MANITOBA PUBLIC UTILITIES BOARD

Re: MANITOBA HYDRO

GENERAL RATE APPLICATION

2014/15 AND 2015/16

Before Board Panel:

Regis Gosselin - Board Chairperson

Marilyn Kapitany - Board Member

Richard Bel - Board Member

Hugh Grant - Board Member

HELD AT:

Public Utilities Board

400, 330 Portage Avenue

Winnipeg, Manitoba

June 11, 2015

Pages 3406 to 3640

1 APPEARANCES

2	Bob Peters	(np)	)Board Counsel
3	Sven Hombach		)
4			
5	Odette Fernandes		)Manitoba Hydro
6	Brent Czarnecki	(np)	)
7	Helga Van Iderstine		)
8			
9	Byron Williams		)Consumer Coalition
10	Meghan Menzies	(np)	)
11	Jared Wheeler	(np)	)
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13	William Gange	(np)	)GAC
14	Peter Miller	(np)	)
15	David Cordingley		)
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17	Antoine Hacault		)MIPUG
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19	Michael Anderson	(np)	)MKO
20	George Orle		)
21			
22	Tomas Masi		)MMF
23	Kris Saxberg	(np)	)
24			
25	Denise Pambrun	(np)	)City of Winnipeg

TABLE OF CONTENTS

LIST OF EXHIBITS

UNDERTAKINGS

UNDERTAKINGS (Con't)

NO.	DESCRIPTION	PAGE NO.
76	Manitoba Hydro to provide two (2) asset sub-ledgers as a result of negative salvage as well as two (2) asset sub-ledgers as a result of keeping with Canadian GAAP	3595
77	Manitoba Hydro to provide what the balance of the deferral account would be after the forty (40) year period	3638

1 --- Upon commencing at 9:00 a.m.

2

3 THE CHAIRPERSON: Good morning. I
4 believe that we can start today's proceedings, so
5 welcome to everyone that's participating today. Before
6 we start the proceedings, I do have a -- a request that
7 I would like to make of Manitoba Hydro on behalf of the
8 Board.
9 The Board would like to obtain a better
10 understanding of the impact of deviations from Manitoba
11 Hydro's requested 3.95 percent rate increase in either
12 direction. On slide 58 of Manitoba Hydro's finance
13 panel presentation, the Board provided a -- a number of
14 scenarios, including a no-rate increase scenario, a 2
15 percent scenario, and a 2 percent until 2019 scenario
16 with 3.95 percent rate increases thereafter.
17 By way of answers to PUB Information
18 Request I-7, Manitoba Hydro also provided a no-loss
19 scenario at 5.3 percent, and a scenario by which the
20 propo -- the projected losses would be cut in half at
21 4.44 percent.
22 These data were helpful to the Board,
23 but in order to further understand the sensitivity of
24 Manitoba Hydro's plan to different rate scenarios, the
25 Board would like three (3) additional scenarios to be

1 modelled. Specifically, the Board would appreciate a
2 twenty (20) year IFF -- pardon me, would appreciate
3 twenty (20) year IFFs for the following rate scenarios,
4 with such rate increases being applied to all years of
5 the IFF: firstly, 3.5 percent; secondly, 3.75 percent;
6 and thirdly, 4.25 percent.
7 The IFFs should include Manitoba Hydro's
8 financial targets for each of the years. The Board
9 also requests bill impacts for these scenarios, as well
10 as for the 4.44 percent and 5.3 percent scenarios for
11 which IFFs have already been filed.
12 Can this, please, be provided by way of
13 undertaking to the Board?
14 MS. ODETTE FERNANDES: Good morning,
15 Mr. Chairman. Yes, we can.
16
17 --- UNDERTAKING NO. 73: Manitoba Hydro to provide
18 twenty (20) year IFFs with
19 rate increases being
20 applied to all years of 3.5
21 percent, 3.75 percent, and
22 4.25 percent, including
23 Manitoba Hydro's financial
24 targets for each of the
25 years and bill impacts for

these scenarios, as well as for the 4.44 percent and 5.3 percent scenarios for which IFFs have already been filed

THE CHAIRPERSON: We'll just put Manitoba Hydro on -- on notice that there may be an additional request coming after the break this morning in relation to -- to the 3.95 percent rate increase, specifically the portion of that increase that would be attributable to operating costs and the portion that would be attributable to future investment.

So in other words, 3.95 percent going forward for the next three (3) years, how much of that is attributable -- is attributable to the operating costs of the Corporation versus that portion which would be basically set aside for the future investments in Keeyask and Bipole and so on going forward?

So I'll formulate something more formal, and we'll have something to you at lunchtime. But perhaps in the meantime, you could signal to the -- to the staff that this is something we're looking for, and if you have any questions, I'd be pleased to respond to them.

1 MR. SVEN HOMBACH: Mr. Chairman, before
2 we call on Manitoba Hydro's panel this morning, I'd
3 like to advise all the parties in the room that
4 Patricia Lee, who is scheduled to testify on Monday, is
5 joining us by teleconference and was -- is listening in
6 to the testimony today. Thank you.
7 THE CHAIRPERSON: So with that, I'll
8 turn over the microphone to you.
9 MS. HELGA VAN IDERSTINE: Thank you
10 very much. Just to remind you, since I haven't been
11 here in this hearing, my name's Helga Van Iderstine.
12 I'm external counsel to Manitoba Hydro, and I'm a
13 lawyer at Aikins, MacAulay & Thorvaldson.
14 So I'd like you -- to introduce you now
15 to the depreciation panel. I believe you already know
16 Mr. Darren Rainkie, who's the vice president of Finance
17 and Regulatory. His CV has previously been filed as
18 Exhibit 32.
19 Next to him in Sandy Bauerlein. She's
20 the corporate controller. She's already been sworn as
21 well, and her CV is at Exhibit 36.
22 Next to her is Michelle Hooper. We have
23 circulated her CV, and if we could have her CV marked
24 as Exhibit 74, we'll start thing -- the proceedings.
25 MR. KURT SIMONSEN: So noted. Thank

you.

--- EXHIBIT NO. MH-74: CV of Michelle Hooper

MANITOBA HYDRO PANEL 7 - DEPRECIATION:

DARREN RAINKIE, Previously Sworn

SANDY BAUERLEIN, Previously Sworn

MS. HELGA VAN IDERSTINE: And as Ms. Hooper has not previously testified, I'd like to take a few minutes to go through her CV briefly.

So, Ms. Hooper, first of all, I understand that you graduated from Brandon University in 1991 with a bachelor of science degree.

Is that right?

MS. MICHELLE HOOPER: Yes, that is correct.

MS. HELGA VAN IDERSTINE: And that was in mathematics?

MS. MICHELLE HOOPER: Yes.

MS. HELGA VAN IDERSTINE: And you followed with getting -- obtaining your designation as a chartered accountant in 1995.

Is that right?

MS. MICHELLE HOOPER: Yes. I'm just

1 having a little trouble with the mic. Yes, I obtained
2 my designation as a chartered accountant in 1995.
3 MS. HELGA VAN IDERSTINE: And after
4 that, you worked initially for a private accounting
5 firm, and thereafter, in 1996, joined Manitoba Hydro.
6 Is that right?
7 MS. MICHELLE HOOPER: Yes, that is
8 correct.
9 MS. HELGA VAN IDERSTINE: And since you
10 started with Manitoba Hydro, I understand you've been
11 working in the accounting department generally?
12 MS. MICHELLE HOOPER: Yes. I've been
13 working in accounting in a number of different areas
14 within the Corporation.
15 MS. HELGA VAN IDERSTINE: And I'm not
16 going to go through each of your positions, but
17 starting in 2007, I understand you were the financial
18 systems supervisor.
19 And if you could tell us what that
20 involved?
21 MS. MICHELLE HOOPER: In my role as
22 financial systems supervisor for management accounting
23 and reporting department within Manitoba Hydro, I was
24 responsible for overseeing a team of individuals who
25 looked after the ongoing monthly systems and processes

1 that supported the accounting functions of the
2 Corporation, so month-end processing, maintenance of
3 cost-allocation processes, overhead pools, that sort of
4 thing.
5 MS. HELGA VAN IDERSTINE: And in 2009,
6 you became a senior analyst, IFRS conversion project.
7 Can you tell us what that involved?
8 MS. MICHELLE HOOPER: Yes. As a senior
9 analyst for the IFRS conversion project, I initially
10 did a little bit of work with respect to the impacts of
11 O&A costs and the effects of IFRS, and then moved over
12 to analyzing the impacts of IFRS on property, plant,
13 and equipment at Manitoba Hydro.
14 MS. HELGA VAN IDERSTINE: As of 2014, I
15 understand you've now got a new position as asset
16 accounting project supervisor.
17 And can you tell us what that involves?
18 MS. MICHELLE HOOPER: That position
19 involves overseeing a team of individuals responsible
20 for implementing the changes resulting from
21 depreciation studies, for implementing changes
22 resulting from IFRS, and generally looking after
23 projects, special projects related to asset accounting,
24 such as depreciation studies.
25 MS. HELGA VAN IDERSTINE: So just to

1 follow up on that, can you tell us a little bit about -
2 - more about what -- your involvement with the
3 depreciation studies and that part of your job has
4 involved?
5 MS. MICHELLE HOOPER: Certainly. I
6 have been involved with both the 2010 and 2014
7 depreciation studies for Manitoba Hydro. And my role
8 in -- in that was preparing and overseeing the
9 preparation of all of the data submissions to Gannett
10 Fleming for those depreciation studies; also,
11 facilitating discussions with Gannett Fleming and
12 Manitoba Hydro's operational and engineering staff as
13 it pertains to depreciation studies and understanding
14 asset lives, asset expectancies -- or life
15 expectancies, impacts of changing technology and
16 changing business of Manitoba Hydro on those assets.
17 I also reviewed all of the materials
18 received back from Gannett Fleming at the conclusion of
19 the depreciation studies in order to ensure that that
20 material was consistent with our submissions to them.
21 MS. HELGA VAN IDERSTINE: All right.
22 Thank you. Thank you. With that, I'd like to turn to
23 Mr. -- I would ask that she be sworn.
24
25 MICHELLE HOOPER, Sworn

1 MS. HELGA VAN IDERSTINE: And, Mr. --
2 Mr. Simonsen, while you're there, I'm -- I'm going to
3 have -- ask that Mr. Kennedy be sworn in a moment, but
4 I -- I -- we -- we might -- if you don't mind, we could
5 do it now and then I will have him qualified as an
6 expert if that's okay.
7
8 LARRY KENNEDY, Sworn
9
10 MS. HELGA VAN IDERSTINE: So I'll just
11 introduce Mr. Kennedy. Mr. Kennedy is from Gannett
12 Fleming. And Mr. Kennedy is being presented to the
13 Board as an expert in depreciation with the necessary
14 expertise to provide expert evidence in the area of
15 depreciation.
16 And if you don't mind, I'd like to go
17 through his report -- or his -- or identify that his
18 report and CV are attached as Appendix A to the
19 repuddle -- rebuttal evidence of Manitoba Hydro Exhibit
20 29, Appendix A. And if they -- somebody's looking for
21 it on the computer you can find it by tabbing down to
22 Adobe 67 -- page 67, because it's not numbered at the
23 end of that appendix.
24
25 EXAMINATION-IN-CHIEF OF MR. LARRY KENNEDY BY MS. HELGA

VAN IDERSTINE (QUAL.)

MS. HELGA VAN IDERSTINE: So, Mr. Kennedy, you have a diploma in Applied Arts and Business Administration from the Northern Alberta Institute of Technology.

Is that right?

MR. LARRY KENNEDY: That's correct.

MS. HELGA VAN IDERSTINE: You're a member of the Society of Depreciation Professionals and a member of the Certified Depreciation Professionals?

MR. LARRY KENNEDY: I hold a CDP designation, Certified Depreciation Professional designation. I am a member of the Society of Depreciation Professionals and I've served as the President of that Society and as a Board Member of that Society.

MS. HELGA VAN IDERSTINE: And I also understand you've done some academic teaching as well?

MR. LARRY KENNEDY: Yes, I have. The Society of Depreciation Professionals is probably one (1) of the few groups that are still undertaking utility depreciation training and I'm privileged to be part of the teaching faculty of that Society in our annual training sessions.

MS. HELGA VAN IDERSTINE: Now, I

1 understand you joined Gannett Fleming Inc. in January
2 1999 and that Ganning Fleming -- Gannett Fleming,
3 excuse me, is a consulting company focussed on global
4 infrastructure solutions with a focus on planning,
5 design, technology, and construction management
6 services. And this includes providing advice to
7 utilities on rate making.
8 Is that right?
9 MR. LARRY KENNEDY: That is correct.
10 MS. HELGA VAN IDERSTINE: And in those
11 services that are provided, I understand they provide
12 experience in revenue and expense analysis, cost of
13 capital and depreciation claims to ensure that the
14 required revenue levels are achieved?
15 MR. LARRY KENNEDY: That's correct. We
16 also advise clients on certain plant accounting issues
17 as they relate to group and -- and public utility
18 accounting.
19 MS. HELGA VAN IDERSTINE: And I note
20 from your website you say that Gannett Fleming develops
21 customized rate -- customized rate structures to help
22 utilities charge rates that are fair and equitable for
23 all users?
24 MR. LARRY KENNEDY: That is correct.
25 MS. HELGA VAN IDERSTINE: And have you

1 been involved in those serv -- providing those
2 services?
3 MR. LARRY KENNEDY: I have.
4 MS. HELGA VAN IDERSTINE: Now, prior to
5 working at Gannett Fleming, I understand you worked for
6 fifteen (15) years at Interprovincial Pipeline.
7 Can you tell me what you did there?
8 MR. LARRY KENNEDY: Certainly.
9 Interprovincial Pipelines is headquartered in Edmonton.
10 I spent the early part of my career from 1980 through
11 1995 in various roles in their plant accounting and
12 regulatory sections. Ultimately, when I left
13 Interprovincial -- or at that time it was already known
14 as Enbridge, I think, or right about the time of
15 transition -- I was holding the title of team -- team
16 leader of plant accounting and I -- the -- the plant
17 accounting section there, as in many utilities, kind of
18 wavered in and out of the finance section and the
19 regulatory sections. I'm not sure if we ever knew what
20 -- where we belonged. But -- but there seemed to be a
21 big overlap.
22 And so I spent much of my career under
23 the title of finance and much of my career under the
24 title of regulatory there. But it was in the role of
25 team lead of plant accounting which provided me with a

1 fifteen (15) year background in -- in plant accounting
2 and the -- the fun and the issues that go on with --
3 with recording the -- the transactions of utilities.
4 MS. HELGA VAN IDERSTINE: And did that
5 include dealing with depreciation issues?
6 MR. LARRY KENNEDY: It did. Very early
7 in my career there I was provided with the opportunity
8 to -- to lead their depreciation studies that were
9 submitted to the National Energy Board of Canada, both
10 through a -- a practitioner standpoint of doing the
11 studies and also in managing the studies now when we
12 had other experts helping us out.
13 MS. HELGA VAN IDERSTINE: And I've also
14 -- I understand that after you joined Gannett Fleming
15 you've worked as a -- a consultant and done
16 depreciation analysis for Alta Gas Utilities, Alta
17 Link, ATCO, BC Hydro, Enbridge Gas Distribution, Centra
18 Gas Manitoba, amongst others. And these are outlined
19 in your CV.
20 MR. LARRY KENNEDY: That's correct.
21 And the -- we -- we jumped over about a three (3) year
22 term where I was -- had the title of depreciation
23 specialist for NOVA Gas Transmission and then with
24 TransCanada Pipelines when TransCanada and NOVA became
25 one (1). Then -- then I joined my career in 1999 with

1 Gannett Fleming, and where we -- we do studies for at
2 last count about 79 to 80 percent of the Canadian
3 electric and gas utilities which has provided me
4 opportunity to provide testimony in every province and
5 territory in this fine country including the National
6 Energy Board of Canada.
7 MS. HELGA VAN IDERSTINE: So just
8 following up on that you have, as I understand it,
9 provided advice and recommendations on depreciation
10 analysis and that your evidence has been accepted by
11 such utility regulation boards as the Ontario --
12 Ontario Energy Board, Newfoundland, Alberta, BC, Yukon,
13 Northwest Territories, and Manitoba.
14 MR. LARRY KENNEDY: Those are
15 definitely part of the list, yes.
16 MS. HELGA VAN IDERSTINE: In addition
17 to that I understand that you've also provided advice
18 and analysis to US electric utilities?
19 MR. LARRY KENNEDY: Occasionally. I
20 have had the opportunity to -- to provide -- to work
21 with a few US clients. Most of our US clients are
22 handled out of one (1) of our US offices. Our --
23 Gannett Fleming is equally as large in the states as we
24 are in Canada in terms of our -- our market in
25 utilities. And I think by last count we do sightly

1 more than half of the US electric and gas utilities.
2 And I've had an opportunity to work with my US
3 counterparts and take the lead in a few cases on US
4 assignments as well.
5 MS. HELGA VAN IDERSTINE: I also
6 understand that you've presented to utilities on beh --
7 and on behalf of utilities on issues surrounding
8 depreciation and the application and interrelation with
9 IFRS?
10 MR. LARRY KENNEDY: That is correct.
11 And as well as to organizations such as the Canadian
12 Gas Association, the Canadian Electricity Association,
13 amongst others.
14 MS. HELGA VAN IDERSTINE: With that,
15 Mr. Chair, panel members, I'd request that Mr. Kennedy
16 be accepted as an expert in depreciation qualified to
17 comment on the issues and impacts associated with
18 depreciation analysis, recommendations, and
19 implementation as well as the application of it in the
20 IFRS milieu as it applies to utilities as raised in
21 this general rate application and by the Board and
22 Intervenors in their requests for information.
23 THE CHAIRPERSON: Thank you for that,
24 Ms. Van Iderstine. I'll call on Mr. Williams.
25 Do you have any concerns about

1 qualifying Mr. Kennedy as an expert on depreciation?
2 MR. BYRON WILLIAMS: Mr. Chair, we will
3 have some questions, but we'll reserve them -- so not
4 in terms of his qualifications, but we will ask a bit
5 more about his qualifications later in -- in the
6 hearing. We certainly, in terms of the public utility
7 plant depreciation, accept his qualifications. We --
8 we take no position in terms of his ability to comment
9 on IFRS.
10
11 (BRIEF PAUSE)
12
13 THE CHAIRPERSON: Thank you mi -- thank
14 you, Mr. Williams. Me. Hacault, would you comment
15 please on the -- the qualifying of Mr. Kennedy as an --
16 ex -- expert on depreciation?
17
18 CROSS-EXAMINATION OF MR. LARRY KENNEDY BY MR. ANTOINE
19 HACAULT (QUAL.):
20 MR. ANTOINE HACAULT: One (1) or two
21 (2) questions just to make it clear.
22 Mr. Kennedy, you do not have any
23 accounting designation?
24 MR. LARRY KENNEDY: I do not hold an
25 accounting designation.

