. You can make your Order, but...

THE CHAIRPERSON: Okay, I think we should -- we should stand down now and resume at one o'clock. Thank you.

--- Upon recessing at 11:55 a.m.

--- Upon resuming at 1:02 p.m.

THE CHAIRPERSON: I believe we're to resume the proceedings, so back to you.

MS. PATTI RAMAGE: Okay. Thank you. Just two (2) things before I get back into -- into the argument, in -- in terms of our scheduled order. When -- just before the break, you had asked Ms. Fernandes some questions about the diesel. And I thought -- one (1) point, and I'm not really sure -- I'm not entirely clear if it's important or not, but I thought I'd just put it on the record that when Ms. Fernandes said about our understanding of what's going on the diesel, it should be clear, we gain -- we've gained our understanding from Canada. We have no -- MKO has not communicated with us at all. So we are hearing it secondhand, and we don't know what MKO thinks we know, if that...

MR. RAYMOND LAFOND: On -- on this topic you said you had digital copies. I presume it's signed digital copies, initials on every page, et cetera?

MS. PATTI RAMAGE: Yes, and what the -- what the concern is, is part of the settlement agreement itself, one (1) of the terms is that we'll ultimately have a -- originally it was an -- each party would have an original copy for their records, and that would ultimately be filed with the PUB, and the rate of ord -- orders would be approved as final.

So there were two (2) conditions outstanding: rate approvals and that original copy. When -- when the copies were lost, we had at least been faxed some copies, so we had that. And when the parties got together and looked, we wanted true copies. That's where the affidavit came up.

So it's a condition now of Canada signing off on their -- their capital contributions that they get something that confirms that the signatures on there are the people who -- who were actually in the room signing it. So they've just asked for a Band council member, for example, to agree that,

That was the Band council resolution that I signed, as opposed to having to go back and get a new Band council resolution from the new Bound -- Band council.

So that's what we are waiting for, is the -- the affidavits. And I think we have three (3) of four (4), if -- Ms. Fernandes has been the one whose been following up on that. And so in order to get Canada's release on that condition, we need that confirmation so that they can meet their financial requirements -- or fin -- their reporting requirements, whatever those are.

That's our understanding. So to get them to sign off that condition we need that, and then we need it filed with the PUB so that that second condition can also come off. It's been since 2004, so I can -- unfortunately, Mr. Warden thought he would see this agreement before he retired, so we may have failed him.

The other point, Mr. Lafond, in the question that you asked this morning, we were asked to clarify the bullet on page 31 of Manitoba Hydro's -- the outline of that final argument. And if I flip to that bullet -- just the confusing bullet -- and we apologize for that -- is that there are also financial risks associated with increased level of leverage and higher rate increases forecast in IFF12.

And I think we've contributed to the -- the confusion here great -- well, it is. We -- it is our fault, and we apologize for that. The intent of the bullet is to communicate two (2) separate ideas, and I guess the way we've structured it, it didn't do that very well.

The reference to leveraging refers to the increasing level of debt in the IFF. And, of course, as you are aware, increased leverage would mean increased financial risk.

The second -- second part of the bullet was intended to communicate an entirely different idea, and that's -- it recognized that when looking at the IFF, you're looking at the projected financial position of the Manitoba Hy -- of Manitoba Hydro, assuming that Manitoba Hydro got approval of each of the indicative 3.95 percent rate increases in each of the years going forward.

THE CHAIRPERSON: So we're talking regulatory risk.

MS. PATTI RAMAGE: Right. That's a --

THE CHAIRPERSON: Okay.

MS. PATTI RAMAGE: -- an -- entirely separate. And unfortunately, in our -- in our quest to try to be efficient and perhaps shorten this down a little bit, we should have had those as two (2) separate bullets.

So our point was these increases are higher than anything we've seen in previous IFFs and, therefore, the risk associated with not getting the approvals is -- is greater. And, of course, the point that you made, Mr. Lafond, with respect to the level of borrowing results in greater risk is -- is true, and that speaks to the first point. But I think it was just the confusion of putting those two (2) together.

Mr. Cathcart, I think, asked Ms. Fernandes at the break also about getting a written copy of -- of what we're dealing with. That's not a problem. We have to clean it up a little bit, because we have little notes to ourselves. I can also war -- for example, the numbering system in here simply doesn't work because I've cut and paste so many things along the way, if you tried to follow the numbering system. But we can get back to the office, clean that up, and get that to you, if that's of assistance.

THE CHAIRPERSON: That would be appreciated. An electronic version would be even better, okay?

MS. PATTI RAMAGE: Perfect. Not a

problem. Ms. Fernandes is -- is in charge of all electronic versions, so it's very easy for me to say, "not a problem." I remember Mr. Lafond --

MR. RAYMOND LAFOND: You're -- you're showing your age.

MS. PATTI RAMAGE: Yeah. That's exactly what I was thinking of, an early comment in the hearing when you said that you used to tell people, That shouldn't be a problem, it's easy.

So we're now onto that second half of the presentation, and that's dealing with revenue requirement issues associated with 2014, '15, and beyond. And we should be at slide 62, by my count.

The original application was based on IFF11-2, which assumed that Manitoba Hydro would transition to IFRS in the 2013/'14 fiscal year, or the second test year of the application currently before the Board. At the time of the filing of the original application, Manitoba Hydro was forecasting that, upon the adoption of IFRS, there would be a retained earnings writeoff of approximately 276 million related to electric operations and that the impact on net income in the 2013/'14 test year would be a reduction of approximately $11 million.

On September 19th, 2012, the Accounting

Standards Board of Canada extended the optional transmission -- transition date to IFRS for rate-regulated en -- entities by an additional year, to January 20 -- January 1st, 2014, based on the fact that the International Accounting Standards Board had committed to reinstate its project on rate-regulated activities.

As a result of the additional one (1) year deferral of IFRS for rate-regulated entities, Manitoba Hydro had forecast that it would adopt IFRS in the 2014/'15 fiscal year in IFF12 and that it would defer adoption on a -- on a number of accounting policy changes that were designed to be IFR -- IFRS compliant, such as the writeoff of rate-regulated assets, further reductions to overhead capitalized, removal of asset retirement costs from depreciation rates, and the change to the Equal Life Group depreciation method for financial reporting purposes. As a result, there are no IFRS impacts contained in the test years as presented in IFF12.

While IA -- IASB had recently reinitiated its rate-regulated activities project at the time of the preparation of IFF12, the project had -- had not yet reached a stage where any forecast assumption, other than derecognition of such assets, would be considered reasonable. As such, IFF12 assumed a retained earnings writeoff of approximately 257 million upon transition to IFRS in 2014/'15 for electric operations, primarily related to the derecognition of rate-regulated assets.

The forecast net income impact for 2014/'15 of the transition to IFRS was an increase of $5 million for electric operations. Here I'm referring to page 23 of the rebuttal evidence.

Over to slide 63. Mr. Rainkie provided updates to the PUB on the status of the IASB's rate-regulated activities project a number of times during the course of the hearing, indicating that there was a significant potential that the IASB could approve an interim standard during 2013 that would continue to allow for the recognition of rate-regulated assets and liabilities for those countries that are first-time adopters of IFRS.

Mr. Rainkie did caution the PUB that such an interim standard would be subject to the final approval of the IASB at the appropriate due process, and, as such, there was some potential that it may not be approved. In addition, after the issuance of an interim standard, the IASB indicated that its plan was to continue with rate-regulated activities project towards the development of a final standard for release in 2016.

The IASB did note that an interim standard would be approved without prejuce -- prejudice to the outcome of the final standard. And, as such, there is still some potential that the ultimate resolution could be that rate-regulated assets and liabilities are not permitted under IFRS.

Subsequent to the end of the evidentiary portion of the hearing, the IASB decided that it would proceed with the issuance of an exposure draft in March of 2013 that would propose that an interim rate-regulated standard be finalized for first-time adopters of IFRS by December of 2013.

As a result of that decision, the Canadian Accounting Standards Board decided on February 13th, 2013, that it would extend the existing deferral of the IFRS changeover date for Canadian rate-regulated entities by an additional year, to January 1st of 2015. In granting the further extension, the Canadian Accounting Standards Board noted that it wanted to give the first-time adopters of the IFRS adequate to prepare comparative information based on the requirements of the new interim standard.

As indicated in Manitoba Hydro's letter

of February 22nd, this development is very recent, and Manitoba Hydro will continue to monitor the situation, but the Corporation expects to adopt the further deferral and would, as a result, transition to IFRS during its 2015/'16 fiscal year.

And then to slide 64. Despite the fact that prior to the commencement of the hearing the implementation of IFRS was already deferred beyond the 2013/'14 test year, there was still a significant amount of discussion related to the acceptability of IFRS for rate-setting purposes during the hearing.

Manitoba Hydro wishes to put these discussions in context for the PUB and ensure that its position is understood by all parties to the hearing.

There's been a suggestion by Intervenors that Manitoba Hydro has not pursued or identified any options in the current filing to mitigate the rate impacts of the accounting changes that have been made to date or are expected on transition to IFRS. This suggestion is not correct. Manitoba Hydro has been making -- has been making any changes that are necessary and permitted under Canadian GAAP gradually over the past number of years in an effort to transition them into customer rates and moderate the impact on customers.

Manitoba Hydro has deferred the implementation of IFRS for four (4) successive years, as permitted by the Canadian Accounting Standards Board, and continues to monitor the developments of the IASB with respect to rate-regulated accounting to ensure that when it does transition to IFRS, it is with the lowest possible impacts to customers.

There was a significant discussion surrounding the fact that a number of other Canadian utilities had adopted US GAAP for financial reporting and rate-setting purposes and that BC Hydro had adopted a modified IFRS approach that included the use of rate-regulated accounting as directed by the BC Government.

In response, Manitoba Hydro had provided evidence that its financial reporting options are limited, given that Public Sector Accounting Board standards require that government-related businesses, such as Manitoba Hydro, adopt IFRS fi -- for financial reporting purposes. US GAAP is not an allowable option for Manitoba Hydro. And even if it was, Mr. Rainkie testified at transcript page 4,722 that it would not be a workable solution for Manitoba Hydro, given its foreign exchange cashflow hedges. It would not be allowed under US GAAP.

Logically, even if Manitoba Hydro could

convert to US GAAP, its financial statements would need to be converted back to IFRS prior to the consolidation with the Province of Manitoba so that the province can receive an unqualified audit opinion. That would create yet another set of financial statements for Manitoba Hydro stakeholders to understand.

In addition, the majority of Canadian utilities that have migrated to US GAAP will be required to transition to IFRS after January 1st, 2015, when their three (3) years -- three (3) year exemptions expire.

The recent extension of the transition date to IFR -- IFRS for rate-regulated entities to January 1st, 2015, will coincide with the expiry date of the US GAAP exem -- exemption granted by provincial securities regulators so as to provide a uniform date for all Canadian utilities to transfer -- transition to IFRS.

Here I'm going slide 65.

THE CHAIRPERSON: Can I ask you a question? Just in relation to the comment you made about having to transition again back to reconcile to IFRS for the province. Now, you would -- you'd be generating your financial statements based on GAAP -- pardon me, based on IFRS, would be for the purposes of this Board? Did I misunderstand you? The purpose of this Board, you'd be using US GAAP?

And then why would you need to then convert that back to the province if you've already established your statements based on IFRS?

MS. PATTI RAMAGE: I -- I think the assumption was we would be generating for US GAAP if we took a -- if we -- if we somehow got an exemption, like in BC.

THE CHAIRPERSON: Oh, I see. Okay.

MS. PATTI RAMAGE: That -- we did US GAAP, we're still going to have to go back for the province.

THE CHAIRPERSON: Okay.

MS. PATTI RAMAGE: One has to consider the motivation behind Canadian utilities to convert to US GAAP as opposed to IFRS. The most prominent reason was avoidance by the shareholders -- that is, the provincial governments -- of significant one (1) time writeoffs to retained earnings for significantly large rate-regulated asset balances, some of which are in excess of $1 billion, depending on the utility.

Evidence has been provided during the hearing that BC Hydro essentially has no choice but to move to a modified IFRS approach, giving the mag --

given the magnitude of its rate-regulated assets, $2.2 billion, and that the BC audit -- Auditor General has expressed concerns over the ever-growing rate regulated asset balances of BC Hydro, and the move to -- and the move to modified IFRS, which could nega -- negatively impact the audit opinion of the Province of BC.

In addition to the one (1) time negative financial impacts to retained earnings of the transition to IFRS, many utilities have cited the move to US GAAP will present it -- will prevent them from having to incur the additional administrative costs and stakeholder confusion associated with maintaining separate financial statements for financial reporting and rate setting; that is, the maintaining of two (2) sets of books.

In general, utilities are very concerned with the additional administration around -- around a requirement, for example, to recognize overhead on capital assets differently for financial reporting and rate-setting purposes. Given the enormous volume of capital activities conducted in a given year, the administrative burden and costs would be substantial, and the administrative -- administration around supporting such schedules would likely grow over time as the balances accumulate in future periods.

There was an exchange between yourself, Mr. Warden, and Mr. Rainkie at pages 5,081 to -- through 5,084 of the transcript, Mr. Chairman. And -- and that exchange dealt with how the PUB would respond to questions from ratepayers that Manitoba Hydro had not pursued measures adopted in other Canadian jurisdictions. It might be helpful for the PUB to review this exchange in its deliberations.

In summary, Mr. Warden and Mr. Rainkie point out that Manitoba Hydro has not had to pursue the measures adopted in other jurisdictions because the one (1) time adjustment to retained earnings for Manitoba Hydro are quite manageable, as are the future net income impacts, such -- such that upon transition to IFRS, no rate increases are required in the short term.

Manitoba Hydro also points out that they have taken measures, in terms of adopting the optional transition date deferrals, as provided by the Canadian Accounting Standards Board and have avoided the move to US GAAP, so as to avoid negative impacts on our US hedge accounting practices.

The most important factors, in terms of the use of IFRS by Manitoba Hydro for rate-setting purposes, are the limited impacts on the Corporation of the transition to IFRS and the use of the cost-of-service rate-setting approach in Manitoba.

And I move into slide 66. As demonstrated in Manitoba Hydro Exhibit 116, and that -- and that would be Tab 15 in our book of documents, the impact on IFRS on electric net -- net income is minimal, less than $5 million in any year in the next ten (10) years. And that's on page 2 of that exhibit.

It won't affect the required electric rate increases in the future. Unlike some other Canadian utilities with substantial one (1) time adjustments to retained earnings, Manitoba Hydro is fortunate to be in a financial position that enables it to absorb the one (1) time adjustments while adopting accounting changes that will not require a corresponding increase in customer rates.

While the impact on retained earnings in the year of transition would be more significant if rate regulated accounting is not permitted, this could be readily accommodated within the cost-of-service rate-setting methodology without the need for near-term compensating rate increases.

With the significant potential for an interim and final standard that allows for rate regulated accounting, this impact may no longer be a factor at all. When asked by the PUB Chair at page

5,061 of the transcript why Manitoba Hydro could use IFRS for rate-setting purposes when other Canadian facilities had pursued other options, Mr. Warden simply explained, and I quote, "Because we can."

Mr. Warden went on to explain that the impacts of transition to IFRS on Manitoba Hydro ratepayers would be minimal. Overall, Manitoba Hydro has demonstrated that the transition to IFRS should not trigger the requirement for a second set of regulatory financial statements, or alternate sets of calculations to assess rate requirements as has been suggested by the MIPUG witness, Mr. Bowman.

As Mr. Rainkie stated at -- on page 2,025 of the transcript, and I'm quoting:

"I think we're looking at all these changes on a perspective basis trying to manage the impact with the customers through careful selection of accounting policies that also work for rate-setting purposes."

It is not necessary to resort to a separate set of regulatory financial statements, or alternate rate calculations under a cost of service rate-setting methodology that is used in the electric rates in Manitoba -- in -- in setting rate -- electric rates.

Unlike rate-based rate of return that is used to set rates in other jurisdictions, the cost-of-service approach used in Manitoba does not determine rates based strictly on changes in costs and an established capital structure in return on equity.

Rather the cost-of-service methodology, coupled with Manitoba Hydro's approach of implementing regular and reasonable rate increases, has the flexibility to recognize changes in costs and levels of retained earn -- and levels of retained earnings, and transition these changes into rates gradually over time, while at the same time ensuring the maintenance of an adequate financial structure over the long term.

This approach serves to protect customers from sudden or large rate increases, and makes a separate set of regul -- of financial statements unnecessary.

Now we're at slide 67. Another one of the benefits of the cost-of-service rate-setting methodology approach employed by Manitoba Hydro is the PUB uses the same set of general purpose financial statements and information to set rates as the Corporation, its Board, and other external users of the statements, for example, credit rating agencies.

This reduces the potential confusion associ -- associated with different users looking at multiple sets of finical information to make decisions, evaluate financial performance, and assess rate requirements. It also improves the transparency of the rate-setting process by aligning the basis used to set rates, and report results.

The use of audited financial information in the rate-setting process also improves the reliability of the information. These principles were outlined by Mr. Rainkie at page 4,710 of the transcript.

In addition, there are significant administrative costs associated with reconciling between the different sets of financial information, and maintaining duplicate transactional accounting that would be necessary to produce reliable and complete regulatory reporting.

This would simply add to the regulatory compliance cost that customers ultimately must bear without any additional benefit to those customers. Interestingly enough when Mr. Bowman was challenged, at page 5,526 of the transcript, to offer examples of a set of -- examples of a second set of regulatory books, he could not cite any examples other than removing the costs of non-regulated subsidiaries, which Manitoba Hydro already considers, and the calculation of rate base which is not applicable to Manitoba Hydro electric operations.

In Mr. Bowman's words, at transcript 5529:

"Well, the phrase 'two (2) sets of books' is thrown around imprecisely in the regulatory world. I'm not aware of any utility anywhere that actually literally has two (2) sets of books or runs two (2) ledgers or has two (2) accounting departments or anything of that sort."

Mr. Bowman makes reference to reconciling schedules throughout his testimony to track the differences between the results reported for ni -- for financial reporting and the results reported for rate-setting purposes.

Mr. Hacault provided his lawyer's perspective that this was a simple matter of reconciling a few items. On the surface, reconciling schedules would appear to require less effort and less costs than producing a full set of -- second set of financial statements. But the professional accountants at Manitoba Hydro who were charged with the responsibility for the production of the Corporation's financial statements have an entirely different perspective based on their years of experience dealing with Manitoba Hydro's finances. There is no simple magic pen.

The additional effort is not so much in preparing the statements and schedules but, rather, in the development of the underlying systems and processes to record transactions separately so that the results are available for those schedules.

In a situation such as overhead costs, Manitoba Hydro incurs thousands of capital transactions annually. And should there be a requirement to capture those transactions separately for rate-setting purposes, the costs associated with the system and administrative process-related changes would be significant. As indicated by Mr. Rainkie, Manitoba Hydro's finances are complex, and the provision of rel -- reliable information is no simple matter.

Now, I'm turning to slide 68. Not withstanding the advantages of US -- of using IFRS for both financial reporting and rate-setting purposes under the cost-of-service methodology, Manitoba Hydro believes it is premature for the PUB to make any determinations about the implementation of IFRS for rate setting in its order. This is due to the deferrals of IFRS and the current uncertainty with respect to the exact requirements of a potential interim standard on rate-regulated accounting and the continuation of rate-regulated accounting in the long term.

Manitoba Hydro will continue to monitor the development of the -- of an interim standard on rate-regulated accounting and the status of the longer-term IASB rate-regulated activities project and will adjust its accounting policies and financial forecasts accordingly.

Manitoba Hydro will also provide updates and recommendations to the PUB with respect to the implementation of IFRS for rate-setting purposes at the appropriate time, which is currently expected to be in conjunction with the General Rate Application respecting the 2014/'15 and 2015/'16 test years to be filed in the late fall of 2013 and which will be based on IFF13.

Now, we're at slide 69. Mr. Bowman attempted to challenge Manitoba Hydro's assertion that the income statement impacts of IFRS were minimal on the grounds that there's been no mistaken information -

- there has been mistaken information and interpretations that need to be reviewed.

In particular, Mr. Bowman views that some of the accounting changes implemented under Canadian GAAP are more appropriately classified as IFRS-related changes and that some of the proposed accounting changes upon transition to IF -- IFRS are not necessary or are understated as a result of missing information.

The areas of concern, as addressed by Mr. Bowman's testimony, include: reductions in overhead capitalize; the removal of net salvage from depreciation rates; reductions in DSM spending; and the move to the Equal Life Group method of depreciation.

I've already discussed the reasons for changing from -- I've discussed Manitoba Hydro's reasoning for changing its overhead capitalization practices. They are acceptable under Canadian GAAP and are intended to make Manitoba Hydro's practices consistent with other Canadian electric utilities. They are also changes the PUB encouraged irrespective of IFRS.

Mr. Bowman's suggestion that the removal of net salvage from depreciation rates should be classified as a Canadian GAAP change is inconsistent with Manitoba Hydro's clear intention to continue to include net salvage in depreciation rates until IFRS is implemented.

With respect to Manitoba Hydro's treatment of DSM, Manitoba Hydro notes that the current practice under Canadian GAAP is to defer and amortize DSM expenditures. Under IFRS with no ra -- assuming no rate-regulated accounting, DSM expenditures will be expensed as incurred.

The impact of this scenario is clearly an IFRS change. The fact that DSM expenditures are projected to decrease in IFF12 does not tur -- serve to change the fact that those DSM expenses will be treated differently under IFRS.

I note that if rate-regulated accounting continues under IFRS, this won't be an issue for Mr. Bowman as the accounting treatment will not change. This perhaps illustrates why it's prudent to wait until the IASB issues its interim standard on rate-regulated accounting before we make any major decisions on how to treat IFRS for rate-setting purposes.

Mr. Bowman also raised a concern regarding the impacts of ELG in an IFRS construct. And if we could turn to slides -- on the slide number 70. As I mentioned previously, the new depreciation study involved an assessment of IFRS compliant depreciation practices and methodologies.

And as part of the second phase of the implementation of the new study, Manitoba Hydro plans to make a change in the depreciation methodology to the Equal Life Group method upon adoption of IFRS, which again is now deferred to '15/'16.

Before jumping into this topic, I want to address the comments made regarding the statutory framework of Manitoba Hydro and the qualifications of Mr. Kennedy because these two (2) matters go to the purpose of presenting this informat -- presenting the PUB with a depreciation study and the weight to be given to the evidence presented.

At the outset of Mr. Hacault's submission on behalf of MIPUG, he attempted to articulate the statutory framework for the setting of rates for Manitoba Hydro. In doing this, Mr. Hacault has argued that a number of sections -- sections which appear in part 2 of the PUB Act have application to Manitoba Hydro, include -- including provisions requiring the PUB fix just and reasonable rates and requiring the PUB to fix rates of depreciation.

This -- the application of these -- these sections simply don't apply to Manitoba Hydro.

To be clear, only part 1 of the PUB Act dealing with the conduct of a hearing has application to the Corporation.

Manitoba Hydro's rates for service are regulated pursuant to the Crown corporation's Public Review and Accountability Act. I'll refer to it as the Accountability Act. I don't think it necessary to review the sections of the Accountability Act. I'm confident the Board is quite familiar with them.

Also though, because my concern isn't with MIPUG's interpretation of that legislation, rather, Manitoba Hydro takes issue with the suggestion that the PUB's powers or duties with respect to its review of rates under the Accountability Act are somehow modified or expanded by provisions in the PUB Act. And in that regard, I direct your attention to section 2(5) of the PUB Act.

And I'm going to try to parse this down a little bit, but 2(5) says:

"Subject to part 4 of the Crown Corporation's Public Review and Accountability Act and except for the purposes of conducting a public hearing in respect of an application made to the Board under subsection

38(2) or 50(4) of the Manitoba Hydro
Act, this Act, other than subsection
83(4) and the regulations under that
subje -- under that subsection, this
Act does not apply to Manitoba Hydro,
and the Board has no jurisdiction or
authority over Manitoba Hydro."

So Part 4 of the crow -- of the Accountability Act creates the jurisdiction except for the purposes of conducting a public hearing and, otherwise, the Board has no jurisdiction over Manitoba Hydro.

Port -- Part 4 of the Accountability Act expressly limits the PUB's jurisdiction with respect to the Corporation to the fixing of rates for service, being the price charged by the Corporation with respect to the provision of power.

The provisions of the PUB Act dealing with the conduct of the hearing are found in their entirety in Part 1 of the PUB Act. Now, Manitoba Hydro, just to be clear, doesn't take issue with the notion that a matter of -- as a matter of practice its rates ought to be just and reasonable, as suggested by Mr. Hacault.

However, the term itself doesn't appear

anywhere in the Accountability Act. The concept has its roots in English common law. And the Manitoba Court of Appeal has certainly repeatedly used this terminology when describing the intent of the legislature and act -- enacting Manitoba Hydro's statutory framework.

But the reason we want to be careful to distinguish where that just and reasonable standard comes from is because of where it takes you to next. In this case, Mr. Hacault likely takes you to section 77 of the PUB Act as the basis for just and reasonable, which in itself might seem fairly innocuous, except in the next breath he then takes us to the next section of the Act, Section 78, and suggests that the PUB is also required to fix depreciation rates pursuant to, in particular, Section 78(2).

This Board has never fixed Manitoba Hydro's depreciation rates, nor is it authorized to do so. Section 78(2) is in Part 2 of the PUB Act, and that's the same section that provides the Board with all of its usual powers, powers such as franchise approval and general supervisory powers. Powers that we've all accepted don't apply to Manitoba Hydro.

So as indicated in the Manitoba Court -- by the Manitoba Court of Appeal, the PUB's jurisdiction with respect to Manitoba Hydro is as set out in the Accountability Act and is expressly limited to fixing of rates for service, being the prices charged by the Corporation with respect to the provision of power. And there we were -- are referring to the 1989 stated case which is reproduced at Tab 7 of Manitoba Hydro's book of documents.

And, to be clear, we -- Manitoba Hydro would not have filed a depreciation study if we didn't know it impacts rates, but it's the suggestion that the -- the rates are -- are set separately that Manitoba Hydro takes issue with.

At slide 71, moving to that slide, MIPUG, and to a lesser extent CAC, attempted to attack the credentials of Mr. Kennedy, Manitoba Hydro's depreciation expert. I want to deal with this upfront, because Manitoba Hydro's depreciation study seemed to be a primary focus of MIPUG's submission.