1 MR. ANTOINE HACAULT: And as far as I
2 can tell from your CV over the last five (5) years,
3 your work has largely been limited to providing advice
4 and counsel to utilities, and appearing at hearings on
5 behalf of utilities.
6 Is that correct?
7 MR. LARRY KENNEDY: Largely, but not
8 totally. I've just recently completed an assignment
9 with the Canadian Transportation Agency, where they --
10 they engaged myself to -- to provide some training and
11 some consulting on the appropriate regulation for
12 railroads in this country.
13 MR. ANTOINE HACAULT: But specifically
14 as regards electric utilities, have your services and
15 your testimony been limited to advocating on behalf of
16 utilities, sir?
17 MR. LARRY KENNEDY: In the last five
18 (5) years, that would be correct. Earlier in my
19 career, I did represent the -- the Intervenor side of
20 the fore, and I have represented at least one (1)
21 Public Utility Board in Canada.
22 MR. ANTOINE HACAULT: I have raised the
23 issues with respect to the lack of accounting
24 expertise, and I'm -- I am concerned about the way it
25 was phrased that it appears that Manitoba Hydro is

1 seeking to have this witness comment on accounting
2 issues. There are well-qualified accountants which
3 could have been brought to deal with accounting issues,
4 and interpretation of IFRS specifically, and no
5 accountants from independent firms have been produced.
6 So I raise that flag with respect to
7 this issue of applying IFRS, as I understood Ms. Van
8 Iderstine's comments.
9 THE CHAIRPERSON: Merci, Me. Hacault.
10 Mr. Orle, please...?
11 MR. GEORGE ORLE: Thank you, Mr.
12 Chairman. We take no position on the qualification,
13 and leave that up to the panel.
14 THE CHAIRPERSON: Thank you for that.
15 Mr. Masi, please...?
16 MR. TOMAS MASI: Mr. Chairman, we take
17 no position as well with respect to his qualifications.
18 MR. KURT SIMONSEN: Mr. Chairman,
19 there's still Mr. Cordingley for GAC.
20 MR. DAVID CORDINGLEY: We take no
21 position either.
22 THE CHAIRPERSON: Thank you for that.
23 The panel will stand down for about -- a few minutes.
24 Thank you.
25

1 --- Upon recessing at 9:20 a.m.
2 --- Upon resuming at 9:28 a.m.
3
4 RULING RE. MR. LARRY KENNEDY (QUAL.):
5 THE CHAIRPERSON: So the panel has
6 deliberated -- deliberated and come to the conclusion
7 that they will accept Mr. Kennedy as an expert on
8 depreciation, but acknowledges that he is not an expert
9 on IFRS, nor on the accounting policy in relation to
10 the requirements of IFRS.
11 So with that, I will turn the microphone
12 over -- back to Ms. Van Iderstine.
13 MS. HELGA VAN IDERSTINE: Thank you.
14 So with that, we are ready to present the evidence.
15 You will have, or I have hope you've been provided with
16 and I see the -- it's on the screen, the first page of
17 the depreciation panel's presentation. I would like to
18 have that marked as the next exhibit, Exhibit 75.
19 MR. KURT SIMONSEN: Thank you. So
20 noted.
21
22 --- EXHIBIT NO. MH-75: Depreciation panel
23 presentation
24
25 MS. HELGA VAN IDERSTINE: And with

1 that, I would like to turn this over to Ms. Bauerlein
2 to introduce us.
3
4 PRESENTATION:
5 MS. SANDY BAUERLEIN: Good morning, Mr.
6 Chairman, Dr. Grant, Mr. Bel, and Ms. Kapitany. So I'm
7 going to be going through the -- the presentation with
8 you. It is fairly lengthy, but we felt that there was
9 a lot of material that we wanted to try and cover this
10 morning. There'll be a brief introduction.
11 We're going to be talking about what
12 some of those prospective depreciation changes are, a
13 bit of background, a discussion on the depreciation
14 procedures, how this ties with IFRS compliance, the
15 work done with our 2010 and 2014 depreciation studies
16 which really support our transition to IFRS, a
17 discussion on the accumulated depreciation surplus,
18 some options for rate setting, areas of concern, and
19 customer rate impacts.
20 So in starting, I wanted to note that
21 Manitoba Hydro feels that the changes in depreciation
22 expense that are planned by Manitoba Hydro comply with
23 the requirements of IFRS and do not negatively impact
24 customer rates.
25 We also feel that using one (1) method

of depreciation for both financial reporting and rate-setting purposes is in the public interest. We also believe that the ELG method is appropriate and reasonable, and we will demonstrate that Manitoba Hydro has the accounting records necessary to implement the ELG, or equal life group, method of depreciation.

As such, we are requesting the Public Utilities Board to accept the collective changes being made to depreciation as reasonable and appropriate for rate-setting purposes.

So what are these changes? Well, there's really three (3) main components for the change in depreciation. The first two (2) are resulting in decreases in depreciation expense.

Item number 1 is the impact of the change in our depreciation rates following the 2014 depreciation study which was primarily as a result of the extension of asset service lives.

The second decrease in depreciation expense is a result of the policy decision by Manitoba Hydro to remove negative or net salvage.

These decreases are being partially offset by an increase in depreciation expense in order to ensure compliance with the requirements of IFRS. Compliance with IFRS has been achieved through a change

1 in our depreciation methodology from the average
2 service life, or ASL, method to the equal life group
3 method.
4 As we go through this presentation, we
5 will provide additional information on the requirements
6 of IFRS and these two (2) methods of depreciation.
7 So this slide was presented in the
8 finance panel, and again it demonstrates that -- the
9 overall reduction to revenue requirement as a result of
10 our accounting changes.
11 As indicated, there is an increase in
12 the OM&A costs, which again was discussed further in
13 the finance panel, but these changes are being offset
14 by the collective depreciation impacts.
15 So a bit of background. So depreciation
16 is the recognition and expense of an asset's
17 consumption over its service life. Manitoba Hydro uses
18 the straight-line method, which is the most common
19 approach used for utilities. Manitoba Hydro calculates
20 depreciation expense using group depreciation, and it
21 uses that whether we're under Canadian generally
22 accepted accounting standards or IFRS.
23 So what is this group depreciation
24 concept? Group depreciation procedures are used to
25 depreciate plant assets where the volume of assets to

be depreciated is so large that it is not practical or efficient for the entity to perform depreciation calculations on each individual plant, item, or piece of equipment, which is the case for many large utilities.

So a few examples that demonstrate the concept of group depreciation used at Manitoba Hydro. For example, we will group all of the turbines and generators at a particular generating station rather than saying, We have this generator, generator number 1, generator number 2, turbine 1, turbine 2. So we group those all together for each station, hydraulic station.

Another example would be for our fleet. We group all of our light trucks in one (1) depreciation component group category, not each individual truck.

So tying back to some of the discussions that you may recall from our planning and operations panel, we will try and address some of the differences of the information that's been captured in the asset management systems that are used for the asset condition assessment versus the information, the type of information that we capture for depreciation purposes in our accounting system.

1 We note, however, that Manitoba Hydro
2 would track in its asset management maintenance systems
3 usually the individual pieces of equipment that they
4 need to maintain where appropriate. Whereas as I
5 indicated, we group together various individual pieces
6 of equipment for accounting purposes.
7 So within each component group will
8 contain assets with a variety of service lives. So
9 service life dispersion is really the range in service
10 lives of different assets within that group. For
11 example, in trying to demonstrate a service life
12 dispersion, in Appendix 11.49, which was in response to
13 the PUB Directives 8 and 9 where we were demonstrating
14 the requirements to move to an IFRS compliant method --
15 or IFRS compliant using the ASL method, we indicated
16 that within our component group of poles and fixtures
17 we have a service life of sixty-five (65) years is what
18 we -- we use in that component group.
19 However, if you actually were to break
20 that component group out, we recognize that within
21 poles and fixtures we actually have the wood poles,
22 which have a service life of approximately sixty-five
23 (65) years, but we also have the cross arms that are
24 attached to those poles with a service life of thirty-
25 five (35) years. So again, within the one (1) group

1 we're showing that we have a fair amount of dispersion,
2 recognizing that we have some assets with ranges of
3 service lives from sixty-five (65) years to thirty-five
4 (35) years.
5 So you note that is assets that are in a
6 group with a narrow range of service lives, they will
7 have actual lives closer to the average as compared to
8 assets in a group with a wide range in service lives.
9 So this is an important concept, because it's -- it's
10 going to get into some of the differences between what
11 the equal leaf -- equal life group method or procedure
12 does versus what -- and how it is calculated versus how
13 the ASL or average service life method is -- is
14 calculated.
15 So with respect to depreciation expense
16 though, there are differences between Canadian GAAP and
17 IFRS requirements. IFRS is more strict. It requires a
18 greater degree of precision. And I will be going
19 through later on in the presentation a little bit more
20 into the details of what those differences are between
21 IFRS and Canadian GAAP.
22 But this level of precision
23 appropriately recognizes the asset over its period of
24 consumption. So in assessing how we needed to comply
25 with IFRS, first of all, Manitoba Hydro did an analysis

1 of the standards and discussions with KPMG. We also
2 recognized in -- in -- with discussions with KPMG that
3 there was a need -- in order to comply with those
4 requirements of IFRS, to be able to have that greater
5 degree of precision, we had to evaluate the options
6 available to us in terms of the depreciation methods,
7 or procedures Mr. Kennedy's going to call them, and
8 what the differences were, and -- and what choices we
9 had to make in terms of being able to ensure that we
10 would be compliant with IFRS.
11 So with that I'm going to turn it over
12 to Mr. Kennedy who will be describing two (2) of the
13 depreciation procedures that are available to Manitoba
14 Hydro.
15 MR. LARRY KENNEDY: Good morning,
16 again. I'm going to spend just a few minutes
17 discussing the -- the procedures that -- that are
18 commonly used by publically regulated utilities in
19 dealing with the -- the issues of group depreciation
20 and how best to manage those.
21 And I'm going to describe -- I think
22 there's been a lot of evidence in this case about
23 procedures, average service life procedure and the
24 equal life group procedure and I want to contrast for a
25 few minutes a little bit of those differences to unit

1 depreciation, which we would see more predominantly in
2 the unregulated world, or in the circumstance of a few
3 regulated utilities that -- that have managed to -- to
4 keep their records at that level.
5 The average service life procedure
6 really is, as its name describes, it calculates
7 depreciation on the average of the group. You heard
8 Ms. Bauerlein describe, for example, the poles account.
9 It -- it says all -- all investment in the poles
10 account is going to depreciate over one (1) average
11 service life, irregardless of -- of the known fact that
12 some of the components of that pole will -- will come
13 out of service sooner, and some will, in the fact, last
14 longer than that average. But the average service life
15 is as its name implies, the -- based on an average of
16 all the investment.
17 Just in -- in terms of some of the
18 literature that's been entered into this proceeding and
19 more broadly throughout the -- the depreciation
20 community, this procedure is also known as the average
21 group life procedure, if we get into some textbooks and
22 some -- some other literature. The equal life group,
23 in contrast, subdivides an asset or subdivides an
24 investment in an account to the expected lives --
25 specific expected lives of the -- of the investment

1 over that whole life.

2 So, for example, if we take all those

3 poles that -- that Ms. Bauerlein was describing, we do

4 know some components of the pole will have a different

5 life, and we also know that not every pole will expire

6 at the same time. There's, you know, cars hit poles,

7 wind storms take poles down. Not all poles are

8 expected, even the physical pole itself, to last the

9 same -- over the same period.

10 In fact, we -- we know for -- for

11 certain that there will be a dispersion in the

12 retirement of those poles due to various forces of

13 retirement. The equal life group procedure subdivides

14 the investment in those poles over that expected

15 dispersion of the retirement activity. So it's much

16 more precise in its ability to -- to determine the

17 amount of investment that will live over very specific

18 periods, anywhere from age one (1) to -- to an age very

19 -- very far out into the future and beyond the average

20 service life. So it -- it includes very precise

21 calculations for very many average service life

22 estimates.

23 The -- the Manitoba Hydro, through -- to

24 this point in time has used the average service life

25 procedure. This -- this application includes a

1 proposal to -- to transition to the -- the equal life
2 group in part because of the precision that the equal
3 life group method or procedure allows for and the
4 manner in which that precision is required within the -
5 - in the new accounting standards.
6 The -- I'm going to contrast that now a
7 little bit to the more traditional world of -- of
8 accounting and -- and depreciation where, for example,
9 a manufacturing plant that may have a -- a
10 manufacturing unit and a building and some chairs and
11 whatever. Given the far fewer number of assets, the
12 accounting systems would allow those organizations to -
13 - to track the specific depreciation expense and
14 ascribe a life specifically to those assets.
15 In that manner, there -- there is no
16 need for grouping, no need for averaging, no need for
17 trying to figure out the various component groups.
18 You've done that already in -- in that assignment of a
19 specific life to each of the units. So usually when --
20 when we see unit depreciation, it's in the -- the more
21 traditional world of -- of non-utility plant or in the
22 world of utility plant where there is a few very large,
23 specific units that -- that you can get more precise
24 with.
25 The input to both the average service

1 life and the equal life group procedures is the same.
2 They both require a -- a historic life analysis. They
3 would both require, if so included, the calculations
4 and determination of net salvage percentages. And
5 it's, I think, a key component here. The -- the
6 determination of the average service life, which we
7 will commonly refer to the Iowa curves or the
8 retirement dispersion curve, is an input to either
9 method. You use the same curve and the same est --
10 life estimate in both of the procedures.
11 Now, that life estimate is -- is built
12 on a number of factors. It's not built precisely and
13 only on the historic information in the retirement
14 activity, albeit that is a -- a significant component
15 when we have a significant amount of retirement
16 history. And in other cases, we use other -- other
17 professional judgment factors. We -- we spent, in this
18 -- in this case, particularly a large number of
19 meetings and a large amount of time discussing the
20 management philosophies of how they maintain and work
21 with their assets, the management philosophies of new
22 capital programs coming up, new replacement programs.
23 We spoke in detail with the engineering
24 staff of the Company to understand the manner in which
25 their assets are -- are placed in service. We, in

1 fact, engaged the operational staff to a very large
2 degree to understand the -- how the assets are being
3 operated.
4 So we -- we spent a long -- a large
5 amount of time discussing with the internal subject
6 matter experts within Manitoba Hydro how the assets are
7 used, what type of assets they have, and their
8 expectations of life.
9 We also bring into account -- think
10 about things like, What's industry as a whole? And
11 when I speak to 'industry', I'm referring to both the
12 utility industry, the peer companies, the BC Hydros,
13 the Ontario Powers, the SaskPowers, the et cetera,
14 right across the country, most of whom I've had the
15 privilege of working with and understand their life
16 estimates and their -- and their philosophies.
17 But also the manufacturing industry in
18 terms of some -- we -- we do keep -- try to keep
19 current with the -- the manufacturers and the type of
20 equipment they put in, and what they say about their
21 equipment. So that all forms part of a -- a very large
22 background of knowledge base that we use in -- in
23 building this -- this dispersion curve.
24 And just for reference, I think we --
25 although it's not the world's most exciting reading, we

1 did provide a detailed description of what we do and
2 how Iowa curves are built through the -- the use of a
3 retirement rate analysis as Appendix -- Appendix 1 to
4 the Gannett Fleming report that I understand was filed
5 as part of Appendix 5.6, Attachment 2, of the rate
6 application. So it -- there it gets a little bit more
7 technical, but it does describe in a fair amount of
8 detail the -- the processes that we do in -- in
9 developing the life analysis.
10 As part of that developing of the life
11 analysis, the -- we end up with this retirement
12 dispersion curve. And that -- that curve was actually
13 -- comes from the -- the use of -- of mortality and
14 actuarial studies and philosophies of -- from the
15 insurance industry, where they -- like physical assets,
16 they -- they recognize that even though 1958 was a very
17 fine year for the birth of human beings, because that
18 happened to be my birth year, that not everybody born
19 in 1958 is going to find their mortality for the same
20 causes at the same time and on the same path.
21 So they -- the develop retirement
22 curves, or dispersion curves. We use that same
23 philosophy in looking at assets. One (1) of the
24 benefit of using those curves is we can gain a lot of
25 information from them. We gain the information that

1 describes the -- the life estimate -- the average
2 service life estimate.
3 We gain the -- the inf -- information
4 with regard to the shape and the pattern of the
5 retirement activity, or -- and the expected retirement
6 activity. We also gain the -- the information that --
7 from that Iowa curve, we can calculate at any age
8 interval the remaining life of the plant that survives
9 at that age interval.
10 So we can calculate a remaining life,
11 and we can also calculate for any -- any age interval
12 the probable remaining life, or the probable life in
13 total of the assets that made -- that made it to that
14 age interval. So there's a number of things that we
15 can gain from reviewing that Iowa curve.
16 The -- in the case of Manitoba Hydro,
17 and I want to be very clear here, the remaining life is
18 not used in the basic calculation of the whole life
19 depreciation rates. The remaining life is used only to
20 provide a mechanism, or the information to -- to
21 amortize any accumulated depreciation true-up
22 requirements.
23 Now, a true-up requirement for accumu --
24 accumulated depreciation results from a snapshot in
25 time where we say -- excuse me -- we say, based on a

1 snapshot in time, in this case, March 31st, 2014, had
2 we known everything that we know at that date in time,
3 and had we used the depreciation parameters, the
4 average service lives, that retirement dispersion, and
5 the net salvage parameters, from day 1 at that point in
6 time, we would have, or we should have, a certain
7 amount of investment, or a certain amount of recovery
8 in the accumulated depreciation account.
9 We compare that to what's actually in
10 the -- the books of account in the accumulated
11 depreciation. The difference between those two (2)
12 numbers, the theoretical number and the -- and the
13 actual number, at that point in time, is a number
14 that's commonly referred to as an accumulated
15 depreciation variance.
16 We -- we would amortize that variance
17 over the remaining life of the assets. That's the only
18 spot we use remaining life in the calculations of
19 Manitoba Hydro, is for the calculation of that
20 accumulated depreciation variance.
21 The -- the key difference between those
22 two (2) procedures -- and I -- I'm going to try to take
23 books of detail and -- and synthesize it down to the
24 Reader's Digest version for about two (2) minutes here.
25 It's the difference between those two

1 (2) procedures is how the actual depreciation rate is
2 calculated. It has nothing to do with the manner in
3 which we figure out the average service life. This is
4 now at the point in time when we're doing some
5 arithmetic and figuring out a rate.
6 I'm going to first describe the average
7 service life. The average service life, as I indicated
8 before, would take Ms. Bauerlein's example of poles and
9 say all poles, including the cross-arms and including
10 the guy-wires and including everything else that goes
11 on with poles, and amortize that over a life.
12 Let's assume for a second that -- that
13 we -- that life is determined to be ten (10) years.
14 We'd say every -- all the investment on that account,
15 no matter when we would expect it to retire and for why
16 we would expect it to retire, would get a 10 percent
17 depreciation rate.
18 The -- but there is -- a key component
19 here is knowing that we are using an average, a 10
20 percent rate, for all investment, and also knowing that
21 there's going to be wind storms and there's going to be
22 ice storms and there's going to be assets that last
23 longer than ten (10) years.
24 There -- the assumption in the average
25 service life method, our procedure, and in fact in

1 group depreciation as whole as -- as it's used by
2 utilities is that we don't -- we can't track the
3 specific accumulated depreciation to a specific asset.
4 The detail required for that would just be massively
5 enormous.
6 So when an asset retires, we assume that
7 it has absolutely been perfectly fully depreciated.
8 There is no gain or loss on the retirement of that
9 asset charged to the income statement. Any -- any
10 variance from the timing that would occur or from the
11 amount of salvage or from any other factor gets buried
12 inside the accumulated depreciation.
13 In other words, when we retire an asset,
14 the -- the entry, in this most simplistic basis, is you
15 credit the cost of the asset and you debit the
16 accumulated depreciation for the original cost. There
17 is no -- no calculated gain or loss on retirement.
18 And so, of course, with the average
19 service life method, the -- the amount of that variance
20 and the amount of that potential variance changes, and
21 it's not quite as precise. And we're going to describe
22 in a little bit here now.
23 With the equal life group method, rather
24 than using that one (1) overall average, it would
25 actually build intrinsically a series of very specific

1 depreciation rates for each of the expected life
2 intervals.
3 Now, an example that's kind of the
4 textbook example of equal life group that -- that I
5 know I use lots and my firm uses a lot is let's assume
6 for a second -- and I'm going to ask -- I'm going to
7 try to take you through a bit of a path of arithmetic
8 here.
9 Let's assume for a second that we have
10 an account. That account in fact has two (2) assets,
11 and each of those assets is worth one thousand dollars
12 ($1,000). And we know that those two (2) assets, one
13 (1) of them is expected to retire after five (5) years,
14 or have a five (5) year life, and one (1) of those
15 assets is expected to have a fifteen (15) year life.
16 In the average service life procedure,
17 we would say the average of the thousand dollars
18 ($1,000) at five (5) years and the thousand dollars
19 ($1,000) at fifteen (15) years gives me a ten (10) year
20 average, thus my 10 percent depreciation rate.
21 In the equal life group, it -- it gets a
22 little bit more precise. It says, I know I have a five
23 (5) year life, an asset worth a thousand dollars
24 ($1,000) with a five (5) year life. I'm going to treat
25 that thousand dollars ($1,000) at a 20 percent rate,

one (1) over five (5).