And -- and I'm not going to get into the muck of this. Suffice it to say that Mr. Kennedy was the only witness at the hearing qualified as an expert in depreciation in utility plant accounting. Mr. Rainkie testified that Manitoba Hydro retains him because he is regarded as one (1) of the preeminent depreciation consultants in the country, and you'll find that at transcript page 4669.

Mr. Kennedy's CV speaks volumes to his qualifications. His client list includes Fortis, BC Hydro, AltaLink, Newfoundland and Labrador Power, ATCO, ENMAX, TCPL, and Mackenzie Valley Pipeline Project. By my account, he's testified at over thirty (30) different regulatory hearings, including appearances before the National Energy Board, the BCUC, the Nova Scotia Utility Board, the Yukon Utilities Board, and multiple appearances before the Alberta Energy Utilities Board.

Add that -- add to that another thirty (30) plus rate cases where his material was filed as evidence but he wasn't required to appear, and it becomes evident that the suggestion that Mr. Kennedy is not qualified to opine on the regulatory treatment of his depreciation studies is ludicrous.

Mr. Hacault also questioned the in -- independence of Mr. Kennedy's work and suggested the depreciation study was not the independent work of Mr. Kennedy. Manitoba Hydro retained Mr. Kennedy to gain the benefit of his and Gannett Fleming's wealth of experience conducting depreciation studies. It was clear in his retainer the policy decisions were to be made by Manitoba Hydro with, of course, the benefit of

Mr. Kennedy's sage advice.

So this is not a great a-ha moment that -- when we discussed during the evidence that Manitoba Hydro worked closely with Mr. Kennedy in producing the depreciation study. In fact, Mr. Kennedy described the relationship at the beginning of his direct testimony, and he said:

"Over the course of this assignment, I provided Manitoba Hydro with an indication of the potential impact of the conversion to the Equal Life Group or ELG procedure, concepts and options for the recovery of net sal -- salvage, options for modelling of gains and losses incurred upon retirement, and development of processes to allocate accumulated depreciation balances from the old -- from the old account structure to the new IFRS compliant account structure. The work related to these areas continued through 2010.

In May of 2010, Gannett Fleming and Manitoba Hydro held discussions regarding the information and policy decisions that I would require from Manitoba Hydro in order for Gannett Fleming to conduct a full and comprehensive depreciation study for Manitoba Hydro that would be in compliance with the conversion to IFRS. It was determined that a significant amount of detailed work would be required to be undertaken by Manitoba Hydro to undertake the detailed research and analysis of the historic asset records in order to properly allocate costs from the existing to the new asset component groups.

Following completion of this work by Manitoba Hydro, Gannett Fleming was retained in May of 2011 to complete a full and comprehensh -- comprehensive depreciation study."

And that can be found at transcript page 1,523.

Mr. Kennedy's direct evidence also described the importance of contributions of Manitoba Hydro staff in putting the study together, as well as the quality of data that they provided. And here he said:

> "In order to provide recommendations regarding average service life, I visited Manitoba Hydro and met with IFRS project staff, operational staff, management staff, engineering staff to determine the nature of the equipment included in each of the components in Manitoba in Manitoba Hydro's operational and engineering experience with the equipment and such in each category. Given the development of new components, Gannett Fleming is required to more thoroughly interview operational and engineering staff to determine appropriate asset service lives. A notable difference from the last depreciation study was the availability of analysis and empirical evidence collected by Manitoba Hydro in con -- in conjunction with its concern over aging infrastructure."

And that can be found at transcript page 1,526, and was part of Mr. Kennedy's direct testimony.

MIPUG has suggested this close and long-standing working relationship that Manitoba Hydro has had with Mr. Kennedy should be taken as a sign that Mr. Kennedy's advice to Manitoba Hydro is not independent. In a word, this is bunk.

You do not achieve Mr. Kennedy's credentials, or be invited to testify in the number of regulatory forums Mr. Kennedy has participated in time and time again, if you can't backup the advice you're given -- you are giving. It's just that simple.

Mr. Kennedy is an expert in preparing depreciation studies, and his evidence is that the best way to go about that task is to interview and work with the people at the utility who are intimately familiar with the assets. Further, we all have trusted advisors, and the attempt to catch -- to cast such relationships in a negative light is just frankly disappointing to Manitoba Hydro.

Now turning to page 72...

(BRIEF PAUSE)

MS. PATTI RAMAGE: Oh, sorry, I'm on -- it's still page 71. As was discussed during the hearing, there are two (2) main methods used by utilities to calculate group depreciation: The Equal Life Group procedure, or ELG, and the Average Service Life procedure, or ASL.

IFRS has a requirement that any gains and losses on the disposition or retirement of an asset must be recognized in net income immediately. This is different than the current North American regulatory practice of recognizing gains and losses in accumulated depreciation has been -- as has been followed by -- in the past by Manitoba Hydro.

This requirement has resulted in the need for Manitoba Hydro to review its depreciation methodology to ensure that, for compliance with IFRS, an appropriate matching occurs between the recoding of depreciation expense and the actual service life of the underlying assets.

The ASL procedure, which has been used by Manitoba Hydro in the past, calculates depreciation expense based on the average service life of assets within each class. This is why it is referred to the Average Service Life method.

Although accepted for utility accounting under current Canadian accounting standards, the ASL method causes an issue from an IFRS perspective because, except for those assets which have a life exactly equal to the average service life of the asset, or of the group, assets are being depreciated over a longer or shorter time frame than their expected life, or their expected service life. To the extent that assets are retired before or after the average service life of the group, losses or gains are generated.

And now we're turning to slide 72. I think we'll all be on the same page. In contrast, the ELG procedure recognizes that similar assets within a group will have different service lives, and it addresses this issue by developing -- developing depreciation rates with specific consideration of the expected retirement pattern for each asset within a class.

Every asset in the class is depreciated over its own expected life and, therefore, is expected to be fully depreciated, not over or under depreciated, when it is removed from service. This effectively minimizes the extent of losses and gains.

The resulting depreciation expense calculations are more robust, and are in full compliance with IFRS, and minimizing retirement gains or losses that must be recognized -- I'm sorry. This also results in minimizing retirement gains or losses that must be recognized in current income.

Given that ELG procedure specifically considers the expected life and desired annual depreciation charge for each individual asset in the calculation of the depreciation rate -- rate, it provides a more robust matching of annual depreciation with the consumption of the depreciable assets.

This matching is desirable from both an inter-generational equity perspective and an accounting perspective, as it provides a -- a systematic and rational allocation of cost in a straight-line method over the life of each asset.

Either ASL or ELG can be employed by an entity in a manner that is IFRS compliant, but the implementation details must differ, depending on the methodology employed. The ASL procedure uses an averaging approach, and as such, it's necessary to define and identify depreciable components quite narrowly, in order to meet the IFR -- IFRS requirement that a group of assets is depreciated in a way that appropriately reflects the useful life of the -- of the included parts.

For Manitoba Hydro an IFRS compliant ASL implementation would require a significantly greater degree of componentization in order to segregate parts within an existing group, which have longer or shorter expected lives than the average.

As pointed out by Mr. Kennedy in his testimony on transcript page 1,702 to 1,703, if one were to further componentize Manitoba Hydro's assets consistent with the Equal Life Groups identified in the ELG procedure, then the resulting annual depreciation expense would be comparable with that calculated by the ELG procedure.

The Green Action Coalition -- or Committee, understood the benefits associated with the adoption of the ELG procedure. Mr. Gange summarized their position, saying:

> "It is the review of the Green Action Centre, that the appropriate method of depreciation is to apply the rate that is most likely to reflect inter-generational equity.
> Green Action Centre accepts the position advanced by Mr. Kennedy in his evidence that the Equal Life Group method meets the rule of depreciation to make the appropriate

charges of their consumption of the value of the assets over their specific life. Green Action Centre accepts Mr. Kennedy's view that the ELG method is fairer in its allocation between generations with respect to the -- the depreciation expense."

And that can be found at transcript page 5748 through 5,749.

MIPUG expressed considerable concern during the hearing, and in its final argument with respect to the use of the ELG procedure. During its final argument, CAC indicated that it shared many of MIPUG's concerns. And the first concern that we're going to deal with is that ELG is front-loaded and onerous to current ratepayers.

And if we could turn to slide 73. Manitoba Hydro contends that the concept -- the suggestion that ELG is front-loaded and onerous ignores the improved matching and inter-generational equity achieved -- and the inter-generational equity achieved with the ELG methodology.

As explained in Appendix 5.7 to this application, and that would be the 2010 depreciation study, the ASL procedure applies the average expected life to every asset in the pool. As such, any assets retired before the average life is reached will be under-recovered, and the under-recovery will have to be either borne by ratepayers in place at the time that the asset is retired, or by future ratepayers who will also bear the costs of the replacement assets. As such, with use of the ASL procedure, later customers are required to subsidize earlier customers, which is contrary to regulatory principles.

Manitoba Hydro has demonstrated that the ELG method produces a smoother overall explen -- expense flow than ASL, when the impacts of gains and losses are considered, which contributes to rate stability for customers. This is consistent with Mr. Bowman's testimony that MIPUG cus -- customers desire stable and predictable electricity rates.

A comparison of the expense flows produced by the ASL and ELG methods is presented in Manitoba Hydro's rebuttal evidence, and you can find that at page 20, figure 6.

While the ELG depreciation rate may be higher than the current Manitoba Hydro ASL rate in the early years, this simply represents improved matching of depreciation with the consumption of the asset as opposed to what MIPUG indicates is accelerated depreciation in the early years. In later years, the ELG will be less than the ASL rate. Using the same logic, this would imply that the ASL method produces accelerated depreciation in the later years. The ASL method could be described as being back-end loaded and thus unfair to future ratepayers.

Overall, the objective is to match the annual depreciation expense with the consumption of the asset. The math demonstrates that the ELG method best satisfies this objective.

Manitoba Hydro would also like to note that the current Manitoba Hydro ASL rate is not the ASL rate that would be required upon adoption of IFRS. If Manitoba Hydro were to use the ASL methodology under IFRS, it would be necessary to further componentize the assets into similar life groups. ASL-based depreciation expense calculated for the revised component groupings would more closely align with the expense determined for the proposed ELG method.

A second issue raised by MIPUG --

MR. RAYMOND LAFOND: Excuse me. Before we go there, could Mr. Rainkie give me the reason why the rates under ASL would be different when -- after adoption of IFRS and maybe give me an example? Because a dam for a hundred and twenty-five years is a dam for a hundred and twenty-five years, right?

MR. DARREN RAINKIE: Mr. Lafond, it goes back to the issue of what components do you need to satisfy the requirements of IFRS. So, what we were trying to indicate there is that the current way of applying ASL in Manitoba Hydro would have to change. You would have to develop components that were more refined.

And when you do that, when you develop the components that are more refined, you're pulling some of the earlier life assets out of that group, and you're really getting closer to what ELG is trying to do. That's really what ELG is trying to do is produce -- is produce -- is look at the different assets -- the life of the different assets that are in each one (1) of those groups. So I think it wasn't understood very --

MR. RAYMOND LAFOND: That rather tells me that the current rates are too low rather than, you know, the adoption of IFRS, because AS -- I mean, it should be the same thing, because it -- no matter how you allocate the components, break it out in more components, the overall total should be, on a prorated basis, about the same unless we admit that current rates are simply too low.

MR. DARREN RAINKIE: Well, I think just the last part of Ms. Ramage's arguments indicates that there are some issues with ASL. I mean, it's been an accepted methodology in many different jurisdictions for a long time, but it -- get into this back-ended/front-ended type of an argument, but it can be accused of back-ending the depreciation, and I think that's one (1) of the reasons that we -- we've looked at ELG and thinks -- think it's a superior methodology. I mean, we --

MR. RAYMOND LAFOND: Oh, I --

MR. DARREN RAINKIE: We've indicated they're both acceptable methods under the current rate-regulated construct that we have, but I guess our comments here was talking about it moving to IFRS and satisfying the requirements of the IFRS standard. IAS 16, we see a different application of ASL.

MR. RAYMOND LAFOND: I hear you, and I follow this. The only thing is I'm not sure you're answering my question because, in fact, what we're saying is the current ASL rates are too low.

THE CHAIRPERSON: I wonder if the "rate" isn't the wrong word here. I mean, in terms of -- Manitoba Hydro, you're referring to a rate, but it's actually -- it's actually a change of methodology for ASL, right? I mean -- I mean, I agree with what Raymond is saying in that, you know, because we have ASL, it's likely to have lower rates than you would otherwise have if you went to ELG given the early adoption -- or the early depreciation rate that -- that's embodied in ELG.

But I -- to this -- this line here, we're talking about the fact that you have to do more components under ASL in an IFRS environment, right? I mean, that's the difference between -- I think we're talking the same thing. We're just not expressing ourselves very well.

MR. DARREN RAINKIE: You know, I think we -- I think we are talking the same thing. It's -- it's -- I guess I was trying to simplify it. And lo and behold, this is very hard to simplify.

But if -- if you start developing more refined components to apply -- to continue to apply an ASL methodology, what you're essentially doing is pulling some -- pulling apart the -- pulling out some of the earlier life assets, right, and -- and recognizing that some assets have shorter lives than the average and some have longer lives.

And I think that's what ELG is trying to do. So I think at its core, that's what -- that's why ELG is better. I think we're talking the same way. Maybe we're just a little tired of the topic.

MR. RAYMOND LAFOND: Again though, this -- this issue has nothing to do with ELG. We're talking of ASL rates which would be different under ASL. You know, the -- the depreciation rates under ASL would be different than under ASL if we were required to adopt IFRS.

I'm just asking why this happens because the conclusion I have to take is whether or not you in -- you -- you view this as one (1) component or three (3) separate components, the proration of all the different years would seem to indicate that currently we're simply -- we simply have two (2) long life expectancies for the -- the ensemble to them all.

(BRIEF PAUSE)

MR. ANTOINE HACAULT: Members of the Board, I really appreciate the questions. And I -- I'm just not too sure how this fits in argument when we start asking witnesses further questions and getting further information because then it raises, should we be asking Mr. Bowman the same question to get both sides of the view on the new questions that are being asked of the Board (sic).

MR. RAYMOND LAFOND: No, but all I want here is some clarification to this statement. That's all I'm asking. I'm not asking for any additional information. I just want an understanding of the statement.

MR. DARREN RAINKIE: Maybe I could help by thinking back to what's already on the record and the simple example that we went -- went through.

If you had an asset with the five (5) -- in one (1) group with the five (5) and the fifteen (15) year life, then you'd, under ASL, apply, you know, a ten (10) year life to that -- to that group of assets and calculate deprecion ex -- depreciation expense accordingly. That's how the ASL works. I think it's -- nobody's disputing that.

But if we tried to apply ASL under IFRS, then I think what we're going to have to do is probably break that -- that component grouping into two (2) components, one (1) asset with a five (5) year life and one (1) asset with a fifteen (15) year life and recalculate depreciation. And that's going to produce a different number than the original application of that in terms of averaging for the ten (10) years.

And I don't know, that's -- I keep thinking about that simple example that Mr. Kennedy put forward. And that's I think the easiest way to understand this, in my mind but...

MR. RAYMOND LAFOND: I think I understand all this. But if you have two (2) components, one (1) with a life expectancy of five (5) years, another one of fifteen (15) years and they're the exact same value, then you would assume that ASL average at seven and a half years (7 1/2) years would give you the same -- the same results whether you componentize or not.

So, therefore, I have to conclude that instead of using seven and a half (7 1/2) years, we're using, for instance, ten (10) or twelve (12) years.

(BRIEF PAUSE)

THE CHAIRPERSON: I suggest that based -- given Maitre Hacault's comments about not wandering too far from the record, I would suggest that maybe we leave this and have the panel examine the example that was given by Mr. Kenney in -- that shows up in the transcript so that we don't wander too far off the record and the nature of this closing argument.

MR. PATTI RAMAGE: I -- I think that's fair. That example is in an appendix to Manitoba Hydro's rebuttal evidence. I don't know if I'm going too far, but I understand, I think, what you're saying, Mr. Lafond. And I think that's the adva -- one of what IFRS is trying to achieve is exactly what you're perhaps saying is -- is a concern with how ASL is currently used.

Moving forward though, a second issue raised by MIPUG is that the ELG procedure is overly sensitive to retirement data. Mr. Bowman claims that in practice ELG will not result in an accurate depreciation expense, as ELG is more sensitive than ASL to the selection of the Iowa curve and relies much more heavily on the existence of accurate historical information data. As such, Mr. Bowman argues that where the retirement data is limited, as is the case for certain long-lived assets, such as dams and spillways, or incomplete EL -- ELG will produce inaccurate results.

Manitoba Hydro asserts that depreciation is an estimate and that the selection of the Iowa curve and the deteriorate -- determination of the corresponding depreciation rate is not based strictly on an analysis of historical retirement data. And just to make sure we're all on the same page, we're now up to slide 74 in our presentation.

The Iowa curve is selected by the depreciation consultant using professional judgment in consideration of historical analysis, discussion with management to determine whether and the degree to which the historical results are predictive of future retirement activity, knowledge of the industry, and peer analysis.

In circumstances of long-live assets -- for example, those in the seventy-five (75) to a hundred and twenty-five (125) year range -- it is reasonable to expect that limited retirement experience would be reflected in Manitoba Hydro's accounting records, given the current age of Manitoba Hydro's generating stations. This is where the professional judgment and the experience of a depreciation pro -- professional, such as Mr. Kennedy, is required to compensate for lack of empirical evidence.

Through this process, a reasonable estimate may be made with respect to the expected future retirement pattern. The ELG procedure will produce a pattern of depreciation expense that aligns reasonably well with the actual assets in use, and -- in use -- use and useful during any given period. In contrast, the ASL procedure makes no attempt to consider and reflect the individual lives of assets within a depreciation pool and, as such, is less accurate than the ELG procedure.

And now turning to slide 75. A third issue raised by MIPUG is that IFF12 understates the impact of ELG on depreciation expense for the Wuskwatim Generating Station as an ASL rate was utilized. On transcript page 5,334, Mr. Bowman indicates an estimated annual impact of $4 million.

Manitoba Hydro asserts that Mr. Bowman's calc -- calculation is fundamentally flawed, and, as a result, he has over stated the impact to IFF12. MIPUG's calculation does not consider NCN's ownership of WPLP. The annual difference between the two (2) calculations shown in Manitoba Hydro Exhibit 106 is $2 million after ded -- after deducting the non-controlling interest.

More importantly, Manitoba Hydro would like to emphasize that ASL with net sal -- without net salvage scenarios reviewed during the hearing are purely hypothetical. In order to use an ASL-based depreciation methodology under IFRS, further componentization beyond that presented in Exhibit 106 would be required. And that would result in annual depreciation expense sim -- similar to that shown for the ELG-based scenario.

Furthermore, Manitoba Hydro would point out that at the time of the preparation of IFF12, ELG-based deprecation rates were not available for Wuskwatim generating station, and Manitoba Hydro had not yet finalized the componentization of cost. As such, it was necessary to make assumptions for the purpose of -- of forecasting IFRS compliant depreciation expense.

As explained by Mr. Kennedy in his dire -- direct testimony at transcript pages 1,532 through 1,533, and further discussed through cross-examination at transcript page 1,982 to 1,990, ASL-based depreciation rates were determined for Wuskwatim for -- for the Wuskwatim Generating Station.

Gannett Fleming considered the ASL rates to be appropriate under the circumstances, as the generating station was not yet in service at the time of the depreciation study, and the final distribution cost by install year and by component was not yet known.

An ELG-based depreciation rate will be calculated in the next depreciation study, which, assuming a five (5) year interval, is expected to be done March 31st, 2015. Considering the long expected life of the generating station, the variance it accumulates by use of a different model for the first few years of the generated station life -- generating station's life is not expected to have a material impact on the plant's depreciation rates for the remainder of its useful life.

We're now at slide 76. The fourth concern raised by MIPUG is that ELG does not work well with the increasing pattern of capital expenditures forecast in CEF12. MIPUG specifically identifies concerns with the depreciation expense included in IFF12 for Keeyask and Conawapa.

Manitoba Hydro would first like to point out that the figures quoted by Mr. Bowman in his testimony at transcript page 5,331 through 5,339 significantly overstate the potential additional impact of ELG for future new generation and transmission items. Mr. Bowman's calculations for Keeyask and Conawapa are based on the overstated number he calculated for the Wuskwatim Generating Station, as previously described, and which Manitoba Hydro has demonstrated is overstated.

Manitoba Hydro would like to further point out that it is not the intent of IFF12 to provide a precise calculation of depreciation expense beyond the test years. For the purposes of the IFF, Manitoba Hydro applies the current depreciation rates to the forecast period. No attempt is made to recalculate future depreciation rates on five (5) year interval -- intervals to reflect changes that might happen in each successive depreciation study.

It is expected that over the next twenty (20) years, depreciation rates will be recalculated a number of times and will -- and -- as will changes in assets -- and will change as assets age, as existing depreciation variances become fully amortized and as new assets are added.

With an ELG methodology, it has been demonstrated that depreciation rates decline over time as assets age. As such, it is reasonable to assume that by the time Keeyask and Conawapa are constructed, depreciation rates in other areas will have declined, partially offsetting the differences identified by Mr. Bowman.

Now if we could turn to slide 77. The fifth concern raised by MIPUG is that Manitoba Hydro does not have accounting policies that reflect ELG and, as such, the use of ELG is inappropriate. MIPUG indicates that Manitoba Hydro currently records the replacement of assets as period repair and maintenance costs.

Manitoba Hydro asserts MIPUG's conclusion regarding Manitoba Hydro's capitalization policies is inaccurate and would appear to be based entirely on a comment made by Mr. Warden at transcript page 4,585 regarding poles. MIPUG has taken a comment regarding a single asset of relatively low value - that is, a single pole -- and has extrapolated it to Manitoba Hydro's entire system.

In most circumstances Manitoba Hydro capitalizes replacement assets, as can be readily verified by comparison of the figures for the surviving original cost of hydraulic generating assets disclosed in the 2005 and 2010 depreciation studies. Appendix 5.7 of Manitoba Hydro's application contains these studies, and they're at page Roman number III-16, and Appendix 24, page Roman numeral III.

But the key point here is that over the five (5) year period between those studies, the hydraulic generation asset base grew from 4.2 billion to 4.7 billion, which is an increase of $500 million, or 12 percent, without the addition of any new generating stations.

Further, although no major changes in

policy were expected, Manitoba Hydro is expecting that in practice most retirements will be recorded in the future than -- more retirements will be recorded in the future than have been in the past, as was explained by Mr. Te -- Kennedy at transcript page 1,580.

The sixth concern raised by MIPUG is that implementation of ELG will result in over advancing fixed costs in the economic assessment of long-term hydraulic assets, which may lead Manitoba Hydro to falsely reject hydraulic development.

Manitoba Hydro rejects MIPUG's argument that the ELG method of depreciation is front-end loaded, as -- as previously discussed. More importantly, Mr. Bowman's understanding of Manitoba Hydro's economic evaluation measures appears flawed. Manitoba Hydro's economic assessment follows the well established, fundamental economic evaluation concept, which is based on discounted incremental cashflow analysis of project benefits and costs, including the initial cash outlay for construction.

Accounting costs such as depreciation, sunk costs, overheads, interest, loans, and loan repayments are not facored -- factored in to the economic evaluation. In fact, inclusion of depreciation costs as well as the initial cash construction outlay would be -- would effectively double-count the capital project costs in the economic analysis.

Moreover, Manitoba Hydro's assessment of reef -- of resource plans is multifaceted. In addition to economics, the Corporation considers environmental, social, political, and financial factors in its overall assessment of alternative resource plans. While depreciation has a role in the financial evaluation in capital plans, it is certainly not an overriding factor, and Manitoba Hydro is in no danger of making erroneous decisions based on its choice of depreciation practices.

The seventh concern raised by MIPUG is that Manitoba Hydro's decision to use ELG would make its depreciation practices inconsistent with that of other Canadian Crown electric utilities. Manitoba Hydro argues that the notion of an industry standard is not reflective of reality.

As noted in Manitoba Hydro's rebuttal evidence, the nature and level of component breakdown varies between utilities, and the larger Crown utilities cited in MIPUG's evidence -- BC Hydro, SaskPower, Hydro-Quebec, and Newfoundland and Labrador Power -- have implemented ASL differently than Manitoba

Hydro.

These utilities have divided their deprecial -- depreciable assets into a much more granular set of components and use a unit accounting approach rather than a group accounting -- a group accounting depreciation approach. And here I refer you to Manitoba Hydro's rebuttal at page 19.

As such, the use of a common descriptor, ASL, does not guarantee that the depreciation practices of the companies using the method are truly comparable. By their comments, Mr. Bowman and Mr. Hacault do not appear to understand the accounting differences between a group accounting methodology as used by Manitoba Hydro as opposed to a unit accounting method which, we have pointed out at page 19 of the rebuttal evidence, is used by the utilities cited in MIPUG's evidence.

While Manitoba Hydro could implement a level of componentization at a much more granular level to allow for continu -- continued use of an ASL depreciation methodology in a manner that was compliant with IFRS and consistent with more of the cited industry peers, there would be a substantial increase in administration costs which would ultimately be borne by ratepayers. This is unnecessary, as comparable results can be achieved with the use of the ELG approach as proposed by Manitoba Hydro.

The final concern raised by MIPUG which we will address is that Manitoba Hydro has overstated the gre -- the degree to which further componentization would be required under an IFRS-compliant model.

MIPUG indicates that other utilities have been able to implement IFRS using an ASL approach without the need for significant additional componentization. MIPUG indicates at page 2-3 of its written submission that Mr. Kennedy acknowledged in cross-examination that the more limited system of accounts in use by the Ontario Energy Board would seem to generally meet the compent -- componentization rules.

Manitoba Hydro asserts that MIPUG has taken Mr. Kennedy's comments out of context and encourages the Board to review transcript page 3,394 through 3,398, which captures the exchange between Mr. Hacault and Mr. Kennedy regarding the Ontario Energy Board's system of accounts.

It is clear from the transcript that this system of accounts is intended for use by the eighty (80) small electricity distributers on Ontario who would -- I would submit, as small distributors only, would ha -- would not have as diverse an asset base as to make it comparable to Manitoba Hydro. Notably, Mr. Kennedy confirmed that the largest generator in Ontario, OPG, does not follow this system of accounts and is much more componentized.