And I know I have an asset in that account with a fifteen (15) year life. I'm going to give that asset a 6.67 percent rate, one (1) over fifteen (15).

And in the good old days, this procedure used to also be known as the unit summation procedure. In fact, the textbooks that first described it called it the unit summation because the expense that is allocated to that account is the summation of the depreciation expense related to the units.

And so the depreciation rate, in my simple two (2) asset example, is going to be 20 percent for the five (5) year asset and 6.67 percent for that fifteen (15) year asset. So for the first five (5) years of its life, the depreciation rate will be 26.67 percent, and in the last ten (10) years, it's going to be 6.67 percent.

Now, that's kind of a lot of arithmetic. So what we do, we -- we summarized on this chart. On this chart, down the left side, you will see the -- the annual accrual amount for average service life procedure for the first five (5) years is two hundred dollars ($200). That rep -- represents the two (2) assets at a thousand dollars ($1,000) each, or two

1 thousand dollars ($2,000), times the 10 percent
2 depreciation rate. It gives me two hundred dollars
3 ($200) per year for five (5) years.
4 At the end of the fifth year we -- we do
5 that retirement. And as I mentioned before, the group
6 accounting concepts as you retire the original cost out
7 of the accumulated depreciation account, that thousand
8 dollars ($1,000), leaving me a balance in the
9 accumulated depreciation account at the end of year
10 five (5) of zero dollars.
11 For the next ten (10) years my -- my
12 asset in service -- my investment in service is one
13 thousand dollars ($1,000), because I retired the first
14 thousand dollars ($1,000). So I have a thousand
15 dollars ($1,000) left to which I apply my 10 percent
16 rate. My rate is the same 10 percent. That -- that 10
17 percent rate equals a hundred dollars ($100) per year
18 for year six (6) through fifteen (15), getting me to a
19 thousand dollars ($1,000) at the -- of accumulated
20 depreciation in the year fifteen (15). I retire that
21 thousand dollars ($1,000) and I have a zero dollar
22 left.
23 The average service life does what we
24 like it to do. It recovered the total cost of the two
25 thousand dollars ($2,000) of investment. Now, I'm

1 going to contrast that a little bit to the equal life
2 group procedure. The equal life group procedure in the
3 year ones (1) through five (5), as I indicated
4 previously, is a two hundred ($200) related to that --
5 to that five (5) year asset and sixty-seven dollars
6 ($67) related to that fifteen (15) year asset, giving
7 me an annual accrual amount of two hundred and sixty-
8 seven dollars ($267) for the first five (5) years.
9 Along comes the end of year five (5).
10 We retire that first thousand dollars ($1,000) unit and
11 I'm left with three hundred and thirty-five dollars
12 ($335) left in my accumulated depreciation account.
13 But in years six (6) through fifteen (15) all I have
14 left is that five (5) -- that fifteen (15) year unit.
15 And my depreciation expense related to that fifteen
16 (15) year unit is sixty-seven dollars ($67) per year.
17 I track that sixty-seven dollars ($67)
18 per year through the end of the year fifteen (15). By
19 the time I get to the end of year fifteen (15) I have a
20 thousand dollars ($1,000) built up in my accumulated
21 depreciation. I retire the thousand dollars ($1,000)
22 of original cost and my accumulated depreciation comes
23 to zero.
24 It also tracks and depreciates the two
25 thousand dollars ($2,000) of investment. Two (2)

1 critical points: One (1) is the investment -- the
2 accumulated depreciation at the end of year five (5)
3 has left nothing in accumulated depreciation related to
4 the recovery of that fifteen (15) year unit. It's
5 totally consumed. And in fact, from year six (6) to
6 fifteen (15) those -- that -- that depreciation expense
7 component includes the under recovery of that five (5)
8 year unit over the next ten (10) years.
9 Whereas in contrast the equal life group
10 procedure at the end of year five (5) is -- is
11 indicating an accumulated depreciation balance of three
12 hundred and thirty-five (335), not with some rounding
13 and no decimal places, it -- it is in essence one-third
14 (1/3) of the fifteen (15) year life related to that
15 fifteen (15) year asset.
16 So at the end of year five (5) we have
17 recovered 100 percent of that five (5) year asset and
18 one-third (1/3) of the life -- or one-third (1/3) of
19 the investment equal to the one-third (1/3) of its
20 consumed life for the fifteen (15) year asset. And we
21 track down after that and the revenue requirement or
22 the depreciation expense component is reduced to be
23 reflective of only that asset left in service.
24 Now, one (1) other kind of critical
25 point here, you'll notice in both cases we retired a

1 thousand dollars ($1,000) at year five (5). We didn't
2 retire just the depreciation expense or try to figure
3 out the assumption is there was no gain or loss on
4 retirement in -- at the time that we booked that
5 thousand dollars ($1,000) to the accumulated
6 depreciation account.
7 So there is a bit of difference. The --
8 we will hear words like accelerated depreciation
9 ascribed to equal life group procedure. We'll hear
10 terms like front end loading. In my view, I don't
11 think that's correct. It's the appropriate recognition
12 of the consumption of the service value of both of
13 those assets.
14 The average service life of anything, I
15 think inappropriately transfers some -- some burden to
16 future years at the benefit of those in the current
17 years, whereas the equal life group attempts to match
18 that -- that consumption of service value a little bit
19 more precisely.
20 Now, the -- the third option, if we were
21 to go to unit depreciation, how would this work? Well,
22 unit depreciation would have taken those two (2) assets
23 and said, Ah, there's a significant enough difference
24 in the five (5) and the fifteen (15) year life, so I'm
25 going to make two (2) accounts.

1 I'm going to have an account for the
2 five (5) year asset and it's going to track a five (5)
3 year life, two hundred ($200) per year and it's going
4 to have a separate account with a separate set of
5 arithmetic and a separate set of accounting
6 depreciation expense going on and it's going to track
7 for fifteen (15) years at -- at sixty-seven dollars
8 ($67).
9 Well, interestingly enough, if you were
10 to follow unit depreciation you're going to have an
11 expense profile that looks identical to the equal life
12 group profile. Because the equal life group is
13 attempting to do that without having to componentize
14 those into two (2) separate accounts.
15
16 (BRIEF PAUSE)
17
18 MR. LARRY KENNEDY: The depreciation on
19 assets that actually live less than the average service
20 life and as compared to the depreciation on assets that
21 live longer than the average service life has a
22 different profile. Depreciation on assets that live
23 less than average will have an increased amount of
24 depreciation. And the -- the depreciation with --
25 related to assets that live longer than average service

1 life will have an -- have a decreased amount of
2 depreciation.
3 And that's just kind of a function of
4 arithmetic. But it's also a function of the fact that
5 typically the shorter life assets are slightly lower
6 cost than -- than the longer-lived components. So you
7 get this -- not only the arithmetic, you get the
8 waiting that -- that's included in -- in that -- that
9 phenomenon, so. That's just -- I think we wanted to --
10 to kind of describe that profile a little bit as -- as
11 we go through some of the more -- more complicated
12 areas, but now I think I'm back to Ms. Bauerlein.
13 MS. SANDY BAUERLEIN: So I'm going to
14 be going through again what the -- the compliance
15 requirements of IFRS are. So first of all, and I -- I
16 talked about this earlier, is the first main difference
17 is the level of precision that's required. So what
18 does precision means? It means that depreciation
19 expense needs to be calculated at a greater degree of
20 componentization. And again, it's componentization is
21 breaking assets into a similar group. It's not really
22 having that you necessarily have to have the individual
23 items or the units.
24 So an example would be again that we
25 group of componentize turbines and generators for each

1 generating station, not each individual generator or
2 turbine at the particular station. Another example
3 where we componentize is that we have several thousand
4 fleet-type vehicles, but for depreciation purposes we
5 componentize or group them into seven (7) categories.
6 So we have categories such as light trucks, passenger
7 vehicles, trailers, et cetera. And again, as Mr.
8 Kennedy emphasized, precision doesn't mean front-
9 loading. It means the improving of matching of the
10 expense to the service life of the assets.
11 The second difference that IFRS requires
12 is that gains and losses on retirement of assets have
13 to be charged immediately into income un -- under IFRS.
14 Under Canadian GAAP any gains and losses on the
15 retirement of the asset are charged against accumulated
16 depreciation and are factored into future depreciation
17 rates.
18 The third difference under IFRS is the
19 treatment of costs of removal or negative salvage which
20 is not permitted under IFRS. So I'm going to go now
21 into a little bit more detail about each one (1) of
22 these differences between IFRS and Canadian GAAP.
23 So the first is on that
24 componentization. So Manitoba Hydro in its response to
25 IR MIPUG-I-17(a), we provided numerous references and

1 excerpts not only from the accounting standards, but
2 from various accounting bodies which highlight the
3 requirements under IFRS standards. So I note that
4 under IFRS 16 -- IAS 16, that each part of an item of
5 property, plant, and equipment with a cost that is
6 significant in relation to the total cost of the item
7 shall be depreciated separately.
8 An excerpt from the accounting firm
9 Deloitte under "International Financial Reporting
10 Standards Consideration for Power and Utilities," in
11 2008 wrote:
12 "The component approach means that
13 different depreciation periods will
14 be used for each component of a fixed
15 asset. For example, a power plant is
16 comprised of separate components with
17 different useful lives."
18 You've got the turbine rotor, the
19 turbine blades, et cetera. So its total book value
20 will have to be allocated to these separate components.
21 In reference to a comment made about Canadian GAAP
22 being less explicit it was referenced in comments made
23 by BDO Dunwoody LLP. And they stated that:
24 "Both Canadian GAP and IFRS require
25 component accounting. However, the

1 requirements under IFRS are much more
2 explicit."
3 And we have had discussions with our
4 external auditors, as well as KPNG -- KPMG in
5 understanding the -- the level of precision that is
6 required under IFRS.
7 So Manitoba Hydro right now has two (2)
8 options to ensure compliance with the componentization
9 requirements of IFRS. We can change to the equal life
10 group method of depreciation, which you'll see as Ms.
11 Hooper goes through, our current level of
12 componentization supports.
13 We have done extensive work since 2010
14 to ensure that the level of componentization would
15 support an equal life group calculation.
16 The second way that we could maintain
17 the ASL method or procedure, but it would require that
18 we further increase the number of asset component
19 groups in order to comply with the requirements of
20 IFRS. And that's again back to Mr. Kennedy's
21 discussion in terms of how the two (2) calculations
22 work differently.
23 Because the equal life group considers
24 those subcomponents and the lives of those, we could
25 subcomponentize to -- or componentize our assets to a

1 lesser degree than you would have to under an ASL
2 method.
3
4 (BRIEF PAUSE)
5
6 MS. SANDY BAUERLEIN: I did want to
7 emphasize though that in Manitoba Hydro's response to
8 the directives 8 and 9 from Order 43/'13, as a result
9 of the IFRS requirement for greater precision and
10 therefore a greater level of componentization, we've
11 identified that depreciation expense will increase
12 regardless of the method of depreciation used as long
13 as you're complying with the requirements of IFRS.
14 We have forecasted that the change to
15 the equal life group method will result in an annual
16 increase in depreciation of approximately 36 million,
17 and this would be comparable to the estimated increase
18 in annual depreciation under an IFRS-compliant ASL
19 method.
20 So because of the way the ELG
21 calculation works, the ELG calculation itself results
22 in -- in assistant -- consistency with the requirements
23 of IFRS as it calculates depreciation expense with
24 consideration of the dispersion in the service lives of
25 assets within a component.

1 Under -- if we were to use the ASL
2 method, compliance with IFRS would require additional
3 component groups so in order to minimize that
4 dispersion in service lives so that the average would
5 more closely resemble the actual service life of those
6 components.
7
8 (BRIEF PAUSE)
9
10 MS. SANDY BAUERLEIN: So Manitoba
11 Hydro's current level of componentization using the ASL
12 method would not meet the requirements of IFRS. And I
13 think I -- I've referenced this example a few times, so
14 again it is in Appendix 11.49.
15 But prior to 2010, we had a component
16 group, Wood poles, conductors, and attachments.
17 Following the 2010 study and the work that my
18 colleague, Ms. Hooper, will discuss, we broke that
19 category into two (2) component groups, wood poles and
20 fixtures with a service life of approximately fifty-
21 five (55) years, and overhead conductors and devices
22 with a service life of sixty (60) years.
23 This level of componentization using an
24 ELG method of depreciation would comply with the
25 requirements of IFRS simply because of the way the ELG

1 calculation works. If we were to move, however, to an
2 ASL method of depreciation, because of the nature of
3 the calculation, we would again further have to break
4 down our component group wood poles and fixtures into
5 wood poles, which would have a life of sixty-five (65)
6 years versus cross-arms at thirty-five (35) years.
7 And again, that requirement would be
8 necessary under an ASL method because as the
9 calculation works they have a service life that is
10 significantly different from the poles. So again you
11 would have to break each component down where you have
12 significant differences in the service life and the
13 costs of -- of the assets.
14 Again, I've -- I've mentioned that
15 getting to that -- that middle box there, that current
16 level of componentization that was necessary for us to
17 comply with IFRS using the ELG calculation, did require
18 a significant work effort as this wasn't the level of
19 componentization captured in Manitoba Hydro's
20 accounting system.
21 We had to basically allocate all our
22 historical costs now between the categories of, in this
23 example, wood poles and fixtures and overhead
24 conductors and devices.
25 And again, Ms. Hooper will provide

1 further details on what that componentized effort --
2 effort required in order for Manitoba Hydro to be
3 compliant with IFRS using the ELG method of
4 depreciation.
5 MS. MARILYN KAPITANY: Ms. Bauerlein,
6 before you leave that slide --
7 MS. SANDY BAUERLEIN: Sure.
8 MS. MARILYN KAPITANY: -- could you
9 just explain why in 2005, when we had wood poles,
10 conductors, and attachments, the -- it was thirty-one
11 (31) years of life. And then when you moved in 2010,
12 it went to fifty-five (55) and sixty (60)?
13 MS. MICHELLE HOOPER: Good morning, Ms.
14 Kapitany. The change in service life that occurred in
15 the 2010 study for poles and fixtures was really not
16 specifically related to the change in componentization.
17 The change in service life came about
18 because Manitoba Hydro had done significant work in the
19 lead-up to the 2010 study to inventory poles and
20 determine exactly what we had out in the field for
21 assets.
22 And we came to the realization through
23 that work that the service life that we had been using
24 of thirty-one (31) years did not accurately reflect the
25 service life that we were receiving for those poles.

1 MS. MARILYN KAPITANY: So that would
2 have quite a major change then in expense depreciation,
3 depreciation expense at that time?
4 MS. MICHELLE HOOPER: Yes. There was a
5 significant reduction in depreciation expense as a
6 result of the service life changes that were -- that
7 were incorporated in the 2010 depreciation study.
8 MS. MARILYN KAPITANY: Thank you.
9 MR. LARRY KENNEDY: Just if I can add
10 maybe one (1) little piece of information to that. The
11 -- that's a really good example of where maybe the
12 historic retirement data provides -- if you relied on
13 that exclusively, you get maybe a bit of a biassed view
14 that isn't correct.
15 As Ms. Hooper alluded to, the Company
16 had undertaken a program to inventory poles, and
17 through this pole management system and work, provided
18 us another source of information that we were able to
19 rely upon in addition to just the historic information
20 that -- that allowed us to make that life estimate
21 change.
22 MS. SANDY BAUERLEIN: I'm just
23 wondering if there's any further questions, or if -- if
24 it's clear what this example is trying to represent in
25 terms of the differences between how the equal life

1 group method words versus the average service life
2 method. Okay.
3 MS. MARILYN KAPITANY: Note on that
4 example, but just back on slide 24 when you had said
5 that there's two (2) different ways to get to IR --
6 IFRS compliance. And you talked about either changing
7 to ELG or staying with ASL and going with increased
8 componentization.
9 Did your auditors give you any view on
10 which way they thought was the best way for the
11 Corporation to move?
12 MS. SANDY BAUERLEIN: No auditors,
13 their view is they need -- that we need to comply with
14 IFRS. And the method of depreciation is really a
15 Manitoba Hydro decision, it's not an auditor's
16 decision.
17 They would be looking to ensure that
18 whatever method of depreciation we do, that that
19 results in compliance with the requirement of IFRS for
20 the level of precision necessary in calculating
21 depreciation expense.
22 THE CHAIRPERSON: I -- I have a
23 question, but it's not in relation to -- to IFRS, so --
24 it's a question I should have asked earlier.
25 In -- and to Mr. Kennedy -- are there

1 any method -- methodological differences in calculating
2 -- in doing a life analysis between ASL and ELG?
3 MR. LARRY KENNEDY: Generally, the life
4 analysis is an input to either one (1), the ELG or ASL.
5 I think, properly done, there is no -- no differences
6 in how we'd perform that life analysis.
7 Companies that are -- are following the
8 equal life group procedure or using the equal life
9 group procedure will sometimes have more information.
10 For example, I think Ms. Lee in some of our evidence
11 talked about synthe -- synthesized data or simulated
12 data, et cetera.
13 You would typically not perform a life
14 analysis, or I would caution a little bit about using a
15 life analysis that was performed with simulated data to
16 a large extent. Sometimes you have to fill in a -- the
17 odd blank here and there in some utilities. But to do
18 a complete study using simulated data, and then
19 implementing the ELG in that, I -- I would suggest is
20 not quite as reliable as having peer actuarial data, as
21 we have in this circumstance. So that -- that would be
22 the main difference is the data availability.
23 THE CHAIRPERSON: But -- but in -- in
24 either case, you'd be using the Iowa curves?
25 MR. LARRY KENNEDY: In either case, we

are using Iowa curves. And the end result of the life analysis would be very similar. There's much -- much written in textbooks and in theory about properly doing simulated studies that, quite frankly, I think often -- I would rather do a simulated study than do a study on the basis of poor actuarial data, because the -- the mechanics of the simulated studies, I think, is pretty reliable. But overall if you have good, reliable, and verified historic data, I think that -- that provides a better result. The end result is you still get this Iowa curve.