If we go to the next slide. In summary, after reviewing the use of ELG as part of the current depreciation study, Manitoba Hydro concluded that ELG was a superior methodology to ASL, both for financial reporting and rate-setting purposes.

ELG reduces the amount of gains and losses that must be recorded in net income and, as a result, contributes to rate stability for customers. In addition, ELG improves intergenerational equity by matching the amortization cost to the life of the assets in use, ensuring that each generation of ratepayers is charged only for the assets of benefit to that generation.

This principle was demonstrated by Mr. Kennedy on pages 1,614 through 1,619 of -- of the transcript, using the simple example presented on pages Roman numer -- numeral XXXVII through Roman numeral -- or Roman numeral II-37 to Roman numeral II-39 of the 2010 depreciation study, which is at Appendix 5.7 of the application.

It is also unnecessary to incur the

additional ongoing administrative costs which would be required to componentize Manitoba Hydro's assets to a much finer level of granularity in order to implement ASL on an IFRS-compliant basis, as ELG delivers a similar level of depreciation expense.

Turning to the next slide. I'm also going to ask -- Mr. Fernandes is going to take over for a bit. And I'm not sure if the Board would like a break themselves. I'll get my break by getting off the mic, but you might...

THE CHAIRPERSON: Yeah, why don't we take ten (10) minutes, please.

--- Upon recessing at 2:18 p.m.

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

THE CHAIRPERSON: I believe we're ready to resume the proceedings.

MS. ODETTE FERNANDES: Thank you, Mr. Chairman. We are now at page 80 of Manitoba Hydro's slides. The topic of Manitoba Hydro's demand-side management programs garnered a significant amount of attention during this GRA.

DSM has been, and continues to be, a significant component of Manitoba Hydro's strate --

strategy in fulfilling the Corporation's mandate and responsibilities. For over twenty (20) years, DSM has and continues to play a key role in meeting Manitoba's electricity demands in the most economic manner.

DSM assists Manitoba Hydro's customers with managing their electricity bills and promotes environmental sustainability. The president and CEO of Manitoba Hydro appeared before you and stated that he was a real believer in the value of managing demand by encouraging energy efficiency and conversation. And that's at transcript page 269.

Ms. Morrison (phonetic), Manitoba Hydro's division manager responsible for the delivery of DSM, also appeared before you and indicated that Manitoba Hydro's long-term aggressive commitment to DSM has resulted in 90 percent awareness of the Power Smart brand in Manitoba, with over 60 percent of residential customers able to recall, unaided, Manitoba Hydro programs available to them to help manage their energy bills, and one-third (1/3) of customers indicating that they have participate -- participated in at least one (1) program. And that was at transcript page 2,734.

I am now moving to slide 81. Manitoba Hydro is a -- is recognized as a leader in DSM, as evidenced by the fact that it is frequently invited to consult and provide advice to other utilities, government, and industry associations with respect to commercial, industrial, and residential Power Smart Program design and marketing.

Manitoba Hydro's Power Smart Residential Loan Program was recently selected as a Canadian example of best practices by the International Energy Association. And this was referred to in Manitoba Hydro's rebuttal evidence at page 25.

Now moving on to slide 82. Manitoba Hydro has invested over $438 million in Power Smart initiatives over the last twenty-three (23) years, offering more than thirty-five (35) incentive-based programs. This has resulted in ratepayers saving 1,966 gigawatt hours and 583 megawatts of electricity as -- as at March 31st, 2012.

This translate in -- into 62 million of annual ele -- electricity bill savings for those customers participating to date. This was discussed at transcript pages 2,734 to 2,735. These savings -- that is, the $62 million per year -- will continue to be realized by customers in each and every year going forward. And we're not stopping there.

Manitoba Hydro continues to have programs in the market today to help customers. Ms.

Morrison spoke to a number of initiatives that are place -- that are in place and continuing, such as the Home Insulation Program and the Low Income Energy Efficiency Program, which specifically assists in managing heating costs. Now, Manitoba Hydro has provided a list of its current comprehensive program offerings at slide 83.

Despite Manitoba Hydro's succ -- successful track record in delivering DSM programs -- and I -- and I note Mr. Dunsky acknowledged Manitoba Hydro's history of DSM success at transcript page 4,167 -- Intervenors are concerned that this success is not going to continue into the future.

Manitoba Hydro does not share this concern. We have a president who is committed to DSM, staff who Mr. Dunsky himself characterized as a strong Power Smart team, and we have a proven track record. When Manitoba Hydro invests in DSM, it is spending ratepayer dollars. And like any other expenditure made on behalf of ratepayers, careful consideration is given to ensure that there will be a benefit to ratepayers.

Manitoba Hydro believes concerns raised by Intervenors with respect to the future of DSM are misplaced and are largely based on a misunderstanding of the use of metrics employed by Manitoba Hydro when evaluating the cost effect -- effectiveness of DSM programming.

I now turn to slide 84. I'd like to address Manitoba Hydro's process for identifying which DSM opportunities to pursue with incentive-based programming and how program designs are developed.

As noted at page 26 of its rebuttal evidence, there are two (2) high-level process that are undertaken by the Corporation in developing its DSM incentive-based programs: first, a screening process and also a program design process.

At the screening stage, a high-level benefit cost assessment is undertaken of a potential DSM opportunity. In this process, consideration is not given to who pays for the opportunity or for any program administration costs. And that is the costs associated with offering an incentive-based program.

For this process, Manitoba Hydro uses a marginal resource cost, or MRC, test. The MRC is a high-level assessment of the present value of the avoided costs over the life of a technology divided by the incremental cost of the energy efficient technology. The MRC test is only a high-level screening process, and Manitoba Hydro is very liberal in using the test to include all opportunities which may be close to passing the MRC. For example, Manitoba Hydro doesn't include the administrative cost associated with the offering which, at times, can be significant. And the MRC test also recognizes measurable non-electricity benefits, such as water savings.

Manitoba Hydro recognizes other utilities use alternative tests, such as the societal test. However, we are confident that the end result of the Corporation's screening process would be the same whether Manitoba Hydro used the MRC, modified TRC, or societal cost test for its screening process. As provided in its rebut -- rebuttal evidence at page 27, Manitoba Hydro considers any and all opportunities that are close to passing the MRC.

Moving on to slide 85. If a potential DSM opportunity passes the high-level screening phase, then Manitoba Hydro undertakes a much more detailed analysis of potential incentive-based programming designed options. At this stage, consideration is given to who pays for implementing the DSM opportunity; that is, how the total cost of the DSM opportunity is shared between the participating customer and the ratepayers.

In assessing program design options,

Manitoba Hydro uses a number of metrics, including customer payback periods; the TRC test; the societal cost test; the levelized utility cost test, or LUC, and the rate impact measure test, or RIM.

Each of these metrics provides useful information, and the metrics are collectively used in making DSM program design decisions. Ms. Morrison was emphatic on this point, and at transcript page 3,303, she stated:

"It's not a simple matter of saying, Well, it's passed this test, so now it goes to this test, now it goes to this test. We're looking at all of these components when we're designing a program."

There was quite a bit of discussion and appeared to be misunderstanding by Intervenors and consultants with respect to Manitoba Hydro's use of these metrics. Intervenor consultants Mr. Chernick and Mr. Dunsky appear to believe that Manitoba Hydro uses the RIM and LUC metrics as being a determinant as to whether Manitoba Hydro would pro -- proceed with the particular DSM opportunity. This is not correct.

As stated by Ms. Morrison during her exchange with Mr. Williams, beginning at transcript page 3,138:

"Manitoba Hydro uses the LUC and RIM as high level metrics and a guideline in the overall DSM program design process, and they are used in combination with other metrics that I've referred to before, such as the total resource cost test, the societal test, and the customer payback calculations.

Within this process, the incremental cost of DSM opportunities are broken down between what the participating customer pays and what the Utility, on behalf of all ratepayers, invests. The metrics assist in determining an appropriate balance of investments by either party."

And this discussion occurred at transcript page 3,177. Contrary to the testimony of Intervenor witnesses, Manitoba Hydro does not use the RIM or the LUC as giving programs the red light or the green light. This is clearly a misunderstanding on the part of the witnesses.

Moving on to slide 86. Manitoba Hydro

takes a different perspective on pursuing DSM relative to Mr. Dunsky. Mr. Dunsky's focus is on pursuing DSM opportunities and assessing the economics of those opportunities by only considering the utility's, or the DSM programming provider's, portion of the DSM cost. Further, Mr. Dunsky appears to only focus on the average cost of a DSM portfolio, as opposed to assessing the margin of cost for each individual DSM opportunity.

Manitoba Hydro is confident that the Corporation is taking the appropriate approach to pursuing all economic DSM opportunities. Appropriate economic decisions should be made for each individual DSM opportunity, and the to -- total cost that each opportunity, and that is the relevant factor to consider in the DSM decision-making process.

Ultimately, ratepayers pay for the total cost of DSM, whether it is through rates or investments made by the participating customers. These metrics are used as guidelines in the DSM decision-making process. However, it is still important to recognize that if a DSM program design has a RIM of less than one (1), then the DSM program design is expected to impact rates.

However, in the DSM decision-making process, Manitoba Hydro recognizes that there are other considerations; for example, fairness and equity among the overall customer base and long-term energy sustainability objectives. Therefore, the LUC and RIM metrics are -- are used as guidelines, as opposed to giving the green light or red light to programs.

THE CHAIRPERSON: Could you repeat that sentence? A DSM program designed with a RIM of less than one (1), could you -- could you repeat that, please?

MS. ODETTE FERNANDES: Yeah, I -- I indicated that if the DSM design has a RIM of less than one (1), then the DSM program is expected to impact rates.

THE CHAIRPERSON: Okay.

MS. ODETTE FERNANDES: I will move on to slide 87.

THE CHAIRPERSON: Okay.

(BRIEF PAUSE)

MS. ODETTE FERNANDES: Manitoba Hydro recognizes a component of the industry has moved away from using the RIM test. There are rational reasons for this shift. However, this shift doesn't mean that the RIM metric has no value in DSM decision-making for all entities involved in delivering DSM programming.

Within the industry, DSM programming is generally provided either through a traditional, regional utility or a non-utility entity created solely for the purpose of delivering DSM programming.

In the latter case, the DSM decision-making process has naturally moved towards a more narrow analysis, which focusses on the non-utility component of DSM costs. In those regions, there is no need or the ability for those non-utility entities to assess the impact of DSM costs on electricity rates.

One (1) would expect that the focus of those entities would be on their cost to deliver energy savings through the DSM programming. Manitoba Hydro would argue that all customer interests are better protected if a broader assessment is undertaken which considers the total cost of DSM.

It should be further recognized that Manitoba Hydro's legislated mandate includes the promotion of economy and efficiency in the end use of power. And that's located at Section 2 of Manitoba Hydro Act.

Non-utility entities delivering DSM programming would not be required to consider the equity issue associated with who pays for DSM initiatives, and that would be the split between participating customers and all ratepayers.

Consideration for the co -- total cost of DSM initiatives, including the customer contribution and ratepayer contribution, is not required to be a factor in that decision-making process, as is the case with Manitoba Hydro. Similarly, where DSM targets are established by third parties, one (1) would expect the role of RIM to be greatly diminished because the focus is on achieving those targets.

I'm now moving on to slide 88. There appears to have been some unfamiliarity with how Manitoba Hydro's generation marginal costs, more properly called a generational marginal value, are calculated, as detailed in the transcript at page 2,910 through 2,931. Manitoba Hydro provided a description of how generation marginal value is determined in Manitoba Hydro Exhibit Number 94. This melo -- methodology is appropriate for Manitoba Hydro's system where incremental energy savings in Manitoba generally result in incremental exports to markets outside of Manitoba.

As noted in Section 5.1 of Manitoba Hydro's rebuttal evidence, the marginal generation value estimates consider the value on the export market of both energy and generation capacity. Hence, there is a generation deferral component to the generational marginal value, but the deferred generation is located in the export market rather than within Manitoba.

As noted in Manitoba Hydro Exhibit 94, the methodology used for determining of current estimates of transmission and distribution marginal costs is provided in the report attached to Information Request GAC/Manitoba Hydro's Second Round 23A. The written, pre-filed testimony of Mr. Chernick identified issues with this work.

Some of these issues were, again, raised in the subsequent testimony of Mr. Chernick beginning on pages 3966. Manitoba Hydro notes issues with the transmission and distribution marginal costs were addressed in Section 5.1 of its rebuttal evidence.

Further in the written, pre-filed testimony of Mr. Chernick and in his subsequent oral testimony beginning at transcript page 3,970, there is an inference that in the conversion of the transmission and distribution marginal costs into cents per kilowatt hour. This calculation implicitly assumes a flat load and that this load shape is not res -- representative of most end uses including average end use for which have a forecast 62 percent load factor.

Mr. Chernick is correct in noting the conversion calculation used in response to CAC/Manitoba Hydro Second Round 27B that that calculation does assume a flat 100 percent load factor; however, as stated in the testimony of Ms. Morrison beginning at page 2,907, Manitoba Hydro does not assume a flat 100 percent load factor in the detailed DSM program analysis but, rather, does take into account the differential between winter energy, summer energy, and contribution to winter peak capacity and summer peak capacity.

And I'm now on slide 89. Thus, energy savings from home insulation which occur in the winter months would be valued higher than energy savings from a commercial chiller program which provides savings in the summer. Manitoba Hydro, in its view, does appropriately consider load profiles and load factors in its detailed DSM program analysis.

There was also some discussion during the hearing that projected levelized costs of Conawapa may appear higher than Manitoba Hydro's current estimates of marginal generation values. Levelized costs of Conawapa such as discussed in the transcript beginning at page 482 are in future dollars based on the in-service dates for these sta -- these stations, as indicated in Manitoba Hydro's capital expenditure forecast '12.

Future dollars include increases due to inflation between today and the projected in-service date. As such, these future dollars are not directly comparable with the generation marginal value figures detailed in its response to CAC/Manitoba Hydro's Second Round 27B, which are noted to be in 2011 dollars.

Further, as discussed in the written pre-filed testimony of Mr. Chernick, the conversation of the marginal cost into cents per kilowatt hour implicitly assumes a flat load, also known as the 100 percent load factor.

Conawapa's annual capacity load factor under average flow conditions, and this is as per Manitoba Hydro's 2012/'13 Power Resource Plan, is around 60 percent. Hence, Conawapa produces much less lower value off-peak energy in comparison with a 100 percent load factor product and, therefore, is of more value to the Manitoba Hydro system.

Based on the submissions of Intervenors during this hearing, it is fair to ask: Can Manitoba Hydro do more DSM? Manitoba Hydro maintains its Power Smart plan consists of pursuing all economic opportunities and that staff regularly assess and revisit programming for potential economic opportunities.

Intervenors argue that much more can be done on the basis that Manitoba Hydro's contribution towards DSM, otherwise referred to as the utility cost, is only in the two (2) cent per kilowatt range.

There are two (2) elements to this argument which are flawed. First, the relevant DSM cost is the total of the utility's investment together with the participating customer cost. As discussed by Ms. Morrison beginning at transcript page 2,956, it is the ratepayer who ultimately pays for the DSM measure either as a ratepayer alone or as a ratepayer and participant.

This reality introduces a complicated component of the DSM decision-making process largely not understood. And I'm moving on to slide 90.

THE CHAIRPERSON: Before you go there could I ask you a question about the first bullet on 89.

"Care must be used in comparing generation and marginal costs [okay] to supply."

What do you mean by "supply"?

(BRIEF PAUSE)

MS. ODETTE FERNANDES: What we mean by "supply option" is the marginal value on the export market.

THE CHAIRPERSON: Oh, okay.

(BRIEF PAUSE)

MR. RAYMOND LAFOND: When you look at these values you look at fixed prices or firm prices or -- or spot prices?

MS. ODETTE FERNANDES: It's the long-term firm prices.

(BRIEF PAUSE)

MS. ODETTE FERNANDES: Now, on slide 90. DSM is different than new generation options in that there is no additional domestic revenues associated with DSM how there is with new generation. With DSM, Manitoba Hydro is able to export the conserved energy in the export market and, therefore, there is marginal increased revenue with DSM.

Overall, in assessing DSM options

against new generation options, the economic assest -- assessment must include the impact to revenues as well as the costs. The assessment of how much Manitoba Hydro can invest in a DSM program is determined by the combination of the LUC and RIM metrics.

Linked with this issue is the equity issue in terms of how the DSM costs should appropriately be split between the participating customer and all ratepayers. To date, Manitoba Hydro's overall strategy has been to design programs whereby all customers are better off.

In Manitoba Hydro's current situation, where its marginal cost is primarily determined by the electricity export market, it is only economic for the Corporation to invest in DSM measures sufficiently justified by the difference between the electricity export value and the value realized by selling the energy in the domestic market with an adjustment made for the value associated with deferring distribution and transmission investments.

From an economic perspective, the objective of a Crown Corporation is to optimize the benefits to its ratepayers by pursuing all economic DSM opportunities, and investing in those opportunities to the gre -- to the degree whereby all customers are economically better off in aggregate.

Moving on to slide 91. The second element of the Intervenors' argument which is flawed is a reference to the average cost of DSM being relevant. Although Manitoba Hydro would agree that the metric provides a valuable measure for the utility cost of its overall DSM plan, the relevant issue is the cost of individual DSM opportunities, not their average costs.

DSM offers the flexibility and advantage for a utility to pursue only economic opportunity as measured on their individual merits. Each DSM opportunity is an opportunity on its own, and a utility has the choice of pursuing each one individually. As such, it is the economics of each opportunity which is relevant. The overall average cost of a DSM plan is simply the end result of a number of economic DSM decisions with some be -- being more economic than others.

Manitoba Hydro -- Manitoba Hydro's point is best demonstrated by undertaking a more detailed assessment of its 2011 Power Smart plan. Manitoba Hydro's response to PUB/Manitoba Hydro First Round 108A shows that the levelized total resource costs for programs range from one (1) cent per kilowatt hour to seven and a half (7 1/2) cents per kilowatt hour with an overall average levelized resource cost of three point nine (3.9) cents per kilowatt hour.

As Ms. Morrison testified, Manitoba Hydro pursues all economic opportunities; some cost less, and some cost more but Manitoba Hydro pursues all those opportunities that have a levelized cost less than the Corporation's marginal value.

The cost of pursuing these DSM opportunities is shares -- is shared between the participating customers and all ratepayers, with the latter being referred to as Manitoba Hydro's DSM cost. The cost of the individual DSM opportunities range in value, and are hidden when only the average cost is considered.

Manitoba Hydro, therefore, cautions the PUB when Intervenors and their consultants only refer to the average cost of a DSM plan, and only the utility's investment in a DSM opportunity. Manitoba Hydro would argue its DSM plan is -- is developed in an appropriate manner with its customers' best interests being the primary consideration.

Manitoba Hydro's DSM decision-making process considers, firstly, the total costs of DSM opportunities, secondly, the economics of individual DSM opportunities as opposed to the average cost of a full DSM portfolio, and, finally, equity issues including ensuring the Power Smart plan has a good balance of DSM programming available for all customers, and an appropriate cost sharing is achieved -- is achieved between participating customers and all ratepayers.

In terms of doing more DSM, Manitoba Hydro is continuously looking for new economic opportunities. As indicated by Ms. Morrison at transcript page 3154, and I quote:

"Manitoba Hydro has a technical engineering group that reviews ongoing technologies entering the marketplace that might suit Manitoba Hydro's market sectors. We're regularly looking on a day-to-day basis. It's part of the integrated work they do."

Mr. Dunsky suggests that Manitoba Hydro isn't pursuing some opportunities which could be economic, such as ductless heat pumps. Contrary to Mr. Dunsky's suggestion --suggestion, ductless heat pumps are not cost effective in Manitoba. Using Mr. Dunsky's estimates of energy savings and installed measured costs, ductless heat pumps have a levelized resource cost greater than the eight point five-two (8.52) cents per kilowatt hour.

Mr. Dunsky's assessment of cost effectiveness appears to have been based on the utility cost test which does not reflect the total DSM cost. Mr. Dunsky seems to suggest the Utility should only consider its direct cost to achieve the conserved energy.

Manitoba Hydro disagrees with this view. As previously pointed out, customers pay for total -- the total cost of DSM whether through direct investments by participating customers or through electricity rates. The relevant cost for DSM is the total cost of a DSM opportunity.

I'm now moving on to slide 92.

(BRIEF PAUSE)

MS. ODETTE FERNANDES: Manitoba Hydro agrees that using a savings ratio metric is generally valid for comparing energy conservation efforts among regions with similar load characteristics and having similar marginal cost considerations. However, caution must be exercised in using the metric for comparison among other regions as a savings ratio metric can produce misleading conclusions. Back when Mr. Dunsky worked for Manitoba Hydro, he provided this same caution, and this was noted in our rebuttal evidence at page 25.

Mr. Dunsky states in his testimony that he has eliminated pars -- possible market reasons for Manitoba Hydro's savings and targets to be lower than other, quote on quote, "comparable jurisdictions." Mr. Dunsky specifically picked the five (5) cohorts, stating that they best represented comparable characteristics of Manitoba markets. Curiously, Mr, Dunsky did not attempt to include the region which most closely resembles Manitoba's load characteristics, Quebec.

Manitoba Hydro's submission is that Quebec is the most comparable cohort to Manitoba Hydro. Quebec has a high number of heating degree days combined with a high penetration of electricity heat. Add on low electricity rates plus a long standing and recognized energy conservation initiative. This is especially interesting given Quebec's ratio of savings to load of .55 percent for 2010, which is more comparable to Manitoba Hydro's ratio of .43 percent in that same year. And that was provided as Exhibit GAC/CAC Number 4. And that was slide 13.

Mr. Dunsky's analysis is oversimplified as each regional comparison is done on an individual component basis and not in aggregate. When Que -- comparing Quebec-Hydro to Manitoba Hydro, one (1) can see that the two (2) entities have more characteristics in common than any of the cohorts identified by Mr. Dunsky, but he chose not to include them.

Manitoba Hydro finds it particularly interesting that Mr. Dunsky expanded his analysis beyond the five (5) cohorts when one (1) of the characteristics and, in this case, low electricity rates was found to have a relationship among his chosen cohorts. This was done with no additional qualification for what may be occurring within those jurisdictions.

Mr. Williams does this again in his final argument by drawing reference to Idaho and New York having low electricity prices, ignoring that they were not part of the chosen cohorts that Mr. Dunsky so carefully selected as being appropriate, comparable jurisdictions. For the record, Massachusetts and Vermont were among the five (5) cohorts, and their rates are fourteen (14) cents per kilowatt hour and thirteen (13) cents per kilowatt hour respectively.

Manitoba Hydro recognizes that all

metrics must be used with caution, and, therefore, the Corporation has concluded that the best approach to assessing its efforts relative to other regions would be best accomplished by comparing its specific DSM programming against DSM programming in other comparable regions.

Now, moving on to slide 93. Declining targets do not mean a declining commitment to energy conservation. Manitoba Hydro's declining tar -- targets reflect the Corporation's long-term market engagement and diminishing availability of economic opportunities. And this was stated at transcript page 2,737. For example, there are a finite number of existing houses requiring an insulation upgrade to Power Smart levels. And once completed, pushing to increase attic insulation from R50 to R60 is not economic and, in many cases, not feasible. And this was discussed at transcript pages 2,777 to 2,778.

Manitoba Hydro agrees that new technologies and evolutions of energy-efficient technologies can be expected in the future. Manitoba Hydro reviews and incorporates these technologies into its DSM plan as they become available.

Manitoba Hydro's fifteen (15) year DSM plan is, however, focussed on technologies that are available today, not what may or may not be available in the future. As such, Manitoba Hydro acknowledges its DSM plan may be conservative in the distant future when more economic opportunities will likely become available.

CAC expressed concern with their proposed future rate increases and Manitoba Hydro's declining future targets. It argued that customers will not have access to DSM programming to assist with managing their energy bills, particularly customers with electric heat or with restricted homes -- incomes. And this was at transcript page 207 to 208.

Manitoba Hydro recognizes CAC's concern. This is why Manitoba Hydro launched the Low Income Energy Efficiency Program. Mr. Williams criticized this program and pointed to Mr. Dunsky's testimony on social equity being an important consideration in DSM programming. And I'm quoting Mr. -- page 38 of Mr. Williams's final argument.

"There are certain types of programs that you know by their very nature -- excuse me, low income customers are not going to be able to participate and it's very important from an equity standpoint that you offer a

specific program to address the
unique needs and barriers of that
customer's segment. That's the
equity portion."

And this was a quote Mr. Williams used that was made by Mr. Dunsky at transcript page 4,160.

What Mr. Williams selectively failed to include was the next sentence of the quote in which Mr. Dunksy states:

"And Manitoba Hydro does that already
with its low income program."

Mr. Williams's concerns are clearly misplaced and does not -- and is not supported by his own witness. As with all initiatives, this program continues to evolve as we strive to increase awareness and participation.

As Ms. Morrison testified to in her discussion with Mr. Peters, Manitoba Hydro recently announced a neighbourhood approach, which is also noted in Tab 36 of PUB Exhibit 14, as part of the low income initiative.

Manitoba Hydro is working with local neighbourhood development organizations, going door-to-door to speak to energy efficiency opportunities specifically targeted. The goal is to identify opportunities for those eligible for the Low Income Energy Efficiency Program and promote other Power Smart programs such as PAYS and home insulation for those not qualifying for free insulation upgrades.

Ms. Morrison also spoke at length about Manitoba Hydro working directly with the First Nation band housing coordinators. The First Nations communities, which are primar -- primarily electrically heated, are also realizing improvements in -- to the insulation levels of their older homes at not cost through Manitoba Hydro's First Nation Energy Efficiency Program.

For those customers with electric heat but not qualifying as low income or residing within a First Nation community, Manitoba Hydro also continues to offer the Power Smart Home Insulation Program which offers significant rebates which contribute a substantial portion of the cost of the improved insulation.

Manitoba Hydro also offers assistance through the Power Smart residential loan. As also discussed, Manitoba Hydro offers a number of ongoing programs which CAC's own witness, Mr. Dunksy, confirmed are not limited by income constraints, such as Manitoba Hydro's fridge retirement program and free water energy saver package.

Now I'm turning to slide 94. CAC argued that one of Mr. Dunksy's main messages was the importance of sales. When speaking to what is required to bring the plan a much higher level Mr. Dunksy states:

"The first is sales, sales, sales. You've got to go out there and sell and market and sell hard and put feet on the ground. What it is: sales is the first thing."