(BRIEF PAUSE)

MS. SANDY BAUERLEIN: So Manitoba Hydro made a policy decision to move to the equal life group method. And why did we do this? We felt it was really the most efficient way to comply with IFRS. We recognize that -- if again, I go back to this previous slide -- we recognize that, you know, prior to 2010, that the component grouping that we had was not sufficient enough to meet that requirement of -- of precision or -- or accuracy under IFRS.

So we knew we had to move -- we had to componentize further. However, in -- in deciding which

1 level of componentization -- so if again, the middle
2 box is where we are, it's equal life group calculation,
3 and it's compliant with IFRS because of the nature of
4 the way ELG is calculated. If we wanted to move to an
5 ASL method of depreciation, or continue with the ASL
6 method of depreciation, we recognize we would have to
7 move one (1) more layer down. We would have to further
8 break down our assets, as in the example wood poles and
9 fixtures. We'd have to break it down further between
10 wood poles and cross-arms.
11 So what we had to do is we had to make a
12 decision. Because it's really a balancing exercise,
13 because your level of componentization is where you
14 have to capture your transactional data. So for
15 example, when we have a capital project, all our
16 purchase orders have to be aligned with the data,
17 because you need to capture those costs at that level
18 of componentization. Your employees who are doing the
19 construction work have to time card to that level of
20 componentization, so all your expenses have to be
21 driven to your level of components.
22 So it was really a balancing exercise in
23 terms of do we -- are we able to meet the requirements
24 of IFRS by having the category wood poles and fixtures,
25 and then overhead conductors and devices, et cetera, or

1 would we need to go one (1) step further and have our
2 wood poles and fixtures broken down between wood poles
3 and cross-arms?
4 So again, if you think about it from
5 sort of that operational perspective, when we're buying
6 those components or we're doing the work, the fellow is
7 replacing a -- a wood pole, he would have to recognize
8 how many hours he spends replacing the wood pole,
9 installing the wood pole, versus installing the cross-
10 arms. So again, it was -- it was a bit of a balance to
11 decide which method would balance what we need to
12 manage operationally for the Company, as well as comply
13 with the requirements of IFRS.
14 So in our discussions with Gannett
15 Fleming, we understood that we could achieve compliance
16 with IFRS with fewer component groups using the equal
17 life group method than we would under an ASL method.
18 So in addition, this would reduce the costs for the
19 conversion effort, and again Ms. Hooper will go through
20 extensively what that conversion effort entailed, as
21 well as the ongoing costs and work effort that we would
22 be required if we had to create additional component
23 groups under the ASL method of depreciation.
24 MS. MARILYN KAPITANY: So, Ms.
25 Bauerlein, you're saying that then it would be less

1 expensive to convert, but you said the increase in
2 depreciation expense is going to be approximately the
3 same, about 32 million, with -- regardless of which
4 method you choose?
5 MS. SANDY BAUERLEIN: Yes. So the
6 depreciation expense itself is similar to -- regardless
7 of each method, but there actually was -- ignoring the
8 depreciation expense itself, there was a cost for
9 Manitoba Hydro to actually convert its -- its asset
10 accounting records from this previous level of
11 componentization to this middle box. And Ms. Hooper
12 will go in detail in terms of what that effort was, and
13 how much it did cost. And then that cost, of course,
14 is passed on to the -- the ratepayers.
15
16 (BRIEF PAUSE)
17
18 MS. SANDY BAUERLEIN: So again, in
19 highlighting, this decision to move to ELG does have an
20 increase in depreciation expense, but it's really not
21 the decision to move to ELG. It's the requirements
22 under IFRS for greater precision, which again, is
23 balancing that -- the asset lives with their period of
24 consumption.
25 So again, if we go back to Mr. Kennedy's

1 slide 18, you can see again that in the ELG example,
2 the asset -- the first asset was consumed over five (5)
3 years. So you're -- you're paying for that asset in
4 the five (5) years rather than spreading the cost of
5 that first asset over the entire fifteen (15) year
6 period.
7
8 (BRIEF PAUSE)
9
10 MS. SANDY BAUERLEIN: So the next
11 difference that IFRS had was in terms of gains and
12 losses on asset retirements. So a gain will occur on
13 an asset retirement when the asset has provided service
14 longer than the average life for the component group.
15 In other words, the asset has been over-depreciated.
16 A loss will occur on asset retirement
17 when the asset is repir -- is retired prior to the
18 average life for that component group. In other words,
19 the asset is under-depreciated.
20 So again as I mentioned, under Canadian
21 GAAP Manitoba Hydro was able to record any gains and
22 losses in accumulated depreciation, and amortize them
23 through to depreciation expense over the remaining life
24 of the assets in each component group. So recognizing
25 we were using an average service life approach, we did

1 have gains and losses upon retirement, because of
2 course the chance that your asset upon retirement was
3 perfectly matched to the average is -- is significantly
4 -- is -- is less.
5 Under IFRS, though, gains and losses
6 have to be recognized to income immediately. So if you
7 use ASL and you continue with a wide dispersion of
8 service lives -- a wide dispersion in the service lives
9 of the assets, your gains and losses could be material.
10 In one (1) of -- IRs that we responded
11 to, it was PUB-II-29, we were asked to provide
12 retirement information for a particular component group
13 within a certain age interval. And the IR provided a
14 response on the retirement of dams, dikes, and weirs
15 for both Seven Sisters and Great Falls Generating
16 Stations.
17 And if you look in the IR, you will note
18 that there were losses on the disposition, so again we
19 retired it prior to it reaching sort of the -- what you
20 would say the average service life, and those losses
21 totalled approximately 30 percent of the retirement
22 value. So if we were under IFRS when those losses
23 occurred, those dollars would have been charged --
24 immediately recorded to net income.
25 So because the equal life group

1 considers in its calculation that service life
2 dispersion, you will have less volatility in your net
3 income if you -- if -- by going with the ELG procedure.
4 You will have increase in volatility net income if that
5 procedure that you choose does not align with the
6 service life of the assets.
7 So again, if you use the average service
8 life approach with a greater degree of
9 componentization, the -- the dollars would be -- the
10 gains of -- the magnitude of the dollars would be the -
11 - equal to what there would be under the ELG method.
12 However, if you use ASL without that greater degree of
13 componentization, as was the case, you know, prior to
14 Manitoba Hydro transitioning to IFRS, then the dollar
15 magnitude of these gains and losses would continue.
16
17 (BRIEF PAUSE)
18
19 MS. SANDY BAUERLEIN: So again, under
20 IFRS, though, the expectation is because you have a
21 greater degree of precision, because the depreciation
22 rates themselves are calculated more representative of
23 the service lives in the group, it will result in fewer
24 gains and losses. So we expect to have -- reductions
25 in gains and losses are expected under the ELG method,

1 because that calculation considers that service life
2 dispersion.
3
4 (BRIEF PAUSE)
5
6 MS. SANDY BAUERLEIN: So the third
7 requirement under IFRS is negative salvage. So
8 negative salvage, again, refers to the cost to retire
9 an asset from service. And under Canadian GAAP, such
10 costs were included in the depreciation rates as an add
11 on for certain asset categories.
12 It is an intergenerational equity
13 concept designed to remove the future costs of removing
14 an asset from service from the ratepayers that receive
15 service from the asset. And I note that in this
16 bullet, we've used the word 'removing'. But in -- in a
17 lot of our situations, especially for our generation
18 assets, it may not be removing the asset. It may be
19 simply the cost to -- to take that asset out of
20 service, to no longer have it operational, and to also
21 make that asset safe.
22 And I just wanted to note that in
23 reference to some of the comments made by some of the
24 Intervenors with respect to negative salvage on
25 generation assets, we note that approximately 65

1 percent of the annual $60 million of charged of
2 negative salvage annually is for the distribution and
3 substation component group.
4 So under IFRS, the costs to remove an
5 asset are added to -- we have a couple situations. We
6 either add them to the replacement asset if you're
7 actually replacing the asset, or they're expensed if
8 the asset's retired and it's not replaced.
9 However, there may be situations where
10 if it meets -- and they call it the 'recognition
11 criteria' under IFRS, if those recognition criteria
12 standards are met, then we will record an obligation,
13 and they refer to it as an 'asset retirement
14 obligation' will be recorded for the costs to retire an
15 asset. But in order to set up an obligation, first of
16 all, there must be a legal or constructive obligation
17 to do so, and we must be able to reasonably estimate
18 the costs to retire that asset.
19 Manitoba Hydro indicated in the
20 2012/'13, '13/'14 general rate application hearing that
21 negative salvage would no longer be included in
22 depreciation rates. And even though we believe that
23 this a -- a good regulatory practice, we made this
24 policy decision in order to offset the impacts of other
25 IFRS changes.

1 So the impact on depreciation expense of
2 Manitoba Hydro's policy decision to no longer include
3 negative salvage in depreciation rates is a reduction
4 of $60 million in depreciation expense beginning in
5 2016, and that reduction continues to grow through the
6 forecast period.
7 I'm now going to turn it over to Ms.
8 Hooper, who will again describe the 2010 and 2014
9 depreciation studies, as well as our IFRS conversion.
10 And it's important to note that that 2010 depreciation
11 study really set the foundation for us for
12 transitioning to IFRS.
13 MS. HELGA VAN IDERSTINE: So, Mr.
14 Chair, I was going to suggest that before we move into
15 -- if you don't mind, before we move into this, you
16 might want to think about whether this is an
17 appropriate time to take a break.
18 THE CHAIRPERSON: Yeah, exactly my
19 thought. So let's -- let's take a -- a coffee break,
20 ten (10) minutes. Thank you.
21 MS. HELGA VAN IDERSTINE: Thank you.
22
23 --- Upon recessing at 10:29 a.m.
24 --- Upon resuming at 10:42 a.m.
25

1 THE CHAIRPERSON: I believe that we can
2 start the proceedings, continue with the -- the
3 presentation. I would like to get this presentation
4 done before lunchtime, if possible. So perhaps
5 accelerate it a little bit, and we could -- we could
6 achieve that goal. Thank you.
7 MS. HELGA VAN IDERSTINE: We do -- we
8 think we're on time for that. So -- but I would like
9 to do one (1) thing, which I forgot to do before we
10 started, and that's introduce my back panel, who are
11 going to give me their titles right here. They've
12 finished writing them out for me.
13
14 (BRIEF PAUSE)
15
16 MS. HELGA VAN IDERSTINE: Thank you.
17 So directly behind me is Kristen
18 Perrault. She's a -- a regulatory financial analyst.
19 And beside her is Darryl Martin, the manager, asset
20 management accounting department.
21 And Ms. Hooper wanted me to make a
22 correction to her CV, which was -- under her present
23 title, it's not asset accounting systems supervisor.
24 It's asset accounting project supervisor, so.
25 And with that, she will begin to educate

1 you about what she's been doing for the last couple
2 years.
3 THE CHAIRPERSON: Thank you.
4
5 (BRIEF PAUSE)
6
7 MS. MICHELLE HOOPER: Thank you. I
8 wanted to cover off the conversion effort that -- and
9 the asset -- all of the work that was done in order to
10 compile the 2010 and 2014 depreciation studies and
11 prepare for IFRS conversion.
12 There's a comment made by Ms. Lee in her
13 evidence that indicates that unaged data does not
14 become aged without some synthesis intervention, and
15 she's absolutely right. A lot of intervention was
16 required, and that intervention was in the form of a
17 significant work effort on Manitoba Hydro.
18 Okay. This Gantt chart provides a bit
19 of a timeline view of the work effort that was entailed
20 in the -- in preparing for compliance with IFRS. So
21 from the 2008 to 2010 time frame, we did a -- an IFRS
22 impact analysis, and begun gathering data for -- to
23 support the 2010 depreciation study.
24 That study was collect -- was conducted
25 throughout the 2011 and into the 2012 fiscal year.

1 Implementation of the component changes from the 2010
2 study started in 2012 and are continuing. We have not
3 quite finished that effort yet.
4 A 2014 depreciation study was conducted
5 in the tail end of 2014 and the 2015 fiscal year. Our
6 IFRS implementation occurred March 2015, and we'll be
7 reporting under IFRS for financial reporting purposes
8 go-forward.
9 So for the 2010 depreciation study, as
10 discussed by Ms. Bauerlein, we analyzed the IFRS
11 standards in consultation with KPMG, our IFRS
12 consultants, and engaged Mr. Kennedy to gain an
13 understanding of the options available to us with
14 respect to property, plant, and equipment and
15 depreciation.
16 As part of that preparation, Manitoba
17 Hydro accounting -- accounting staff Gan -- and Gannett
18 Fleming held workshops with Manitoba Hydro engineering
19 and operational staff from all areas of the Corporation
20 in order to understand the nature and types of
21 equipment included in each of Manitoba Hydro's then
22 asset component groups in order to determine how much
23 additional componentization would be necessary to
24 comply with IFRS.
25 We made a decision to change to the

1 equal life group method of depreciation for IFRS and to
2 remove net salvage in order to mitigate and offset
3 other IFRS impacts.
4 New component groups were determined
5 based on use of ELG. As a result of that analysis, we
6 developed a hundred and ninety-eight (198) new
7 component groups. So we moved from a hundred and
8 twenty-eight (128) component groups in the 2005
9 depreciation study to three hundred and twenty-six
10 (326) in the 2010 depreciation study.
11 This next slide provides an example of
12 our change in component groups. So for each hydraulic
13 generating station -- and the example here is Great
14 Falls -- we had in 2005 and prior depreciation studies
15 four (4) components for that generating station: a
16 civil component, turbines and generators, accessory
17 station equipment, and other categories.
18 For the 2010 depreciation study, in
19 order to implement the level of componentization that
20 would be necessary for an ELG implementation, we
21 expanded those component groups.
22 So, for example, the civil component was
23 broken down into dams, dikes, and weirs; powerhouse;
24 powerhouse renovations; spillway; water control
25 systems; and roads and site improvements.

1 (BRIEF PAUSE)

2

3 MS. MICHELLE HOOPER: Significant work
4 was required in order to determine the costs
5 attributable to each of those new component groups. It
6 was necessary for us to computerize our sys -- our
7 historical accounting records. Prior to 1997, Manitoba
8 Hydro's asset accounting records were all kept on
9 paper. So we had enormous, big plant ledgers. We had
10 gener -- cards for some of the -- just which showed all
11 the history of handwritten expenditures. We have a
12 large -- a lot of capital -- historical capital work
13 order packages, which have all of the costs associated
14 with individual capital projects.
15 So we had a team of folks take those
16 calc -- those historical ledgers and rekey that
17 information in order to recapture all of the original
18 transactional data for all of the historical additions
19 and retirement activity for each of the original
20 component groups prior to our componentization change.
21 We then analyzed that data in order to allocate those
22 costs between the old components and the new
23 components.
24 So that involved reviewing captions in
25 the asset registers with respect to the nature of the

1 expenditures where there was insufficient information
2 in those captions. It involved going back to the
3 original capital projects in order to review the types
4 of costs and the nature of the expenditures in order to
5 break down those original costs into the new component
6 categories.
7 Once we had that information in
8 spreadsheets broken down by new components, we had to
9 compile that into a format that could be delivered to
10 Gannett Fleming for a new depreciation study. We
11 submitted an entirely new data set for the 2010
12 depreciation study. So typically, a depreciation study
13 just carries on from the previous study. So you would
14 have a data set for 2005, and you would submit the
15 incremental transaction data for the next five (5)
16 years to the next depreciation study. The depreciation
17 consultant would append that to the old information and
18 then redo all of their life analysis with that
19 incremental information.
20 That's not what happened for Manitoba
21 Hydro for the 2010 study. We created a whole new data
22 set for those new components. So as Ms. Lee indicated
23 a -- unaged data doesn't become aged. No, it doesn't.
24 You need to do a lot of work in order to get that. And
25 there were thousands of hours incurred over several

1 years in order to develop that data.

2 This next slide provides a summary of

3 costs incurred in order to identify those new component

4 groups and convert the assets aft -- after the

5 depreciation study. So efforts to identify new

6 components and develop histalor -- sorry -- historical

7 costs and vintage or installation year information,

8 cost approximately $.9 million. Gannett Fleming's

9 assistance in idet -- identifying new components,

10 vintaging, and developing depreciation rates was

11 approximately point two (.2).

12 Gannett Fleming's assistance with

13 regulatory support in the -- in the past hearing was

14 about fifty thousand dollars ($50,000), and our asset

15 conversion exercises, which included detailed review of

16 historical records, reallocating costs, staff training

17 to educate all of the staff across the Corporation as

18 to what those new component groups were, conversion of

19 historical asset records, conversion of all capital

20 project records to break the costs down into new

21 components, was another cost of about $1.7 million.

22 So that takes us to 2.85 million in

23 order to do that conversion effort that happened for

24 the 2010 study. That conversion is not yet complete.

25 We are still working on implementing that conversion.

We're most of the way there, but there are some areas that are not quite complete. We expect to finish within the next fiscal year.

(BRIEF PAUSE)

MS. MICHELLE HOOPER: Okay. The impact of the depreciation study, which is a result of componentization and reassessment of service lives for 2010, was a reduction in depreciation expense of $35 million annually.

With that breakdown in -- in component -- the -- the lower level of componentization we were better able to assess the service life for the equipment remaining in each new component group. We also looked to -- outside of the asset accounting registers to try and determine what other information was available to help us determine what the services lives should be.

And where we discussed poles earlier, that's one (1) area where a lot of work had been ongoing in order -- for asset condition purposes to understand the assets that the Corporation has, and understand what the population of those assets was and the condition of those assets.

And from that work, at the time of the 2010 study their inventory was not complete but there were strong indications that the physical assets of the Corporation were lasting a lot longer than what we had previously estimated. So that was the result of the change in service life for poles. And those changes in service lives had a significant impact on depreciation expense.

(BRIEF PAUSE)

MS. MICHELLE HOOPER: For the 2014 depreciation study, we're using the same level of componentization that was developed in the 2010 study. Excuse me.

We did develop fifty-nine (59) new component groups for 2014, but all of those new component groups were in response to changing business requirements. So the majority of those new component groups relate to the Wuskwatim Limited Partnership assets. There were also some new components developed for new -- new developments at Pointe du Bois in order to separate those new assets from the constraint of the old powerhouse. So, for example, the new spillway that

1 has been built at Pointe du Bois.
2 And there are a few other new component
3 groups that were developed but, as I said, all were in
4 response to changing business.
5 We refined the estimates for service
6 lives on several components during the 2014
7 depreciation study. As we have been transitioning our
8 component groups and implementing those changes in SAP,
9 we've been reviewing estimates made in 2010 and
10 refining them.
11 In addition, more information has become
12 available through asset condition assessment work to
13 understand -- operationally understand what the assets
14 are, and we have leveraged that information in order to
15 ensure that our asset accounting records are as
16 accurate as they can be, and that they're reflective of
17 the physical assets of the Corporation.
18 The impact on depreciation expense for
19 the 2014 study as a result in the change in service
20 lives was a further reduction of $25 million annually.
21 I'd now like to discuss the accumulated
22 depreciation surplus. So as Mr. Kennedy explained
23 earlier, an accumulated depreciation variance is
24 measuring the difference between actual depreciation
25 charged to date versus what would have been charged if

1 the current depreciation assumptions, such as service
2 life, Iowa curve, and salvage factor, had always been
3 used.
4 We have a -- assuming con -- adoption of
5 the ELG method, we have a surplus value balance of $602
6 million at March 31st, 214 -- 2014, and that surplus
7 will be amortized over the remaining lives of the
8 assets within each component group.
9
10 (BRIEF PAUSE)
11
12 MS. MICHELLE HOOPER: This surplus
13 reflects the extension of asset lives in the last dep -
14 - two (2) depreciation studies, the removal of net
15 salvage, and the change in methodology. The life
16 extension in the depreciation -- for depreciation
17 purposes is consistent with the findings in the asset
18 condition report, and is representative of where
19 Manitoba Hydro is at in its life cycle. Our assets are
20 lasting longer than we had previously estimated.
21 Amortization over that -- of that
22 variance over the remaining services lives of the
23 respective assets supports the principle of inter --
24 intergenerational equity. Okay.
25 It is important to note that the fact

1 that there is invaria -- a variance is not -- does not
2 mean there was an error in our past depreciation. It
3 just means that we've changed our assumptions. We've
4 changed our estimates. We've changed our practices.
5 The depreciation that was charged in past years was
6 charged using the best information that was available
7 at the time and the practices that were in place at the
8 time and approved. It wasn't an error.
9 Amortization of that variance over the
10 remaining service lives of the respective assets is
11 consistent with accounting standards for -- the
12 practices for changes in estimate. As we provided in
13 the response to MIPUG Round 2, Question 18, and
14 consistent with IAS 8 accounting policies for changes
15 in accounting estimates and errors, a change in the
16 estimated useful life of, or the expected pattern of
17 consumption of the future economic benefits embodied in
18 a depreciable asset affects depreciation expense for
19 the current period and for each future period during
20 the asset's remaining useful life.
21 I'd now like to discuss some of the
22 options available for rate setting. Manitoba Hydro is
23 recommending that the Board accept IFRS-compliant
24 depreciation by moving to the ELG procedure for
25 depreciation with current levels of componentization.

1 We believe that that is the option. It is the best --
2 in the best interest of the public.
3 There are, however, some alternatives.
4 The Board could accept IFRS compliant depreciation but
5 move to the ASL procedure for depreciation with
6 additional componentization requirements or the Board
7 could reject IFRS compliant depreciation and order
8 Manitoba Hydro cont -- to continue with the ASL
9 procedure and current levels of componentization for
10 rate setting purposes.
11 If we were to maintain current ASL
12 methods and further increase the number of asset
13 components we would need to determine, again, what new
14 component groups would be required in order to comply
15 with IFRS. As -- as Ms. Bauerlein indicated, there
16 would be additional componentization. Our Appendix
17 11.49 provides some examples of where additional -- we
18 believe additional componentization would be necessary,
19 but that is not meant to be a complete list of new
20 components.
21 We would have to go through the same
22 analysis that we did in 2010 in order to determine the
23 full list of additional components required. And then
24 for each new component group we would have to determine
25 actual historical cost by installation year. That

1 would involve revisiting all of those historical asset
2 accounting records, recalling capital work orders and
3 analysing them in order to determine the nature of the
4 expenditures that were incurred.
5 And in some cases where the accounting
6 records were insufficient to apply the -- to determine
7 the breakdown between new components, we would need to
8 obtain engineering estimates in order to break those
9 costs down. Okay. It's a significant amount of
10 additional work would be required and we believe that
11 it would be a similar work effort to what was involved
12 in the lead up to the 2010 depreciation study.
13 All of that would still result in a
14 similar increase in depreciation expense. So the
15 depreciation expense that would be charged would be
16 very close to what it would be under ELG with a whole
17 lot of additional administrative effort and cost.
18 There's a cost not only to convert, but an ongoing cost
19 to maintain. As Ms. Bauerlein indicated, that
20 additional degree of componentization would require
21 that all of our ongoing processes be modified such that
22 costs go forward were captured at that lower -- lower
23 level of detail.
24 That's not just a few accountants
25 working in the head office that have to allocate costs.

1 That's every person that's captured charging time to a
2 capital project, everyone that's involved in purchasing
3 for those capital projects. It's a very significant
4 impact to the Corporation.
5 Okay. We believe it would take
6 approximately two (2) additional years to complete that
7 further level of componentization. And based on our
8 past experience for the 2010 depreciation study we have
9 a high-level est -- cost estimate of approximately 2 to
10 $3 million in order to perform the associated analysis
11 and conversion. And that is -- breakdown of that cost
12 is detailed in the response to PUB/MH Round 2 Question
13 59(a) and (b).
14 If, on the other hand, the Board were to
15 reject IFRS-compliant depreciation and -- and order
16 Manitoba Hydro to continue with the ASL procedure and
17 current level of componentization for rate setting, we
18 would have differences between the depreciation used
19 for financial reporting purposes, which would have to -
20 - still has to be compliant with IFRS, and depreciation
21 used for rate setting.
22 Those differences would need to be
23 recognized in a regulatory deferral account. We cannot
24 avoid this requirement. And that regulatory deferral
25 account, in order to support the calculations, we would

1 require two (2) full asset accounting sub-ledgers.
2 The regulatory deferral account must be
3 amortized, and amortization of that deferral account
4 affects net income which reduces the difference in
5 depreciation between financial reporting and rate
6 setting.
7 The process for maintaining two (2) sets
8 of asset sub-ledgers would be onerous, time consuming,
9 costly, and confusing. It would impact monthly and
10 quarterly reporting, forecasting requirements, audit,
11 and depreciation study requirements.
12 We need to consider the long-term
13 implications of this approach. In the first year or
14 two (2) after implementation, it would not be that
15 difficult to track accumulated depreciation for rate
16 setting versus accumulated depreciation for financial
17 reporting purposes.
18 But as time goes by, those two (2) sub-
19 ledgers will diverge. And the processes around trying
20 to reconcile those costs and those -- that accumulated
21 depreciation will get more and more complex over time.
22 Depending on what policies, what exact
23 package of accounting policies were accepted and
24 rejected, you could have various differences in those
25 ledgers that make it much more -- more complex.

1 Manitoba Hydro's a very big, asset-
2 intensive company with many billions of dollars' worth
3 of assets. This is not a simple exercise in order to
4 contain two (2) ledgers.
5 THE CHAIRPERSON: Could we spend a bit
6 of time talking about slide 56, the last bullet on that
7 slide? So the amortization of deferral account will
8 impact on income, reducing different and precision,
9 okay, and so on.
10 But at the end of the day, what's the
11 difference in depreciation costs versus ELG versus
12 staying with -- with the current methodology, kind of
13 methodology? What -- what would be the depreciation
14 expense difference? Could you -- could we pull that
15 out of the --
16 MS. MICHELLE HOOPER: I think --
17 MR. DARREN RAINKIE: Oh, sorry, Mr.
18 Chair. We're jumping to the mic here. I've been awful
19 quiet this morning, so I -- I think I'm due one (1). I
20 was resigned to let our experts here fill you in on
21 this issue, but I think this in the PUB -- may be in
22 the PUB Board book of documents, at least the summary
23 of it.
24 But in the response to the Second Round
25 PUB 21(a) to (c), we provided a scenario where we -- we

1 did just that, where we said, Okay, we would -- we'd
2 have to record the differences in a regulatory deferral
3 account and amortize that account over a period of
4 time.
5 And, you know, using kind of a
6 mechanical calculation of what would happen to the 3.95
7 percent rate increases, I think they went to 3.90
8 percent, like literally a basis point or two (2) away
9 from the -- the -- what we're -- what we have in our
10 forecast.
11 So really, we're getting back to the
12 same place with these three (3) options. If we -- if
13 we go to ASL and do -- go through all the work effort
14 to recomponentize a hundred (100) years worth of plant
15 records, we're going to come up with a similar level of
16 depreciation as ELG.
17 If we say, Let's divert for rate setting
18 from financial reporting and let's use the Canadian
19 GAAP ASL method with the requirement of a rate-
20 regulated account to be deferral -- deferred, we're
21 coming back to the same -- to the same answer.
22 So the question becomes: Why? Why
23 spend that money for customers? I mean, the Board is
24 asking us to -- to be lean on our operating costs. Why
25 would we want to do that if we're coming back to the

1 same thing?

2 And this is really an issue of working

3 smarter versus working harder. You know, there's

4 always two (2) ways to do things in life. You can plan

5 something out and use a methodology, an elegant

6 methodology like ELG to capture this. Or we can try to

7 do this through bull work, through going through a

8 hundred years of records, through breaking our plant

9 accounts down into small, little, minute amounts. But

10 -- but why do we want to do that? Why do we want to

11 impose those costs on customers?

12 And -- and, you know, you asked me

13 questions a week or so ago about what are we doing to

14 monitor our assets. Well, I would rather have the

15 asset accounting folks, you know, Ms. Hooper who has

16 worked on this for five (5) years. Every day -- every

17 time I come into the office on Saturday and Sunday

18 she's there working on this and Mr. Martin behind me.

19 I would rather have them looking at how we move forward

20 with the asset build that we have planned rather than

21 going through the last hundred years of records to -- I

22 -- I can't see the benefit of it.

23 THE CHAIRPERSON: But I'm trying to

24 dissect the difference between the accounting choice

25 you made for IFRS versus the choice we have to make as

1 well, which is, you know, rate setting on -- based on
2 GAAP -- Canadian GAAP versus -- so I'm trying to
3 segregate the two (2). I'm trying to make sure we
4 understand and put on the table all of the -- the pros
5 and cons of each of those major decisions. So let's
6 get back to -- you know, the -- the -- so leaving aside
7 ASL versus ELG on -- on the IFRS accounting, go back to
8 -- to Canadian GAAP versus another -- you know, versus
9 IFRS.
10 MR. SVEN HOMBACH: Mr. Rainkie, if it
11 helps I think the reference that you're looking for in
12 the book of documents is page 52 in Volume VI.
13 MR. DARREN RAINKIE: I'm not sure if
14 the Chairman's going to another point or not, so I -- I
15 think we'll let him lead.
16 THE CHAIRPERSON: We need to under --
17 this is a cri -- I think a critical point that we need
18 to ventilate so that we understand what's going on
19 here.
20 MS. SANDY BAUERLEIN: I -- I'd actually
21 like us to turn to -- it's an IR response. It's PUB-
22 II-21 and it's page 5. I think this is -- is where we
23 can -- we can direct you, Mr. Chairman. So what this
24 scenario was doing, Mr. Chairman, was it was assuming
25 the continuation of the CGAAP. So it's not saying --

1 it's -- it's assuming that we continue with -- with our
2 current level of componentization and we continue that
3 we do not meet the requirements of IFRS. So we're --
4 we're doing something different. It -- it's the option
5 number 2 in alternative options for rate setting
6 purposes.
7 And what this -- to just kind of walk
8 through this with you is it was showing the impact to
9 our retained earnings as a result of a couple of
10 things. One (1), we would continue with CGAAP and the
11 other thing is we were assuming the continuation of
12 negative salvage to kind of offset that -- that -- so
13 it's continuing with current practice. So again, we
14 could do a scenario with or without, but this was
15 assuming current practice which is the ASL method and
16 the inclusion of net salvage.
17 So you can see that if you look at the
18 difference really on the second in two (2) boxes. So
19 it shows the depreciation expense reduction if we were
20 to continue with CGAAP ASL of approximately $1.2
21 billion. But then for financial reporting purposes, as
22 Ms. Hooper indicated, we have to amortize that
23 difference between what financial reporting requires
24 versus what rate setting requires.
25 And that amortization -- and we've

1 chosen a -- a ten (10) year amortization period --
2 would result in a one point-five-eight (1.58) decrease
3 to retained earnings. Or actually, sorry, the
4 depreciation expense increase -- hold on a second.
5 I've got to -- I've got to think about this again for a
6 sec.
7
8 (BRIEF PAUSE)
9
10 MS. SANDY BAUERLEIN: Oh, I'm -- I
11 guess -- I guess this example gets a little bit
12 confusing because it actually has two (2) options and
13 it has taking net salvage out. So I have to look at
14 this again. So I'm going to step back again. So the
15 first is we now have the provision for net salvage so
16 that results in a reduction to rate -- retained
17 earnings of $2 billion.
18 We would have to amortize that as a
19 rate-regulated account because again IFRS requires that
20 you remove net salvage. So that would have the offset
21 of the 1.2 billion. So that -- those first two (2)
22 lines are de -- dealing with the impact of net salvage.
23 It's the next two (2) lines that I'd want to look at.
24 The first line again is the effect of
25 the amortization of the change in depreciation methods.

1 So again we're looking at two (2) -- the difference
2 between -- the one point five (1.5) and the nine
3 twenty-one (921) would be the difference between con --
4 maintaining a CGAAP ASL method versus being compliant
5 with IFRS.
6 So there, Mr. Chairman, those two (2) is
7 the difference in your retained earnings as a result of
8 continuing with your CGAAP ASL versus moving to IFRS.
9 We did note that we calculated what this would do on
10 impact on rates, and we've calculated that that impact
11 would be about a 3.90 percent rate increase rather than
12 a 3.95 percent increase.
13 So overall, if we were to continue with
14 our current practice of depreciation, which is
15 including net salvage and continuing with the CGAAP
16 method, it would result in a net change to retained
17 earnings of $100 million. So it is trying to -- and
18 again this example may be a little bit confusing
19 because we have two (2) scenarios in there. One we're
20 assuming continuation of negative salvage, and we're
21 also con -- assuming continuation of the CGAAP method
22 of depreciation.
23 The first two (2) are showing the net
24 impacts of the net salvage. The next -- the -- the
25 third and fourth lines are showing the impact of

1 changing depreciation methods.

2 MR. DARREN RAINKIE: Mr. -- Mr.

3 Chairman, I think if we flip -- I'm sorry, I'm not sure

4 I'm -- we're on the same page as you, and I do want to

5 make sure because this is obviously important in your

6 mind.

7 If we flip the page back to page 4 in

8 that -- in the IR that we're in right now, Diana, if we

9 could do that and -- and present the table, this is a

10 scenario where we eliminate net salvage but we continue

11 with the Canadian GAAP ASL. And that would reduce

12 expense, or increase retained earnings by a -- by about

13 $1.2 billion over twenty (20) years.

14 The next line down says that, Well, we'd

15 have to amortize that difference -- that regulatory

16 account into our -- into our income, so that's going to

17 increase depre -- depreciation expense by $921 million,

18 or reduce retained earnings by nine twenty-one (921).

19 And the question here was, Well, what --

20 what kind of a rate increase would result out of that

21 scenario? So we -- we calculated an even annual rate

22 increase of three point nine-o (3.90) versus the three

23 point nine-five (3.95) that we've applied for and we

24 have in our forecast.

25 So that gives you obviously a smaller --

1 a little smaller rate increase is going to reduce
2 retained earnings by $184 million, I suppose. And
3 there's a few other small puts and takes, but at the
4 end of the day when you go down to the end of that
5 chart you see that the difference of all of that is $62
6 million over twenty (20) years in terms of our balance
7 sheet. You know, 62 million out of $5.6 billion worth
8 of retained earnings.
9 So once again I think the question on
10 Manitoba Hydro's mind is, Why would we do something
11 different? It's not going to result in -- or shouldn't
12 result in a different rate increase. Why would we
13 spend more ratepayer money on administration? Let's
14 use -- let's work smarter, not harder, by breaking our
15 books into tiny pieces and going back a hundred years
16 on hand ledgers.
17 Let's look forward. I want my asset
18 accounting folks, you know, to be helping the
19 Corporation move forward into the big investment that
20 we have, not going backwards, so. Hopefully that
21 answers your question, sir.
22 MS. SANDY BAUERLEIN: I apolo --
23 MR. DARREN RAINKIE: It took us a while
24 to get there, but --
25 MS. SANDY BAUERLEIN: -- I -- I was

1 actually looking -- I didn't remember that there was
2 this previous example on page 4. I quickly looked and
3 -- and grabbed page 5, but page 4 is clearer because
4 it eliminates that net salvage issue.
5 THE CHAIRPERSON: I'm sorry, Ms.
6 Hooper, I'm interrupting you. So go ahead, please.
7 MS. MICHELLE HOOPER: No, that's --
8 that's perfectly fine. Are there any other questions
9 with respect to our options for rate setting purposes?
10
11 (BRIEF PAUSE)
12
13 THE CHAIRPERSON: No further questions,
14 thank you.
15 MS. MICHELLE HOOPER: Okay. Okay, in
16 that case I'd like to continue with some -- some reply
17 to specific areas of concern that have been raised by -
18 - throughout the -- throughout the hearing to date.
19 The first concern that has been raised
20 primarily by the MIPUG is that Manitoba Hydro's
21 financial asset records are not sufficient to support
22 the ELG method of accounting that we're recommending.
23 We would like to assure you that our records do in fact
24 contain detailed historical data, as I indicated
25 earlier when I talked about our conversion exercise.

1 For asset additions, historical asset
2 additions, Manitoba Hydro has the cost by installation
3 year for each depreciable component group. So right
4 back to the beginning we know what our level of
5 investment was and how much was invested in each
6 component group.
7 For asset retirements the nature of the
8 data can be separated into three (3) different
9 categories. For three hundred and sixty-five (365) of
10 our component groups, or 94 percent from a volume
11 perspective of our component groups, we have the -- we
12 know the install -- original installation year for all
13 of the retirement activity that has occurred in those
14 accounts.
15 So for 94 percent of our asset component
16 groups we have full and complete asset accounting
17 records to support the depreciation study. Okay. We
18 have twelve (12) component groups where we do not have
19 full installation year information. Three (3) of those
20 component groups have a -- a -- original installation
21 year for a subset of the data in that area. We're
22 looking at things like distribution meters where we
23 have a very high volume of activity. We have eleven
24 (11) years worth of retirement information on those
25 accounts that spans all vintages of historical

1 additions.

2 Okay. For the remaining nine (9)

3 accounts in this group we have determined the ending

4 population balance for those accounts. So we know from

5 the underlying equipment what our population looks

6 like. There are some estimates involved in that, but

7 we believe that we have a representative population

8 that is reflective of the assets -- the physical assets

9 of the Corporation. And from that, we're able --

10 because we know the original installation year and the

11 transaction year of the retirements, we're able to

12 determine when those assets -- the ages of those assets

13 that came out of service.

14 For ten (10) component groups, which is

15 les -- less than 3 percent, about 2 1/2 percent of all

16 of our component groups, we were unable to determine

17 original installation year. And so for those ten (10)

18 accounts the installation year has been statistically

19 derived using Iowa curves by Gannett Fleming.