Manitoba Hydro agrees with Mr. Dunsky that sales are an -- are an important component of a successful DSM approach. As Ms. Morrison testified at transcript page 2,752 and 2,774, Manitoba Hydro has a specialized Power Smart sales group which focusses on key commercial sectors, such as property management hospitality. And Power Smart is a key component of our key and major account representatives and our energy service advisors serving customers across the province with a focus on commercial and industrial customers.

Residential customers are reached through a variety of sales strategies, including some offerings door-to-door in targeted areas, such as the Water & Energy Saver Program.

The sales strategy is a component of the overall design and supported by the business case. As Ms. Morrison testified at transcript page 2,781, going door-to-door to every single household in Manitoba would be cost prohibitive.

All of these initiatives have been and continue to be available to address rising energy, particularly for the groups Mr. Williams identified as having little or no opportunity to reduce their consumption.

Manitoba Hydro's programs are designed and delivered with the objective ach -- of achieving market acceptance and adoption. Manitoba Hydro would also point out that Mr. Dunsky is the perfect example of the challenge we face in encouraging customers to participate in energy efficiency, and this is not a criticism at all. But as noted on page 4,281 of his testimony he, a self-professed twenty (20) year advocate of energy efficiency, only recently upgraded the insulation and heating systems in his home. And this is -- this perfectly reflects some of the challenges that we face.

Moving on to slide 95. Both CAC and GAC advocated the PUB allocating monies, or a portion of the rate increases, to DSM. As you are aware, Manitoba

Hydro's rates for services are regulated by the Public Utilities Board, pursuant to the Accountability Act, which legislation serves to define the PUB's powers.

In the case of Manitoba Keewatinowi Okimakanak versus the Manitoba Hydro Electric Board, and this is a 1992 Manitoba Hydro Court of Appeal case, the Court of Appeal was providing the opportunity to interpret the Accountability Act, in particular, the issue of whether the PUB could compel Manitoba Hydro to expend funds for a particular purpose; in that case, to improve service in diesel communities. The answer was a very clear no.

The Court of Appeal stated that:

> "It must be emphasized at the outset that the jurisdiction of the Board is expressly limited to the fixing of rates. Section 26(1) of the Accountability Acts -- Act makes it clear that rates for service, in the case of Manitoba Hydro, simply means the price charged by that Corporation with respect to the provision of power."

The court concluded that the PUB did not have jurisdiction to direct Manitoba Hydro to expend monies on capital projects, as that would be requiring -- as would be required to improve the level of service in diesel communities.

The identical logic applies with respect to the request that the PUB direct a portion of the rate increase be applied to expend monies on DSM, or to contribute to the Affordable Energy Fund for that same purpose.

Dealing specifically with Mr. Williams' suggestion regarding finding a mechanism within the PUB's jurisdiction to free up some funds for a targeted purpose for DSM, as already noted, this is attempting to do through the back door that which cannot be accomplished -- accomplished through the front door. Manitoba Hydro located a number of cases where this principle is accepted by the courts without the need for debate, and if interested, these can be provided on request.

Green Action Centre recommended, at transcript page 5,745 that the PUB set targets for Manitoba Hydro, require Manitoba Hydro to increase its efficiency investments and achievements to reach the 90th percentile of North American jurisdictions, and direct Manitoba Hydro to abandon the use of the RIM test in program design or screening.

Manitoba Hydro notes that the government enacted legis -- legislation to deal with the specific issue of energy savings. The Energy Savings Act received royal assent in June of 2012. Under this act, the legislature has specifically directed that Manitoba Hydro develop an energy efficiency plan in consultation with the Minister responsible for Manitoba Hydro.

And I'm now on slide 96. Pursuant to section 7(2) of the Energy Savings Act, DSM targets, and a strategy for achieving those targets, will be established as part of that consultation process. The recommendations being made by Green Action Centre are already under the purview of this new legislation. Ms. Morrison testified to this new consultation step in the DSM planning process on page 2743 of the transcript.

Moving now to 597. In summary, Manitoba Hydro is confident its DSM approach is appropriate, and in the best interests of its customers. The Corporation continues to pursue all economic DSM opportunities, and intends to do so into the foreseeable future. Manitoba Hydro takes into account the total cost of DSM opportunities, and assesses the economics of individual DSM opportunities on their own merit.

To assist in the various DSM decision-making processes, Manitoba Hydro uses a number of me -- metrics to guide those decisions. This approach recognizes the benefits to both the Utility and the participating customer, acknowledging that the customer can realize a significant return by participating in DSM opportunities.

Manitoba Hydro would argue that this approach is appropriate and that for the Utility to invest in energy efficiency with no consideration to the possible impact to the ratepayer, assuming that the regulator will keep the Utility whole, would be irresponsible on the part of the Utility.

Manitoba Hydro's targets are reassessed every year, and these targets are based upon achievable and identifiable economic market opp -- opportunities. Manitoba Hydro recognizes the diminishing availability of economic energy efficiency opportunities with existing technologies, and the Corporation is continuously searching for new opportunities, as well as increased participation within existing targeted opportunities.

Manitoba Hydro shares the view that it is important to establish aggressive DSM targets. However, the Corporation is mindful that it is just as important, if not more important, to establish realistic economic DSM targets based on sound business practices and identifiable opportunities.

I'm now moving on to the topic of fuel switching in slide 99. Manitoba Hydro recognizes that there are benefits when customers use natural gas for space heating, and under some instances water heating, from the customer, utility, and global environmental asp -- perspective.

Manitoba Hydro believes that if customers are well informed, they will make the best choice for their situation. To aid customers in making informed decisions, Manitoba Hydro has initiated a heating education campaign to enhance customers' awareness of factors relevant to their decisions on space and water heating.

The campaign includes a multifaceted approach targeting homeowners, HVAC suppliers and installers, home builders, commercial builders, and property developers. Manitoba Hydro would argue that we are already using similar marketing-related tools as used to promote DSM initiatives by offering an aggressive, targeted education campaign, and convenient on-meter financing.

The use of an education campaign is more direct, targeting specifically those customers in gas-available areas, and are much clearer for customers to understand and act upon than any rate design intervention options, which under current legislation cannot differentiate between customers across Manitoba. Manitoba Hydro plans to continue monitoring the impact of its educational campaign, and further consideration may be given to using additional intervention -- intervention tools if warranted.

I'm now briefly going to touch upon the issue of residential inverted rates, which starts at slide 101. Green Action Centre continues to encourage Manitoba Hydro and the PUB to move towards inverted residential rates as a means of sending an appropriate price signal and encouraging conservation.

Manitoba Hydro agrees that, in principle, inverted residential rates with a tail block, and that is the last increment of energy based on marginal costs, provides an efficient price signal. Manitoba Hydro's current application before the Board does not request inverted residential rates or otherwise include them within its scope.

In its response to PUB/Manitoba Hydro Second Round 102A, Manitoba Hydro provides a high-level response to a question about alternatives which could be considered in implementing a residential inverted rate while minimizing adverse impacts on electric heat customers.

In light of the foregoing, Manitoba Hydro takes the position that residential inverted rates continue to be a subject of interest but that the development of an inverted rate proposal is not a matter of urgency. Manitoba Hydro is open to enter into dialogue with interested Intervenors on this subject but not until such time as there has been a resolution of the more immediate issues which have been deferred from this current proceeding. And that is the cost of service study and the time of use rates.

I'm now moving on to the area of electronic spreadsheets, which is at slide 103. In 2006, Manitoba Hydro implemented the practice of making available its regulatory submissions electronically in PDF format on the Corporation's website. This step was well received by both the PUB and Intervenors and, for the most part, has worked very well in achieving some regulatory efficiencies.

In the current proceeding, Manitoba Hydro took us -- took the step of providing electronic Excel spreadsheets in its response to a number of IRs. And those IRs are listed at -- at slide 103.

Manitoba Hydro was able to provide these particular electronic spreadsheets because they contained data only, no formulas, and were not subject to concerns of complexity, commercial sensitivity, or proprietary interest. Manitoba Hydro outlined the considerations it made when determining whether to place information in a live spreadsheet format as opposed to a PDF format on the public record in its response to GAC/Manitoba Hydro First Round 3A.

I'm now moved on to slide 104. Manitoba Hydro is concerned with the potentially significant amount of time and effort that would be required to prepare models to be placed in the public domain to educate other parties in the use of these models and to verify alternative scenarios developed by third parties using the models.

Manitoba Hydro is also concerned that some of these models contain commercially sensitive information and that the provision of certain models may potentially infringe on third-party proprietary rights over those models. Where these concerns do not exist or can reasonably be addressed, Manitoba Hydro will provide the information requested av we -- as we have in this hearing.

I would like to deal with some of the concerns raised by GAC. At transcript page 3,956, Mr.

Chernick asserts that not having access to Manitoba Hydro's proof of revenue models in Excel format is problematic because the data underlying the revenue calculations has not been provided, including number of customers, number of bills, and number of kilowatt hours billed.

To the contrary, Manitoba Hydro notes that it provided billing determinate -- determinant information for all customer classes in response to MIPUG/Manitoba Hydro First Round 20A and B and also provided the billing units, charges and revenues for the time of use rate proposals in response to GAC/Manitoba Hydro's Second Round 30A. This material demonstrates how Manitoba Hydro calculated the anticipated revenues at proposed rates for each of its customer classes.

I'm now on to slide 105. Through the interrogatory process, Manitoba Hydro received -- receives requests to run specific scenarios using its models, changing the assumptions as requested, and providing updated results for all parties to examine. This process of review has served us well. It av -- it avoids confidentiality issues, it avoids incurring the expense of recreating models to remove metadata, it avoids the time and expense of educating third parties on how to use the model perhaps for a one (1) time use only, and it avoids Manitoba Hydro having to verify the results of third-party analysis.

Manitoba Hydro does not understand Mr. Chernick's concern that the current process requires he disclose his work product. We're talking about running different scenarios on Manitoba Hydro's models. If that exposes an issue or, alternatively, confirms no concerns exists, we're not sure why it concerns Mr. Chernick that Manitoba Hydro recognize the area of concern at the discovery stage as opposed to waiting for Intervenor evidence.

Manitoba Hydro is of the view that an understanding of Intervenor positions at the time of the Information Requests provide for -- provides for a more efficient and meaningful examination of alternative scenarios that may be proposed by Intervenors.

Mr. Chernick also suggests that parties need access to Manitoba Hydro's Excel spreadsheets in order to verify consti -- consistency among assumptions and to identify any mistakes or conceptual problems in the analysis. This assertion takes us to the larger question of: What is the appropriate role of Intervenors and their witnesses?

Manitoba Hydro believes that the Intervenors' role is to test the reasonableness of its rate's proposals and to challenge the Corporation's thinking in an effort to ensure that the end product reflects the public interest. In Manitoba Hydro's opinion, the public interest is not served by paying external consultants to audit the work of Manitoba Hydro employees. This is duplicative and expensive.

Quite frankly, Manitoba Hydro questions whether the public interest is properly served to have consultants pore over the level of detail provided in this application - for example, hourly market pricing for each and every hour for a six (6) year period representing eight thousand, seven hundred and sixty-one (8,761) data points to confirm Excel averaged them correctly. That is not a good use of ratepayer funds.

I will now turn the mic over to Ms. Ramage to bring it home.

MS. PATTI RAMAGE: That's exactly it. Not much longer. Two (2) quick -- a couple of quick points, and -- and we can move on and enjoy the Jets game.

Mani -- the PUB received a number of written presentations. And here I'm dealing at slide 107. And those written presentations dealt with

Manitoba Hydro's rate application. In addition to three (3) oral pres -- in addition, three (3) oral presentations were delivered during the hearing, the MIPUG group of presenters, Mr. Ciekiewicz and Mr. Stokke.

Under the rules of natural justice, as well as the PUB's own rules of practice and pre -- procedure, presentations are not evidence. There is no requirement to pre-file materials. Presenters are not sworn. And the information presented is not subject to the usual discovery process or the rigours of cross-examination.

Presentations have the potential to provide the PUB and Manitoba Hydro insights into the ratepayer's ability to manage a rate increase, as well as valuable feedback on the public's perceptions of a rate proposal, does the public understand what is dri -- driving the proposal and is there opposition reasonable in the circumstance.

This is valuable information when assessing whether a rate increase is in the public interest. Presentations, however, are not intended to be technical in nature. For good reason, technical information must be tested through the processes set out in the rules of practice and procedure. And to such -- and to such extent a presentation puts technical information before this Board, it can't be relied on as evidence.

The presentation made by Mr. Stokke did not purport to address Manitoba Hydro's rate proposal. Rather Mr. Stokke's presentation challenges the determination of Manitoba Hydro's engineers charged with responsibility for dam safety in a discussion which goes well beyond the parameters of a presentation before this Board, both in that it is very technical in nature and that its subject matter -- matter falls outside the parameters of a GRA.

Having said this, Mr. Stokke's comments are on the public record. And in the circumstance, Manitoba Hydro believes it important that the Board understand that expenditures of this magnitude are always carefully examined by Manitoba Hydro and are never undertaken lightly.

As described in Manitoba Hydro's response to PUB/Manitoba Hydro pre-ask 21, Manitoba Hydro engaged in an extensive process encompany -- encompany -- encompassing assessment, planning, evaluation, design, consultation and obtaining required environmental and regulatory authorizations prior to making the decision to proceed with the spillway replacement project.