20 We also wanted to just have a little bit

21 of a discussion about the nature of the asset

22 accounting records as compared to the asset maintenance

23 records that are used by the operational staff for

24 asset condition assessments. So there was some

25 discussion during the oper -- the operations panel

about the nature of the data that's captured in those systems. And we wanted to just explain that the purpose of asset maintenance records is to track past and future maintenance work on individual pieces of equipment.

So those records are used by the operational folks in order to schedule maintenance, in order to predict future maintenance requirements, in order to assess what -- whether or not it makes sense to continue to maintain assets or to replace them. It's not the purpose of those systems to track the financial investment in -- the historical financial investment in those assets.

That's a sunk cost. It's not relevant to the decision as to whether or not to continue to maintain or replace those assets. Those systems are also not designed to track past equipment that we no longer have. They're designed to track equipment that we have today at the individual maintainable piece of equipment level.

Okay. The purpose of the financial accounting records, on the other hand, is to track investment dollars. And we track investment dollars by installation year by component group in order to facilitate depreciation calculations. The financial

1 records do not contain information on individual pieces
2 of equipment.
3 Okay. So we have information on poles
4 generally and when the dollars were invested in poles
5 and when that investment was retired. We do not have
6 on the financial asset records, records of each
7 individual pole that makes up those totals.
8 Okay. So in order to get a full
9 appreciation of the population, you need to look at
10 information from both systems.
11 Okay. The maintenance systems do
12 contain some financial information, but it is not
13 complete. So for example, our substation asset
14 maintenance system, they do have purchase order --
15 purchase price information for many of their larger
16 pieces of equipment, so things like power transformers
17 and smaller transformers.
18 For the majority of the population, they
19 actually have information in their system that shows
20 what the original purchase price was and the
21 manufacturer date and the installation date of those
22 pieces of equipment.
23 They don't tend to have that information
24 available for smaller pieces of equipment.
25 When you look at some of the other

1 operational systems, the nature of the data that's been
2 captured over time differs. So the generation system
3 uses a completely different system that captures a lot
4 of different information.
5 A lot of their historical information
6 was captured by way of photos rather than filling out
7 data fields. So they have pictures, for example, of
8 the name plates from individual pieces of equipment.
9 But in order to determine installation date, they have
10 to -- somebody has to actually go look at that picture
11 and zoom in and try and read from the picture what the
12 -- what the date was.
13 Okay. So just to understand. And for
14 each area of the Corporation, a different maintenance
15 system has been used historically. So the nature of
16 the information differs.
17 We also use different definitions for
18 service life. For asset condition purposes, their
19 service life relates to the typical lifespan of an
20 asset provided it's not replaced sooner for other
21 reasons.
22 And there was a -- there's a definition
23 of that in the asset condition report, and I don't know
24 what -- okay. But it specifically says in there that
25 they're not considering things -- early retirement-type

activities.

So they're not looking at the poles that come out of service early because they're hit by a car or there was a forest fire or there was some need for a system capacity change that required us to change our equipment.

For depreciation purposes, we have to consider all of the factors that could result in retirement. And as a result, for depreciation purposes, this average service life that we're using tends to be shorter than the service -- than the expected service life that's being used for asset condition purposes.

We'd also like to just have a little bit of a discussion with respect to the appropriateness of using ELG. Manitoba Hydro believes that EL -- the ELG method is appropriate for long-lived assets.

The argument that it's not appropriate for long-lived assets is based on the premise that hydraulic generating assets provide the most benefit many years after initial in-service.

That approach would be linking depreciation to the profitability of a plan -- of plant assets, and that is not an appropriate method of depreciation.

1 Excluding technology changes, the
2 decline in service potential of an asset is based on
3 its consumption, not the revenue that it generates.
4 Revenue is dependent on a number of factors that do not
5 impact physical wear and tear of an asset, such as
6 commodity and export prices, exchange rates, operating
7 costs, and many other factors.
8 It's dependent on variables that are
9 much more unpredictable and can change dramatically
10 from year to year.
11 Setting depreciation rates based on
12 variables that influence revenue would re -- lead to
13 erratic swings in depreciation rates between studies.
14 The ISB has formally rejected the concept of
15 depreciating an asset based on the revenue that it
16 generates.
17 And, overall, we should not be
18 discounting the ELG method because it provides an
19 improvement to how an asset is depreciated. It better
20 matches the pattern of depreciation expense to the life
21 expectancy of the individual pieces of equipment that
22 make up those asset component groups.
23 Okay. With that, if there's -- or if
24 there aren't any questions regarding my portions of the
25 presentation, I'll pass -- pass this on to Mr. Fleming

1 to -- Mr. Kennedy, sorry, to deal with some of the more
2 technical questions that were -- have been raised.
3 MR. LARRY KENNEDY: Thank you. My --
4 my forefather in, you know, in Harrisburg,
5 Pennsylvania, Mr. Fleming who formed the company a
6 hundred years ago, would be happy to know he's still
7 alive and presenting in public -- public forums. I've
8 been asked by Manitoba Hydro to include just a few
9 comments on some of the areas of concern from -- from
10 my perspective. And so here we go. And I'm -- I'm
11 keeping -- I -- I put my watch out in front of me, so,
12 Mr. Chairman, I hope I can -- I -- I'm going to press
13 the accelerator pedal a little bit to try to ensure
14 that we meet the -- the lunch time.
15 The ELG method is reasonable and it is
16 appropriate. It's recognized in most of the textbooks
17 as being the most mathematically correct method of
18 depreciation for group accounting practices. The --
19 there's been some -- some evidence in this proceeding
20 that the ELG method is not widely accepted. Quite
21 frankly, with all due respect to all parties, I don't
22 think that's quite correct.
23 The equal life group method is, while I
24 would say not the most used method, because that would
25 not be factual, it is used in various pockets and used

1 throughout both Canada and the United States. I'll
2 give an example on that in -- an example in Alberta.
3 Virtually every utility in the Alberta mar -- Alberta
4 jurisdiction uses the equal life group procedure with
5 one (1) small exception. Most of the maritime
6 utilities use the equal life group method. The CRTC,
7 for example, mandates the use of the equal life group
8 procedure.
9 Throughout the United States, we have
10 seen some pockets adopt it and some -- and some pockets
11 not adopt it. So I don't think it's fair to
12 characterize it as it's -- it's this little method that
13 was bought up by the telecommunications in the 1970s
14 and not used anywhere else. That, in fact, is -- is
15 not accurate. We did provide a response to -- to
16 PUB/MH-I-42(b) that -- that outlined some of the -- the
17 utilities that -- that, in fact, do use the equal life
18 group procedure.
19 THE CHAIRPERSON: Mr. -- Mr. Kennedy, I
20 guess, you know, CRTC deals with a different technology
21 than --
22 MR. LARRY KENNEDY: Yes.
23 THE CHAIRPERSON: -- than a utility --
24 the -- the utility does. An -- an obvious issue that
25 will be raised this afternoon probably will be that,

1 you know, it -- is it most appropriate for a -- a
2 industry where technology changes very rapidly as
3 opposed to ASL? Now, we can address that now or we can
4 wait this afternoon.
5 MR. LARRY KENNEDY: Well, we can -- we
6 can talk about it this afternoon a bit, but I will
7 address it now. Only -- that was kind of the genesis
8 of the equal life group procedure was by the
9 telecommunication companies. The -- and largely, they
10 adopted it because it was really critical for them.
11 They had a strong need for additional componentization
12 of that plant because of the short life variability and
13 to mitigate losses on retirement, quite frankly, that -
14 - that was appearing into their balance sheet.
15 So in the 1980s and '70s --
16 predominantly the 1980s when we came up with these
17 things called personal computers and computers that
18 could do the -- the amount of calculations, quite
19 frankly, with the push of a button now. The -- the
20 telecommunication industry was really the first to see
21 that dire need of this additional level of -- of
22 precision within the depreciation rate calculations.
23 Thus the CRTC was actually even a little bit further
24 ahead than the FCC in the United States and in
25 mandating it. FCC accepted it and recognized it. In

1 Canada, the CRTC went as far as to mandate its use.
2 The -- over the period from, I would
3 say, 1980 through the mid-1990s, some pockets, Alberta
4 was one (1), various jurisdictions looked at it. The -
5 - the argument against it was the -- the bump that you
6 see in equal life group in the immediate years of
7 implementation of equal life group procedure in an aged
8 utility.
9 Now along comes -- and -- and then I
10 think the -- the distinction was along came the years
11 2000, and we started getting more technology introduced
12 into the technol -- into the asset bases of electric
13 and gas utilities. Control systems, smart meters, for
14 example, would be ones where we see this fast pace of -
15 - of change. The control systems used in the -- the
16 electric utilities are far different now. And in fact,
17 they're not even mini computers anymore. They're
18 powerful computers that drive those control systems.
19 They are very short-lived assets.
20 Con -- the -- so we've started to see
21 the introduction of some of this technology change,
22 combined with, I would suggest, the -- as assets were
23 replaced, the -- the focus on the componentization and
24 how we componentize assets increased. And so we
25 started seeing, I would say in the mid '90s, more and

1 more utilities thinking about equal life group again
2 that weren't telecommunication utilities.
3 And we've seen, particularly now with
4 the IFRS, kind of this question come up, is this now
5 the right time for -- to deal with the precision
6 requirements of IFRS without having to go through all
7 the detail that Ms. Hooper has gone through for the
8 last five (5) years, so?
9 So why I will admit, and then I do agree
10 the telecommunication industry was really the
11 forefather and -- and kind of the leader, and that we
12 are seeing it more widely accepted in other industries.
13 The -- and kind of the second bullet
14 point on this slide deals with the -- the concept that
15 I talked about this morning. The -- it -- it is far
16 better in dealing with the dispersion of the
17 retirements at the expected time of retirements.
18
19 (BRIEF PAUSE)
20
21 MR. LARRY KENNEDY: The -- the question
22 was, Well, gee, is Manitoba Hydro going to be really
23 different than all the other hydroelectric utilities in
24 the country? And the answer is, quite simply, no.
25 The -- the equal life group procedure --

1 and I had 'method' on some of these slides, and I
2 thought I'd caught all those, the technical --
3 technically correct term is 'equal life group
4 procedure', is being recommended by Manitoba Hydro, or
5 for Manitoba Hydro.
6 And we contrast that to the other Crown
7 utilities across the country, because in -- in most
8 circumstances, the -- the large hydro operators are, in
9 fact, Crown utilities.
10 The -- the Crown -- some of the other
11 Crowns people, like Ontario Power Generation or --
12 would -- would have actually decided to move to USGAAP
13 rather than IFRS. And so it's not really a fair
14 comparison to say, Well, gee, they have a lesser level
15 of componentization under ASL, therefore ASL is good
16 for prob -- you know, for the -- the depreciation, or
17 they're following a different accounting standard.
18 They're following the USGAAP, which doesn't require the
19 level of precision that the IFRS standard would. So we
20 have that group of utilities follow -- that have moved
21 to USGAAP.
22 In my experience across this country, I
23 would say close to half the utilities, maybe slightly
24 less, have decided to move to USGAAP rather than IFRS.
25 Now, there's some very specific requirements around

1 moving to USGAAP. It's not just like -- it's not like
2 opening door number 2 and I can do USGAAP. There's
3 some -- some requirements around that. And a number of
4 utilities have, in fact, found mechanisms to allow
5 that. And there is, in fact, some other issues that go
6 with that in terms of time. You know, how long they
7 can stay there, et cetera.
8 The other group of -- of hydro electric
9 utilities would, in fact, be those that are using ASL,
10 but using it at a far more granule level -- granular
11 level, or in fact, following unit depreciation.
12 Companies like SaskPower actually do follow unit
13 depreciation. So they're doing, if you will, ELG on
14 steroids. It's -- it's right down to the unit -- right
15 down to the unit basis. Why do we call it ASL?
16 Because it's a very straight line. In one (1) rate
17 fall, the investment in that -- in that asset is one
18 (1) asset, so it's -- it's very componentized.
19 And so generally, if -- if we run across
20 the country, we'd find that the utilities -- the
21 hydroelectric utilities are falling into one of those
22 two (2) groups, the -- the USGAAP group, or the much
23 more componentized, and in fact, componentized to the
24 extent of unit depreciation.
25 The -- as we talked about this morning

with my little two (2) asset example, the ELG meth -- procedure, in my -- in my view, promotes generational equity. The -- the acquisition -- accusations that it's front-end loaded is, quite frankly, false.

It -- it's a better and more robust method to deal with the estimation of the consumed service value of assets over the period of time of which they're in service. The -- a -- a vertically -- vertically integrated utility such as Manitoba Hydro have a -- an array of long and short-lived assets, both in varying accounts, but within the same account.

We talked this morning about poles and -- as compared to cross-arms being in the same account. We may have some analog controls and digital controls in a control account. There's -- there's this variety of -- of life expectations within these accounts that -- that are really a function of the size and the magnitude of companies such as Manitoba Hydro.

The -- the change to ELG will increase the depreciation for assets with a life lesser than the average service life, as it ought to. If you have a five (5) year life asset, you have to depreciate it over five (5) years. The IFRS Standard 16 recognizes that.

It doesn't mean it's front-end loaded.

1 It doesn't mean it's accelerated. It's the -- giving
2 the appropriate recognition to -- to the life of the
3 asset.
4 The same increase, and I've talked about
5 this, this morning on my two (2) asset examples, the
6 ELG gives you the same result as would componentization
7 down to a unit level or increased level of
8 componentization.
9 I think the -- the report that we filed
10 with Manitoba Hydro, I -- is filed as part of this
11 application as part of Appendix 11.49, and it came to
12 the conclusion that there's little difference in the
13 increased level of componentization using ASL and the
14 use of the equal life group procedure.
15 The -- in my view, even given all the
16 options, the ELG is the one that's going to best
17 achieve that generation of equity, you know, when you
18 consider the amount of work that's going to be involved
19 in -- in the -- the effort to -- to anything other.
20 I'm going to move -- change my -- my hat
21 a little bit and talk about net salvage. In my view,
22 the recovery of net salvage is -- is the right
23 practice. It's sound regulatory practice, and I do
24 believe that to better achieve and most properly
25 achieve generation of equity, the inclusion of net

1 salvage is appropriate in the rates.
2 The -- I describe that at page Roman
3 Numeral ii-ii of the Gannett Fleming report, where we
4 talk about the -- the inclusion of net salvage. I do
5 recognize that there is needs and -- and Manitoba Hydro
6 did make a policy decision not to implement this as
7 part of the -- as part of their move to the IFRS.
8 But from a conceptual level, I think the
9 -- the practice of including net salvage is -- is
10 appropriate. As I indicated in these bullet points,
11 the depreciation expenses is intended to recover all
12 costs associated of an asset, including the cost of
13 decommissioning.
14 The -- my reference back to page ii-ii
15 of my Gannett Fleming report is the definition of
16 depreciation that really comes from FERC. And it comes
17 from FERC Part 101 on the -- on both the gas and the
18 electric sides that describe depreciation as the
19 consumption of service value less the salvage. I --
20 the -- the consumption of service value, then, in the
21 next paragraph defines service value as cost less
22 salvage.
23 Putting those two (2) together, it's
24 obvious that the FERC definitions, which is really the
25 definition of -- of depreciation expense that's widely

1 recognized within the regulatory practices in
2 jurisdictions, it's the one (1) that's in virtually all
3 the uniformed system of accounts that I've seen, it's
4 clear that it is the intention to recover net salvage
5 in the -- in the -- the depreciation rates.
6 The inclusion of net salvage provides a
7 -- an ability to decommission assets, even when it's
8 not removed. And including net salvage, I -- I believe
9 strongly supports the concept of generational equity.
10 Ms. Hooper just alluded to this, and has
11 spent the last five (5) plus years of her life making
12 sure that I can make this statement. Manitoba Hydro
13 records are definitely sufficient for applying the
14 equal life group method. In fact, I -- I consult with
15 thereabouts of 80 percent of the utilities across this
16 country. And I would suggest that the Manitoba Hydro
17 plant accounting records are at the top of the group,
18 or within the very top of the group of regulated
19 utilities that I have the opportunity to work with.
20 Their -- their plant accounting base,
21 following all the work that Ms. Hooper and her crew
22 did, is in fact, very excellent. And there's no doubt
23 in my mind, nor should there be in anybody's mind, that
24 those -- that plant accounting base is not sufficient
25 to support the equal life group procedure.

1 As -- as Ms. Hooper alluded to, Manitoba
2 Hydro, in 94 percent of their accounts, has complete
3 full back -- back to day 1 retirement history,
4 including the installation date. That's incredible. I
5 mean, we're talking on company of one hundred (100)
6 years of transactions or thereabouts. To have that
7 level of detail on all of them is -- isn't -- is --
8 isn't actually, it might be very good -- or very
9 incredible.
10 The remaining 6 percent, 3 percent of
11 those are ones where we have definitely sufficient
12 information to which we could make a very -- a very
13 educated estimate of -- of the vintage of the original
14 -- vintage of the retirement transactions. Don't
15 always have to go back to the original orders. We
16 could, in -- in some cases, but we had other
17 operational systems, the pole management system, and
18 that type of thing that allowed us to -- to estimate
19 those with a strong degree of confidence.
20 And then that leaves the remaining 3
21 percent that -- that may be work to come, but it's --
22 it's an amazingly small piece of this Company as a
23 whole. And to suggest that there is insufficient data
24 is, in my mind, just not accurate, because this Company
25 has excellent and some of the best plant accounting

1 data that I've seen across this country.
2 The group method of depreciation doesn't
3 require individual asset details, nor should it. The -
4 - we don't need to get down to the unit turbine 1 ex-
5 generating plant.
6 We don't need that level of detail to --
7 to build that Iowa curve and to go through that
8 retirement rate analysis that I was talking about this
9 morning. Where we have it, it forms one (1) of the
10 many inputs.
11 Depreciation looks at -- and when we
12 build those life analysis -- we had a question this
13 morning from the panel about why we saw life change on
14 poles from thirty-one (31) to fifty-five (55) years.
15 We had more and better information other than just the
16 -- the detailed retirement information.
17 We take those into account. We talked
18 about our meetings that we had. I got to know -- I got
19 to know Winnipeg very well over the last few years as
20 they were going through this process and talking with
21 their operation staff.
22 So there's much more information, and to
23 suggest that only the historic retirement information
24 drives that curve selection is -- is fact, not
25 accurate. There's much more that ought to go into it.

As I -- I teach life analysis and courses, both at the Society of Depreciation Professionals and with other -- and other -- other groups. And one (1) of things I stress to them is that exact fact. Don't get carried away.

I like statistics. It's what I do for a life. But we -- we can't get -- we can't get focussed on only the statistics. We have to look at the broader view. Otherwise, I think we're not doing our job effectively.

The -- the question came up about the need to use -- with the use of the equal life group procedure, you have to have the accumulated depreciation by vintage year. This has -- this has come up in -- quite frankly, since about 1940, when we started talking about the equal life group procedure.

The -- and I want to be clear, here. The -- the method that we used and the process that we used to develop the dep -- the depreciation rates for Manitoba Hydro use what we referred to as a whole-life approach. It says, I'm developing a depreciation rate. I want that ten (10) year estimate, I want -- I want a life curve that's based on a set of parameters that can be applied to all plant.