Following the acquisition of Point du Bois in 2002, Manitoba Hydro assessed long-term planning options for the Point du Bois generating station. It was determined that despite extensive repairs and upgrades over the years, major repair or replacement was required to maintain public and dam safety consistent with the Canadian Dam Association dam safety guidelines so as to provide a safer work environment for staff and to ensure reliable power production.

The decision was not made lightly and its justification was certainly not based on the letter of Manitoba Hydro's integrity officer, which is not, as Mr. Stokke describes it at transcript page 566, the Corporation's dam safety report.

Manitoba Hydro has listened to and considered the concerns raised by Mr. Stokke and found no basis on which to alter any of its plans and actions related to the spillway replacement project.

A formal response outlining the investigation and addressing Mr. Stokke's concerns was provided to him in a letter dated April 26, 2012, from Manitoba Hydro's integrity officer. That's the one I had just referenced.

In the interest of transparency, Manitoba Hydro provided additional information on the Point du Bois site through its responses to PUB Pre-ask 1 through 23, which materials made up an additional binder of materials.

Manitoba Hydro has made the decision to proceed with the spillway replacement project. And the decision for rebuilding the powerhouse has been deferred, demonstrating a balance between a commitment to employee, public and dam safety and the need to be fiscally responsible.

Manitoba Hydro has complied with the processes internal and external to commit to this project. While Manitoba Hydro and the PUB have attempted to be responsive to Mr. Stokke's concerns, the purpose of this hearing is not to review or justify Manitoba Hydro's decision with respect to the Point du Bois spillway.

Turning to slide 110. Before concluding, Manitoba Hydro would like to address the frustration expressed by the chairman regarding the currency of information before the PUB when issuing its orders. On page 739 of the transcript, Mr. Chairman, you posed the question:

"How do we address this so that when

ultimately our Order comes out some
months down the road, it reflects the
most currently available data? I
don't know what the solution, I'm
just presenting a problem that I
think we both have."

Manitoba Hydro acknowledges this frustration, and especially the sensitivity of near-term financial projections to sudden and significant changes in water supply conditions, and other variables during the regulatory process. However, as Mr. Warden testified at transcript page 740, this GRA process was subject to unusual circumstances, and was outside the typical GRA cycle.

Typically, Manitoba Hydro would file for a rate increase, and the hearing would be held during the fall and winter, when water conditions are more stable. Manitoba Hydro would suggest that this problem would be mostly resolved once we're able to return to that typical cycle.

In a normal year, the timing of the GRA submission would occur in late fall, following approval of the IFF by the Board of Manitoba. With this timing, the est -- estimate for net export revenues in the first year is fairly accurate, as it is based, to a large extent, on a combination of actual results and forecast results for the winter season, when the water supply is quite predictable. The IR process, and the actual hearing, would then occur over the winter, when the water supply forecast is more stable, for a rate decision effective April 1st.

However, the timing of this GRA was such that the process commenced in the spring, with the first increase effective September 1st. Although IFF11-2 contained almost full actual results for 2011/'12, water conditions for the second test year were not yet known, and were subject to dramatic variation depending upon spring and summer rainfall, precisely the period during which the filing and IR processes were scheduled.

Manitoba Hydro expected below average inflows for 2012/'13, which added to the magnitude of the variations that occurred over the summer of 2012. Manitoba Hydro had recognized in IFF11-2 that runoff conditions in the spring of 2012, were likely to be below median, due to below average precipitation conditions during the previous winter. So when water supply conditions improved in mid-June to above average, the variation was higher than would normally have been the case had IFF11-2 assumed median inflows for 2012/2013.

The fuel for a predominantly hydroelectric utility is water, which supply is completely weather dependent. Although current water storage conditions are known with confidence, future inflows are weather dependent and, therefore, future hydraulic generation is never fully predictable. Depending on the season, inflows can change dramatically over a short period of time, and this can result in significant changes to Manitoba Hydro's outlook for future hydraulic generation.

Mr. Cormie, in his testimony beginning at transcript page 513, reviewed a chart on page 48 of Manitoba Hydro's Exhibit 15. This chart illustrated the variability of inflows that can occur within the year, and how inflows can change significantly in a matter of days, particularly during the spring and summer seasons.

Outside of the winter months, this variability is mostly due to major storm events which are poss -- impossible to accurately predict beyond a few days into the future. As a result, water supply uncertainty is greatest during the spring and summer seasons, less so in the fall, and least uncertain in the winter.

The chart also illustrates the unforeseen improvement to inflow conditions following the April -- following April 2012. It was at this time when Manitoba Hydro made its filing without accurately knowing in advance what the supply conditions would be for the balance of the year.

As indicated by the jump in the red line near the end of April on page 48 of Manitoba Hydro's Exhibit 15, conditions were rapidly changing. In order to reflect that improvement in the water supply, and recognizing that insufficient time was available to undertake a complete analysis, Manitoba Hydro chose to apply a forecast adjustment to export revenues and fuel and power purchases in order to provide the more up-to-date information in IFF11-2.

This adjustment also accounted for anticipated expenses to export transactions that were significantly above MISO market price, which was expl -- which is -- was explained on page 4,922 of the transcripts. Subsequently, additional improvements in water supply occurred, which ultimately ref -- were reflected in IFF12, which was filed after it was approved by the Manitoba Hydro Board of Directors.

We're at slide 111 now. Although Manitoba Hydro uses the most current information available in its General Rate Applications, conditions will change during the period of the regulatory process. For this reason, Manitoba Hydro updates the Board with its quarterly reports, and provides an update on water supply and other conditions in its direct testimony.

Manitoba Hydro attempts to provide the PUB with all the information necessary upon which to make its decision; however, we remind the Board that Manitoba Hydro sets rates based on the long-term view, and that both favourable and unfavourable variations will occur in the regulatory time frame.

Over time, these will tend to offset each other with only limited long-term rate impacts. As a result, Manitoba Hydro would suggest that this issue is -- is more one that effects the efficiency of the regulatory process and less an issue of rates. As stated previously, to the extent that we return to the typical GRA cycle, this issue should largely resolve itself.

And at slide 113. Betch ya were never so happy to see the word 'conclusion'.

MR. RAYMOND LAFOND: That's the one we were looking for.

MS. PATTI RAMAGE: Mr. Chairman and

members of the PUB, Manitoba Hydro submits that the facts that have been presented during this GRA proceeding clearly demonstrate that final approval of the requested rate increases and reinstatement of the 1 percent rate rollback are required to maintain net income and financial ratios during the 2012/'13 and 2013/'14 test years at acceptable levels, to preserve the financial integrity of the Corporation for the period covered by this application, and to promote rate stability for customers by avoiding the need for larger or sudden rate increases in the future.

Despite the significant reduction in the financial outlook and -- and projected financial ratios that are lower than target levels, Manitoba Hydro is proposing to maintain the rate increase request at the 3.5 percent level previously forecast for 2012/'13 and 2013/'14 to achieve the appropriate balance between customer sensitivity and financial integrity.

The proposed rate increases strike the delicate balance between financial integrity and customer sensitivity that Mr. Warden spoke of a number of times during the hearing.

After a detailed review of the Application over the twenty-one (21) days of public hearings, the reasons for the requested rate increases and the reinstatement of the 1 percent rate rollback remain valid.

No Intervenor to the proceeding has provided an alternate credible view, or seriously challenged the reasons that have been articulated by Manitoba Hydro as to the need for the rate increases. As such, Manitoba Hydro is requesting that the PUB grant the rate -- rate relief that is requested in this application in full.

One last comment about the timing of the PUB's rate decision. As the PUB is aware, Manitoba Hydro's year end of March 31st, 2013, is fast approaching. Manitoba Hydro requires the PUB's decision on the 1 percent rate rollback reinstatement and the interim rate increases in a timely fashion in order to close its books and determine its net income for the 2012/'13 fiscal year. As such, Manitoba Hydro is respectfully requesting that the PUB render its decisions on the rate application in advance of March 31st, 2013.

Mr. Chairman, Board Member Lafond, Board Member Soldier, that concludes Manitoba Hydro's final submission in this matter. At the beginning of this process we invited to the -- the PUB to stop us, and ask questions at any point if you wanted to hear more on a particular topic. You took us up on that topic -- or on that offer, and we want to thank you for your interest. We think it's made for a better hearing.

We also appreciate the positive working relationship we have with Mr. Singh and Mr. Simonsen, and the work they do to make these hearings go smoothly. Mr. Peters, Ms. Southall, Mr. Cathcart, and Mr. Buhr have also contributed to the smooth running of the hearing.

And we'd also like to thank the Intervenors for their contributions to the proce -- process. Just the fact that we know that our decisions are going to be probed by this group makes us really think how to best achieve the optimum balance between the various interests that compro -- that comprise the public interest.

So finally, I'd like to thank the Manitoba Hydro staff who worked night and day to answer infor -- to answer Information Requests during the early stages of this process, and undertakings once the hearing began. It's a huge undertaking, and we couldn't pull it off without the commitment of dedicated staff, staff that largely go unrecognized whether they're in the back room or back at the office.

And for our front row, this is the end

of an era. I'm going into my 20th year of participating at rate hearings, and I believe this was my first final argument without Mr. Warden at my side. He has dedicated his entire career to Manitoba Hydro, and ratepayers are no doubt the better for it. We will miss both his knowledge and his insight. He has set the bar high.

I'm confident that he has taught us well and that we'll be able to catch the -- carry the torch forward. Yesterday was his last day. I think he was disappointed that he wasn't going to be here today.

And, Vince, I know you won't be able to resist reading the transcript of Manitoba Hydro's final submission, so I want to use this opportunity to once again wish you and Cheryl all the best in your retirement.

Thank you, Mr. Chairman, Mr. Soldier, Mr. Lafond.

THE CHAIRPERSON: I think for the record we should acknowledge Mr. Warden's contribution to the deliberations of this panel and the previous panels that have heard the applications of Manitoba Hydro. So he's made a significant contribution. I think the record should acknowledge that contribution.

Before we adjourn, I just want to

confirm that there are no other questions from my panel members.

MR. RAYMOND LAFOND: I -- I guess it's a comment and a very brief question at the end that only requires a "yes" or a "no".

MS. PATTI RAMAGE: I object.

MR. RAYMOND LAFOND: At many times throughout the day in your presentation, slide 15, slide 37 through the DSM program talking about export market prices and its influence, I mean, export markets are significant, and I look at the IFF12 and it shows that the -- the projection over the next twenty (20) years is an increase by 400 percent. And yet, yesterday I read in the Globe and Mail, and I'll cite this:

> "Research by the National Bank Financial asserts that Canada's electricity exports are expected to fall sharply with the rise of US production from gas-powered thermal plants and renewable -- and renewable power generation."

And then it goes on -- and the article goes on:

> "After revising its forecast, the US

Department of Energy believes that 2012 was the peak year for electricity import. It predicts volume electricity imports will fall 44 percent by 2030 with the steepest drop in coming years."

My only question is: Is Manitoba Hydro aware of these two (2) reports?

(BRIEF PAUSE)

MS. PATTI RAMAGE: Yes.

MR. RAYMOND LAFOND: Thank you, thank you.

THE CHAIRPERSON: Just to let you know that I've conferred with the fellow members of the panel and decided that there's not much point in having Ms. Fernandes prepare a written presentation because we can read the transcript tomorrow, so I'll save you the work of having to do the -- the presentation, although it would probably have been useful if we'd had it today.

I -- I do want to acknowledge the -- the -- the extensive amount of work that has gone into this particular rate application, and I'm citing -- I think

I'm correctly citing, Ms. Ramage, two hun -- two thousand two hundred and twenty-eight (2,228) IRs; is that right?

MS. PATTI RAMAGE: I believe that's correct. Two thousand one hundred and forty-eight (2,148).

THE CHAIRPERSON: A hundred and forty-eight. A hundred and eighteen exhibits, seventy-nine (79) undertakings, twenty-one (21) days of hearings, so thank you to the Manitoba Hydro witnesses, the backroom staff, and all the people back at the office who have contributed to the application, the IRs, and the pre-asks. It's very much appreciated.

I also want to acknowledge the contribution of the CAC, Ms. Desorcy and counsel, Mr. Williams, and the consultants that appeared on behalf of CAC.

Also acknowledge GAC and Professor Miller and Mr. Gange and -- and the consultants appearing on their behalf.

MIPUG, Maitre Hacault, and the consultant Mr. Bowman.

Of course, the people working on behalf of Digi-Tran, who prepare the -- the transcripts.

And of course, finally, the PUB staff

and Mr. Hollis Singh and Mr. Kurt Simonsen as well as the admin staff and also the advisors who capably serve this panel. Mr. Peters, Mr. Cathcart, Mr. Buhr, thank you very much for your contribution.

And finally, I think we should acknowledge the participation of the presenters who -- who took advantage of the opportunity that citizens have to appear before this panel to -- to share their views about the evolution of utilities and their views about the actions of utilities. So those are very much appreciated, and it's freedom that's available to citizens and I think it's one we need to respect. So I wish to acknowledge their contribution.

So thank you, all. And all the best. We will endeavour to try to deliver a decision as promptly and as capably as possible. Thank you very much.

--- Upon adjourning at 3:46 p.m.

Certified Correct,

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Cheryl Lavigne, Ms.

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