In that calculation, there is nowhere in

1 the calculation that we look at the accumulated
2 depreciation balances. It's purely the life, the
3 retirement dispersion curve, and -- and the current
4 surviving investment in your asset ledger, not your
5 accumulated, but your asset ledger by vintage year.
6 Manitoba Hydro has all of those, as I just talked
7 about, in excellent detail.
8 Where you would need accumulated
9 depreciation information is if you were following a --
10 a remaining life calculation in the development of your
11 depreciation rates. That practice is almost
12 exclusively followed in the United States, and almost
13 exclusively not followed here in Canada.
14 And that comes back to the way that
15 we've implemented equal life group in Canada over the
16 years is to recognize the benefits of the equal life
17 group procedure without needing that accumulated
18 depreciation information by detailed vintage year.
19 We do the whole-life calculation where
20 the accumulated depreciation does not come into play.
21 And then we calculate that remaining life. And if you
22 remember this morning I talked about that Iowa curve,
23 and from that Iowa curve, we can calculate the
24 remaining life.
25 We actually calculate that remaining

1 life using the ASL procedure. So the -- the comments
2 that -- that we need the -- the accumulated
3 depreciation by vintage to get the remaining life using
4 the ELG may be accurate if we were, in fact, using ELG
5 to determine that remaining life.
6 But we actually use the ASL procedure
7 for that determination. And we are allowed to do that
8 or we -- we find that reasonable because we only use
9 that remaining life as the period over which we
10 amortize that accumulated depreciation variance.
11 It's not used in the detailed
12 calculations of the rate. It's used in the
13 calculations of that variance amount.
14 So we've -- we've really dissected that
15 formula into two (2) pieces, used the benefits of the
16 equal life group to get the depreciation rate, and
17 appropriately used a method to determine the remaining
18 life of the assets. And that is -- we did with the ASL
19 method.
20 That's a long-standing approach that
21 we've used in Canada. It was really largely debated in
22 the 1982 proceeding in Alberta, where we started using
23 the equal life group procedure and we had -- well, many
24 of the forefathers of that development appear in a
25 hearing in Alberta, and we debated how -- how best to -

1 - to go through the whole process.
2 There has been some -- some discussion
3 about if, in fact, this Board was inclined to adopt
4 equal life group to phase it in on only new additions.
5 Again, absent the work that Ms. Hooper and her crew did
6 for the last five (5) years to develop very, very good
7 data, I would say that may have some merit. But that's
8 not the case. We have an excellent database here upon
9 which to apply the equal life group. There's simply no
10 reason to suggest that we can't rely on the data that
11 we have to -- to use the equal life group on all data.
12 And secondly is, as we've heard,
13 Manitoba Hydro has made a policy decision to offset the
14 impact of equal life group by removing net salvage.
15 Quite frankly, that was not necessarily my
16 recommendation to Manitoba Hydro. I would just as soon
17 have seen them in -- leave net salvage in the
18 calculation, but they've -- they -- they've chosen to
19 implement the -- the IFRS and the equal life group by -
20 - by mitigating the impacts by removing the net salvage
21 from the calculations.
22 And kind of in summary -- and I have
23 beat the clock here almost, Mr. Chair, the Manitoba
24 Hydro records really are absolutely sufficient for
25 applying the equal life group method -- procedure. The

1 -- in my view, and I've testified to this many times,
2 is the equal life group procedure is reasonable and
3 appropriate, and where it can be implemented, I think,
4 is the -- is best method for aligning the consumption
5 of the service value of utility assets to the revenue
6 requirement inclusion. And as -- as such, it promotes
7 the intergeneration equity for all ratepayers.
8 And then I think I'm handing back to Mr.
9 Bauerlein.
10 MS. SANDY BAUERLEIN: So as stated at
11 the beginning of our presentation, the collective
12 impact of all the accounting changes with respect to
13 depreciation is a reduction to depreciation expense of
14 approximately 25 million in '14/'15 and 53 million in
15 '15/'16. And I note that this reduction grows to a
16 hundred million after the ten (10) year forecast
17 period, and we've identified in the response to IR PUB-
18 1 -- Round 1, 37(b) that that will grow to
19 approximately 2 billion over the twenty (20) year
20 forecast period.
21 As such we feel that the changes in
22 depreciation expense com -- to comply with IFRS are not
23 negatively impacting customer rates. And as we've
24 discussed, we believe using that one (1) method of
25 depreciation for both financial and rate-setting

1 purposes is in the public interest, that the ELG method
2 is appropriate and reasonable, and that again, Manitoba
3 Hydro has the accounting records necessary to -- to
4 implement the ELG method.
5 So we are requesting the PUB to accept
6 the collective changes being made to depreciation as
7 reasonable and appropriate for rate-setting purposes,
8 including our recommendation to change to the ELG
9 method. And we also want to note that any selective
10 changes, and we've talked about this in some of the
11 prior panels, to Manitoba Hydro's approach in order to
12 justify lower rate increases will again reduce cash
13 inflows and would result in increasing debt levels
14 during this vulnerable period of capital investment.
15 So with that we thank you, and if
16 there's any further questions of any of us...?
17 THE CHAIRPERSON: Looking at those
18 numbers, Mr. Rainkie, I guess that's pretty clear that,
19 you know, we could have -- you could have made a
20 decision to continue with net salvage without unduly
21 impacting depreciation expense. If you look at the
22 lines -- the first, second lines offset against this
23 change in methodology. They're pretty close. So you
24 could have gotten away -- you -- we could have, you
25 know, made Mr. Kennedy happy and kept the salvage value

1 in there.

2 So tell us why you -- you chose to do

3 that at the present time. Would it have meant more

4 cash for the -- the Corporation?

5 MR. DARREN RAINKIE: Well, sir, for the

6 same reason that you and I chatted about it I think on

7 day 1 is that we were -- in the selection of accounting

8 policies as we moved to IFRS, we weren't just concerned

9 about how books looked. We were concerned about rate

10 setting and the impact that that may have on customers.

11 So our approach is, was, and always will be to look at

12 the selection of accounting policies not only for

13 financial reporting purposes, but for rate-setting

14 purposes as well.

15 We were conscious that we're -- there

16 were also some overhead changes on the -- you know,

17 that we're increasing costs on the operating cost side.

18 And so we quite frankly used negative

19 salvage as a means to manage all of those puts and

20 takes to get back to pretty much where we were because

21 we believe the discussion we've been having at this

22 hearing in terms of the investments for Manitobans is

23 what's driving rates, and what we should spend our time

24 here talking about.

25 So, yes, negative salvage value has been

1 a long-standing practice -- regulatory practice in
2 Manitoba probably for two (2) or three (3) decades, if
3 we want to go back. It's a valid concept and there's
4 every reason why we could have maintained it for rate-
5 setting purposes, but in trying to balance all of the
6 changes in -- on the move to IFRS we felt it was an
7 appropriate tradeoff to make.
8
9 (BRIEF PAUSE)
10
11 DR. HUGH GRANT: Can I ask a couple
12 naive questions? One (1) with respect to Mr. Kennedy's
13 presentation, and then another one (1) I just want some
14 accounting advice.
15 So the -- the question I had, Mr.
16 Kennedy, is on your example that you provided on page
17 18. I'm just trying to understand the -- what's going
18 on with this accounting difference. I was asking a few
19 people about this.
20 What I don't find compelling about this
21 example is you don't have any replacement investment
22 going on, right? So you've got this fifteen (15) year
23 -- let's say you've got one (1) asset which is a dam
24 and another asset which is a turbine. One (1) lasts
25 fifteen (15) years, one (1) lasts five (5). You don't

1 replace the turbine.
2 So -- so I was trying to work through
3 your example where you do -- do some replacement
4 investment. And would I be correct then if I -- in
5 year five (5) I replace this turbine for a thousand
6 dollars ($1,000).
7 Would the accruals every year be two
8 hundred dollars ($200) in the average service life
9 example?
10 MR. LARRY KENNEDY: They would be if in
11 -- if -- two (2) assumptions again, and the problem
12 with simplistic examples is they're simplistic.
13 You're correct, we don't have a --
14 reoccurring capital -- reoccurring or replacement
15 capital going in. If we were to assume that you were
16 going to replace that -- that five (5) year turbine or
17 whatever, and it's going to last another five (5)
18 years, and then you would have a -- you would have a --
19 well, the first thing that would probably happen is
20 your life would change slightly. Maybe not.
21 You would have a two hundred dollar
22 ($200) continually accrual from year 6 to 10, and then
23 you would probably start finding that your 10 percent
24 rate is a little bit shy in that last five (5) years.
25 So what you've done in that circumstance is really

1 further enhanced the inequity, and you're going to
2 strongly push out to those guys from years 10 to 15.
3 Now, to take that example -- and -- and hire those --
4 those toll-payers even slightly harder.
5 The -- to take your example one step
6 further, let's assume that we're going to replace that
7 turbine again in year -- in year eleven (11) and have
8 another five (5) years. What would happen is you'd
9 eventually find that your accumulated depreciation
10 account is going to start under funding itself because
11 really you've got this ongoing -- you've got this --
12 you no longer have an average of ten (10) years.
13 Over that fifteen (15) year period you -
14 - you've had three thousand dollars ($3,000) that had a
15 five (5) year life, and a thousand dollars ($1,000)
16 that a fifteen (15) year life. That -- that period
17 ought to have been something more like seven (7) or
18 eight (8). So as -- as time would go on, we'd start
19 having to make adjustments to reflect that -- that that
20 occurrence of that thousand dollars ($1,000)
21 reoccurring and having a continual five (5) year rate.
22 So your weighting would drive you to a lower average
23 service life eventually.
24 DR. HUGH GRANT: Okay. So when -- when
25 I was trying to apply this, I ended up with an annual

1 accrual of the average service life of two hundred
2 dollars ($200) a year throughout because I kept
3 replacing -- I replaced the turbine a couple times.
4 And so taking your average service life
5 example, I ended up with accumulated accruals of only
6 three thousand dollars ($3,000) on assets worth four
7 thousand (4,000), and -- and now they've all fallen to
8 the ground and are useless.
9 So I guess I'm just not sure in terms of
10 your example if something is missing, or you're
11 treating the average service life example -- it's too
12 simplified in terms of how you'd --
13 MR. LARRY KENNEDY: Well, when you
14 start introducing the -- the reoccurring capital,
15 you're right, it's over simplified. What would happen
16 is -- and -- and you found the precise problem. You
17 came to year fifteen (15) and you'd recovered three
18 thousand dollars ($3,000), not four thousand dollars
19 ($4,000).
20 So what would happen is we would
21 probably start recognizing that in -- in a study in
22 years 5 or 6 somewhere, and start looking at, Okay that
23 average service life of -- estimate of ten (10) years
24 is no longer appropriate. It would need to be
25 shortened up. And then we would accelerate the

1 depreciation rate from that period forward to ensure we
2 -- we recover the full four thousand dollars ($4,000)
3 by the end of the -- so.
4 So you're right, the -- the -- as I say,
5 the - - the problem with simplistic examples is
6 sometimes they -- they can be overly simplistic. The -
7 - and what you're finding the reason you're recovering
8 only three thousand dollars ($3,000) rather than four
9 thousand dollars ($4,000) is the -- the losses on
10 retirement that are inherent in that five (5) year
11 asset that the average service life drives.
12 And so realistically what would happen
13 is we -- we would -- made the assumption that that five
14 (5) year asset is fully accrued, but over that period
15 when you've had that reoccurrence of three (3) of those
16 five (5) year lives it hasn't. And in fact, that
17 accumulated depreciation account is -- has absorbed
18 about a thousand dollars ($1,000) of losses on
19 retirements that would have to have something done to
20 it going forward from there.
21 And so that's where you start getting
22 into the -- the inequities of the average service life
23 method.
24 MS. MARILYN KAPITANY: Well, Dr. Grant
25 --

1 THE CHAIRPERSON: Well, we're on that
2 table --
3 MS. MARILYN KAPITANY: Oh.
4 THE CHAIRPERSON: I'm sorry. I was
5 going to say, while we're on that table we might as
6 well address the front loading issue, because it's
7 right there, two sixty-seven (267) versus two hundred
8 (200). Now, this is the point that MIPUG is going to
9 make later, you know, you disputed the front loading
10 part, but it's pretty clear there's a front loading on
11 the ELG.
12 MR. LARRY KENNEDY: I -- I would make a
13 comment to that, Mr. Chair, the numbers are higher, but
14 a higher number doesn't mean it's front loaded. Front
15 loaded has a certain connotation that it's perhaps
16 inappropriately higher. So I will agree it's higher,
17 and -- but I wouldn't agree that appropriately higher,
18 not inappropriately higher, if that makes -- I don't
19 know if that helps clarify that a bit.
20 THE CHAIRPERSON: Okay. Let's -- let's
21 concede that perhaps it's misnamed, but it's
22 nonetheless higher.
23 MR. LARRY KENNEDY: It definitely is
24 higher. And -- but it's higher to recognize that five
25 (5) year asset and to avoid some of the -- the -- as

1 Dr. Grant alluded to, as you go through life if you
2 continually don't recognize that you have that five (5)
3 year asset in your depreciation rates you eventually
4 run yourself into an accumulated depreciation problem
5 that has to be rectified somehow.
6 And so while the -- that -- that higher
7 number really alleviates that over the customers that
8 had the benefit of that first asset providing service.
9 MS. SANDY BAUERLEIN: I did want to
10 note that we have an example from the prior GRA, a more
11 complex example. So we could have an undertaking to
12 provide that example. It has in it replacements and I
13 believe there's also some gains and losses on
14 retirement to demonstrate -- because again, we
15 recognize this was a fairly simply example, if -- if
16 the Board would like.
17 DR. HUGH GRANT: I guess I was just --
18 you know, beware of accountants and -- I just wanted to
19 make -- it just seemed really odd if you just modified
20 this example a bit that your sum of accruals wouldn't
21 equal. So sure, that would be useful.
22
23 --- UNDERTAKING NO. 74: Manitoba Hydro to provide a
24 more complex example from
25 the prior GRA

1 CONTINUED BY DR. HUGH GRANT:
2 DR. HUGH GRANT: The -- the other
3 question I had was in trying to sort out some of the
4 things that are going on here at the same time, one (1)
5 of them would be that you've done a -- is a -- not
6 average service life isn't the right term, but you --
7 you looked at your capital stock and you found out that
8 the remaining life was greater on average than you had
9 anticipated.
10 Is that correct?
11 MS. SANDY BAUERLEIN: Yes, we've
12 changed the -- the service lives of some of the
13 component groups, correct.
14 DR. HUGH GRANT: Could you just --
15 MS. SANDY BAUERLEIN: Through our
16 depreciation studies, yeah.
17 DR. HUGH GRANT: So -- and I -- I know
18 this isn't the correct way of saying it, but a -- a
19 roundabout way of saying is you -- you wrote off your
20 assets too quickly in the past. And -- and so now you
21 find that you've written them down to zero, but
22 actually there's still some value left in them, if I
23 can say that in a simplistic way.
24 How -- how do you deal that in an
25 accounting sense, because if what you're saying is you

1 wrote off your assets too quickly, it means that you
2 took them as expenses in the past that would have been
3 inco -- incorporated into rates. And so in a sense you
4 -- you paid for the -- you paid too quickly for the
5 asset.
6 Now you -- we're in the present period
7 and you find out these assets are still worth
8 something. Does this mean that you now have to charge
9 a new depreciation charge -- cost on the remaining life
10 of the asset? Because it seems like it's kind of
11 double counting that ends up happening, right, so.
12 THE CHAIRPERSON: I wonder if we could
13 hold the response, give you time to think about it,
14 because I made a commitment to Board member Bel that he
15 could get away at lunch time. So let's adjourn for now
16 and we'll get an answer at one o'clock. One o'clock
17 we'll get together again.
18 MR. BYRON WILLIAMS: Mr. -- Mr. Chair,
19 I don't want to interrupt Mr. -- back -- back here, I
20 don't want to harm Mr. Bel's lunch, so I'll be very
21 quick --
22 MR. RICHARD BEL: Meeting.
23 MR. BYRON WILLIAMS: Oh, meeting, of
24 course. Just -- I've conferred with the other
25 Intervenors and I -- I think the only two (2) who will

have questions are Mr. Hacault and myself. And I think in total it will be four (4) hours or less. And I'm not sure how long Mr. Hombach is going to take this afternoon.

I have also talked with My Friend from Manitoba Hydro, Ms. Van Iderstine, and what -- what I'm hoping is -- if need be I could go today, but I would certainly prefer to go tomorrow. That would give me the opportunity, along with My Friends from MIPUG, to confer with Ms. Lee at the end of the day.

So we'd ask the Board to consider that. And I think I've canvassed this with all My Friends in the room.

THE CHAIRPERSON: Okay. Let's -- let's talk about -- we'll talk about that at lunchtime. But thank you for that request, and we'll consi -- we'll give you an answer after lunch. Thank you.

--- Upon recessing at 12:03 p.m.
--- Upon resuming at 1:01 p.m.

THE CHAIRPERSON: I believe that we're ready to resume the proceedings. So before we -- we start the proceedings, I do -- I had -- I had made a commitment to formulate a -- a request. And -- and

1 what I'm requesting is an undertaking by Manitoba Hydro
2 which reads as follows.
3 So Manitoba Hydro is seeking 3.95
4 percent rate increases for the test year and -- and
5 future years. And I would like Manitoba Hydro to
6 undertake to -- to identify that portion of the rate
7 increase being sought which addresses the core required
8 earnings for Manitoba Hydro versus that portion which
9 relates to future investment needs.
10 And I would like Manitoba Hydro to
11 provide that infor -- that information for the test --
12 for '15/'16, '16/'17, '17/'18, and '18/'19. So -- so,
13 for example, three point nine-five (3.95), if it's 1
14 percent for the current test year, that means 2.94 --
15 95 percent is for future investment needs.
16 I'm just -- that's just an example. I
17 just wanted to make -- clarify what my thinking is, but
18 so we have an idea of the portion of the rate that's
19 going to serve future investment needs.
20 And I'm stopping at '19/'20, because I
21 think that's when the numbers started getting red, and
22 so I'd like to go out to the point at which the net
23 operating income becomes negative.
24 MR. DARREN RAINKIE: Sir, we'll --
25 we'll take that undertaking. And it would be good if I

1 could probably read it in black and white in the
2 transcript and -- and think about it, if I have any --
3 I can't ask you questions, but if I need -- if I need
4 any clarification, I'll -- I'll -- we'll think about
5 it, and maybe have a chat tomorrow at some point on the
6 record.
7 But we'll definitely undertake to do our
8 best to answer that.
9 THE CHAIRPERSON: Thank you for that.
10
11 --- UNDERTAKING NO. 75: Manitoba Hydro to identify
12 the portion of the rate
13 increase being sought which
14 addresses the core required
15 earnings for Manitoba Hydro
16 versus that portion which
17 relates to future
18 investment needs for years
19 2015/2016 to 2018/2019
20
21 THE CHAIRPERSON: Now, I notice we have
22 a -- a number of documents before us. So, Ms. Van --
23 MS. HELGA VAN IDERSTINE: Yes. Thank
24 you.
25 THE CHAIRPERSON: -- Iderstine.

1 MS. HELGA VAN IDERSTINE: We've got a
2 few little housekeeping things to do to start. And
3 then, once I've dealt with these exhibits that I'm
4 going to take you through, which are answers to
5 undertakings, I would just like to advise you that the
6 panel would like to answer the question that you posed
7 just before the break, together with clarifying a
8 couple of other answers that -- that had come up and
9 issues that came up during this morning. So we'll just
10 go with that.
11 So the first one is -- will be Manitoba
12 Hydro Exhibit 76, and it is a response to Undertaking
13 number 1, which was to reconcile the capital costs for
14 the Great Northern Transmission Line of 507 million
15 found on page 126 of the PUB's NFAT report, and 542
16 million discussed during oral examination.
17
18 --- EXHIBIT NO. MH-76: Response to informal
19 Undertaking 1
20
21 MS. HELGA VAN IDERSTINE: The second
22 one will be Mani -- Manitoba Hydro informal Undertaking
23 number 2, and that will be Manitoba Hydro Exhibit
24 number 77. And that was answering Mani -- the
25 question:

1 "Manitoba Hydro to prepare a chart
2 showing new sharing arrangements with
3 respect to the Great Northern
4 Transmission Line, and explain how it
5 works from an accounting
6 perspective."
7
8 --- EXHIBIT NO. MH-77: Response to informal
9 Undertaking 2
10
11 MS. HELGA VAN IDERSTINE: And then we
12 have from Manitoba -- Undertaking number 3, which was
13 Manitoba Hydro was to provide end date of its union
14 agreenen --agreements, and that is Manitoba Hydro
15 Exhibit number 78.
16
17 --- EXHIBIT NO. MH-78: Response to Undertaking 3
18
19 MS. HELGA VAN IDERSTINE: Then we have
20 Manitoba Hydro Undertaking -- sorry, number 1. Sorry,
21 I -- I'll have to correct the transcript. My first
22 comment with respect to the end -- first undertaking, I
23 failed to say it should have been informal Undertaking
24 number 1. I am now up to formal Undertaking number 1,
25 which will be Exhibit number 79. And that one was to:

"Manitoba Hydro to provide further information on the average bills of residential customers outside of Winnipeg."

--- EXHIBIT NO. MH-79: Response to Undertaking 1

MS. HELGA VAN IDERSTINE: Manitoba Hydro Undertaking number 2 will be Manitoba Hydro Exhibit number 80, and that one was to answer:

"Manitoba Hydro to provide the residential average bill for outside of Winnipeg rural compared to other jurisdictions."

--- EXHIBIT NO. MH-80: Response to Undertaking 2

MS. HELGA VAN IDERSTINE: Manitoba Hydro Undertaking number 25 which will be Manitoba -- Exhibit number 81, and that is answering the question:

"Manitoba Hydro to confirm whether there is currently a tool anago -- analogous to an asset health index with regard to ongoing buildings."

1 --- EXHIBIT NO. MH-81: Response to Undertaking 25

2

3 MS. HELGA VAN IDERSTINE: Then we come

4 to, if you're following along, the large fatter number

5 of pages. That will be response to Manitoba Hydro

6 Undertaking number 39. It will be labelled Manitoba

7 Hydro Exhibit number 82, and it is in response to:

8 "Manitoba Hydro to provide the most

9 recent updates to the financial

10 institutions who contribute to the

11 consensus forecasts."

12

13 --- EXHIBIT NO. MH-82: Response to Undertaking 39

14

15 MS. HELGA VAN IDERSTINE: Then we have

16 Manitoba Hydro Undertaking number 49, which will be

17 Manitoba Hydro Exhibit number 83, and the question

18 which is being answered is:

19 "Manitoba Hydro to file a summary

20 chart breaking out the electric

21 investment in DSM measures for each

22 of the measures listed on page 154 of

23 Volume V of the book of documents."

24

25 --- EXHIBIT NO. MH-83: Response to Undertaking 49

1 MS. HELGA VAN IDERSTINE: And that
2 brings me to -- I've got -- it brings me to Exhibit
3 number 85, but was there any -- I seem to be missing a
4 page. Nobody else has an Exhibit 84?
5
6 (BRIEF PAUSE)
7
8 MS. HELGA VAN IDERSTINE: Sorry. And
9 the last page -- page of the fatter bound documents, or
10 the last page of the document, there should be an
11 Exhibit number 84, if you've got it. Manitoba Hydro
12 Undertaking number 57. Do you have it, everybody?
13 THE CHAIRPERSON: Yes.
14 MS. HELGA VAN IDERSTINE: Good, okay.
15 Manitoba Hydro was to provide quarterly updates to the
16 surplus energy program and the factors that caused
17 variances in their rate set and the day-ahead costs.
18 That's been answered, and that will be Manitoba Hydro
19 Exhibit 84.
20
21 --- EXHIBIT NO. MH-84: Response to Undertaking 57
22
23 MS. HELGA VAN IDERSTINE: Is that
24 agreeable?
25 MR. KURT SIMONSEN: Agreeable.

1 MS. HELGA VAN IDERSTINE: Thank you.
2 So then I have one (1) further exhibit that I just want
3 to address specifically. This will be Manitoba Hydro
4 Exhibit 85, and it is in response to the undertaking --
5 taking given by Ms. Bauerlein just before lunch, where
6 she said that she would be able to provide some further
7 information in response to Mr. -- Dr. Grant's question
8 about the chart, and whether or not the chart comparing
9 ASL to ELG was too simplistic.
10 So I think Ms. Hooper is going to speak
11 to this a little bit in a minute, but this is the
12 answer to the undertaking, and it will be Manitoba
13 Hydro Exhibit number 85.
14 MR. KURT SIMONSEN: Thank you. So
15 noted.
16
17 --- EXHIBIT NO. MH-85: Response to Undertaking 75
18
19 MS. HELGA VAN IDERSTINE: All right,
20 Ms. Bauerlein, did you wish to respond further?
21 MS. SANDY BAUERLEIN: Yes. Initially,
22 we were going to respond to Dr. Grant's questions
23 regarding the accumulated depreciation surplus. If my
24 memory serves me correct, he had discussed it being
25 viewed as an overcharge to customers.

1 Depreciation expense is based on -- it's
2 an estimate based on the most -- the information you
3 have at that point in time those assumptions are made.
4 So we don't consider it an error. We consider it an
5 estimate based on the facts that you have, and we
6 calculate our depreciation rates based on those facts.
7 We then do a depreciation study every
8 five (5) years to review and validate those facts and
9 to make changes based on new information. And as such,
10 then we update our rates. So any previous revisions to
11 those rates are then reflected in the current rates,
12 which is why you're seeing, as a result of both our
13 2010 and 2014 depreciation studies, some reductions.
14 So you're -- you're offsetting, then, those -- those
15 charges that you've had previously, because you now
16 have new information in which to set your rates from.
17 And it is -- as Ms. Hooper -- I think
18 it's in slide number 50, accounting standards require
19 you to do that. They require an estimate based on your
20 information, and that you update -- when you update
21 that information, you reflect those changes over the
22 remaining service lives of the assets.
23 MR. LARRY KENNEDY: And perhaps -- and
24 perhaps I can add just maybe a little bit of maybe
25 broader context. The -- the utility industry in --

1 throughout North America, but in particular, my
2 experience in Canada has been that we are seeing the
3 average service life estimates of assets pull out over
4 the last -- oh, I'd say the last decade. And that's --
5 that's caused by a number of factors.
6 Largely, the -- the utilities -- and
7 that -- that specifically includes the electric
8 utilities, have had a need to make their assets last
9 longer, partly because they sometimes have a -- a
10 challenge in attracting the approval for new capital
11 projects, which mean they've got to make due with the
12 old assets somehow, somehow longer. And then they find
13 -- when we find those, that perhaps is resulting in an
14 offsetting increase in operating costs.
15 But more and more specifically, and I
16 think more logically, the -- the use in the way in
17 which assets are maintained is improved. We've got new
18 -- new methods for maintenance. We have new programs
19 for how we look at maintenance. Rather than waiting
20 for something to fail, a lot of utilities are doing
21 preventative maintenance type of activities to drag
22 their lives out longer.
23 So -- so we -- the -- the whole -- the
24 whole era of -- of assets, we do seem to -- to drag out
25 -- to drag out on a longer, and -- and kind of

1 logically, a more and more active basis. Offsetting
2 some of those longer ones, there is some asset groups
3 that are, in fact, going shorter.
4 High technology groups, the Chair and I
5 were chatting about this morning, things like digital
6 control systems are -- are a shorter life influence.
7 We see -- do -- we do see it go both ways. But I think
8 it's important to note that -- that every time we do a
9 study, we -- we see that the companies have gotten
10 better and smarter and use new -- new and innovative
11 methods to -- to extend the life of the assets, because
12 really, that's their ultimate goal.
13 And then I think we also have to
14 remember that it's not only the life estimates that --
15 that can impact on that -- on that surplus, or that
16 deficiency, it can be changes in your net salvage
17 rates, or in fact, in this case, the removal of net
18 salvage. So we -- we see a fairly large surplus.
19 Well, the -- in large part, that can be
20 caused by a change in your salvage policy, as we've
21 seen with this organization, where -- where the
22 decision's been made to remove net salvage from the
23 rates. Well, that's created a -- an accumulated
24 depreciation surplus, in large parts. So -- so there's
25 a number of factors that go on -- but I think the key

1 point is this is a kind of a common trend we see within
2 the industry, and every three (3) to five (5) years, we
3 try to make a new estimate, recognizing the -- the
4 practices and price at that time.
5 DR. HUGH GRANT: I'm just going to sort
6 of interrupt. I didn't want to take up people's time
7 here. My question was really an accounting one. And a
8 few people straightened me out at the break about how
9 an accumulated depreciation surplus gets carried in and
10 --
11 MS. SANDY BAUERLEIN: Okay.
12 DR. HUGH GRANT: So I'll do my homework
13 with Exhibit 85 and read through all these charts, and
14 -- but I didn't want to take up your time with this.
15 MS. SANDY BAUERLEIN: The other
16 question, we weren't sure if we had fully satisfied
17 your answer, Mr. Chairman. It was regards to slide
18 number 18 of the presentation. And we just wanted to
19 emphasize again that the reason you're seeing the two
20 hundred and sixty-seven dollar ($267) charge versus the
21 two hundred dollar ($200) charge under ASL is it's
22 really because that asset, the first asset, had a
23 service life of five (5) years, so it was consumed in
24 that five (5) year period. As such, the -- the
25 depreciation expense reflects that consumption in the

1 asset. So those ratepayers who benefited from that
2 asset are being charged.
3 We actually see that under the average
4 service life approach, you're actually taking some of
5 that benefit of that asset that no longer exists after
6 year 5, and you're having that benefit being paid for
7 by future ratepayers in years 6 through 15.
8 THE CHAIRPERSON: No, I realize the
9 oversimplified example which -- which tends to distort
10 the picture, but, you know, it serves its purpose. But
11 my recollection from the last rate hearing that dealt
12 with depreciation was a very clear example from MIPUG
13 that demonstrated that the -- the investment being
14 projected for Keeyask and Conawapa and so on using ELG
15 generated a higher rate of depreciation than was the
16 case if we had stayed with ASL under GAAP -- or under
17 Canadian GAAP.
18 And so I was trying to -- to -- trying
19 to hear the arguments of Manitoba Hydro that addressed
20 that very issue, because we are heading into a period
21 of extensive investment. And we want to know what the
22 impact will be because we have made the transition to
23 ELG from a financial reporting standpoint.
24 MS. SANDY BAUERLEIN: So I think this
25 might be a -- a good lead into the exhibit that we've

1 put forward. So it's a little bit more of a -- a
2 comprehensive type example that may help demonstrate
3 that point.
4 So with that, I'm going to let Ms.
5 Hooper walk through...
6
7 (BRIEF PAUSE)
8
9 MS. MICHELLE HOOPER: Okay, Exhibit 85
10 is an excerpt from Manitoba Hydro's rebuttal evidence
11 from the last GRA. So it sets forth an example that
12 shows what the impact of the different depreciation
13 alternatives would be if you assumed a constant level
14 of investment in an asset pool.
15 So, excuse me, it uses the same premise
16 of half of your asset pool having a five (5) year life,
17 and half having a fifteen (15) year life, as is used in
18 Mr. Kennedy's example. But as each asset is replaced -
19 - is retired, it is immediately replaced with an
20 identical asset.
21 So we did not include the effects of
22 escalation here and increasing in costs over time.
23 Those costs, you would still have a similar kind of a
24 pattern of depreciation expense, except that all of
25 your expenses would slant upwards instead of being

1 flat, as is shown here.

2 If you look at page 20 of 62, which is

3 the second page of the exhibit, there's a chart that

4 compares the depreciation expense pattern for a

5 constant level of an inve -- a pool with a constant

6 level of investment under three (3) different

7 scenarios.

8 So the first scenario, the first set of

9 data, is green bars, is ELG using group depreciation

10 and immediate recognitions of gain and losses -- sorry,

11 immediate recognition of gains and losses, which is

12 what Manitoba Hydro is proposing to move to. And you

13 can see that there is a flat pattern of depreciation

14 expense throughout -- throughout the example, which is

15 -- ties very nicely with the level of -- of the flat

16 level of investment that is present in the same period

17 of time.

18 The second pur -- set of data, the --

19 the purple bars, is average service life methodology

20 with group depreciation and deferral of gains and

21 losses, which is comparable to what Manitoba Hydro has

22 been using under Canadian GAAP.

23 In that case, you have a lower

24 depreciation expense initially, but it grows through

25 the period of time of the example, so you end up with a

1 wavy pattern of depreciation expense rather than a flat
2 pattern. Irre -- even though the level of investment
3 is the same, the depreciation expense is variable.
4 Your third scenario with the blue bars
5 is a average service life with segregation of assets
6 with different life. So this would be, if you did a
7 more componentized version of ASL, as -- similar to
8 what we described as one (1) of the options, you end up
9 back at the same place with a flat depreciation expense
10 pattern.
11 Okay, the calculations supporting all of
12 these examples are in Attachment B to this, which is
13 here. The -- the third page of your handout actually
14 has Attachment A. That's not relati -- relevant to
15 that chart, it's an example for a declining asset pool.
16 If you flip forward to page 51, there's
17 Attachment B, sets forth the assumptions that we've
18 used on page 51 of 62 explaining the assumptions are
19 five (5) units of a hundred dollars with a five (5)
20 year life and five (5) units of a hundred dollars with
21 a fifteen (15) year life. So that at any point in time
22 you have an equal level of investment of a thousand
23 dollars, 50 percent of your asset base has a five (5)
24 year life, 50 percent a fifteen (15) year life, and the
25 weighted average is ten (10) -- ten (10) years

1 throughout.

2 Page 52 has a continui -- a cost

3 continuity. I'm not going to walk you through this,

4 but if you look at the far right column of that chart

5 on the top of page 52 you can see the costs at the end

6 of each year is a thousand dollars all the way down.

7 Okay. The graph at the bottom of page 52 shows that

8 ELG depreciation expense pattern. The top of page 53

9 shows the -- a depreciation continuity schedule and how

10 the calculations work.

11 All the supporting calculations for --

12 for these graphs and charts are in this document. I'm

13 not going to walk them through you unless you have

14 specific questions. They're there for you to -- to

15 look at and we'd be happy to answer questions at a

16 later time once you've had a chance to review them.

17 Okay. Page 54 shows the depreciation expense flow

18 under the average service life methodology. And page

19 55 has the supporting calculations showing that wavy

20 depreciation expense pattern under ASL.

21 Page 58 is the supporting -- and

22 following pages are the supporting calculations for the

23 ASL with segregation. This is comparable to what a lot

24 of our competitor utilities are using with their ASL

25 and more componentized depreciation components.

1 And I just wanted to also bring your
2 attention to a fourth scenario that's in this handout
3 on page 61. There's a chart with red bars at the top.
4 This is the depreciation expense -- or the expense
5 pattern that you would see in a situation where you use
6 ASL and immediate recognition of gains and losses as is
7 required under IFRS. And you end up with a very
8 erratic expense pattern that would not be suitable for
9 use in rate setting in our opinion. Okay.
10 DR. HUGH GRANT: Could you just -- what
11 is a true-up rate?
12 MS. MICHELLE HOOPER: The true-up rate
13 is the -- is -- it's a jargon I guess, depreciation
14 jargon. That accumulated depreciation variance that --
15 that exists at the -- at a depreciation study is
16 brought back into rates as an increase or a decrease to
17 the depreciation rate in order to recover that variance
18 over the remaining life. So that true-up rate is the
19 difference -- the change that you need to make to
20 depreciation expense in order to recover the
21 accumulated depreciation variance. Okay.
22 MR. DARREN RAINKIE: Mr. -- Mr.
23 Chairman, I -- I wanted to take a second to address
24 your last question because I think we left some
25 unfinished business there. And sorry to keep switching

1 documents, but if we can move back, Diana, to our
2 presentation page 77 for a second. I'd just like to be
3 sure that the record is clear.
4 So if we -- if we look at this -- this
5 table of depreciation changes in the next ten (10)
6 years and if we go to the 2021 column for instance when
7 Keeyask and Bipole are all fully in-service, let's just
8 use it as an example. So we move down to the two (2)
9 last rows and we see that the change in the methodology
10 to ELG was going to start off at a $36 million increase
11 in depreciation in 2016. And that number is going to
12 grow to $63 million by 2021 and our asset base is
13 roughly doubling over that time frame. So that -- the
14 doubling of that impact doesn't necessarily surprise
15 me.
16 But if you go one (1) row up we see the
17 elimination of the provision for asset removal or
18 negative salvage value, what you and I were just
19 chatting about before lunch. And you see by that time
20 the provision -- the elimination of that provision has
21 grown -- has doubl -- almost doubled as well and such
22 that depreciation has reduced by $107 million.
23 So at that point in time the cumulative
24 effect, if you like, on that particular year is not the
25 cumulative effect. It's the effect in that one (1)

1 year of these two (2) policy decisions that we've made
2 is a reduction in depreciation expense of $45 million
3 on a net basis.
4 And then if you go out to the end of
5 2024, you see the difference is a $69 million increase
6 because of ELG, but a $119 million decrease because of
7 net salvage. So by the end of the decade, depreciation
8 of these two (2) policy choices is down $50 million, a
9 reduction of $50 million.
10 So I think you can see why our audit
11 committee was saying to me when I brought these changes
12 to them, Why are -- you know, in an era where we need
13 to invest even more on behalf of Manitobans, why are we
14 reducing depreciation expense so much? This was --
15 this was their concern.
16 But certainly, that's the way we're
17 looking at it. We -- we recognize that ELG has that
18 impact, but it's an appropriate thing for rate setting
19 because, I mean, on the -- on the Keeyask project,
20 there will be buildings in the Keeyask project that
21 aren't a hundred (100) year assets.
22 There will be buildings that are ten
23 (10) or fifteen (15) year assets. They're getting
24 lumped in with the hundred (100) year assets under ESL
25 right now. So it's appropriate that those -- those

1 buildings that will only last ten (10) or fifteen (15)
2 years are depreciated over that time frame, and the
3 customers that enjoy that particular building pay for
4 that over that time frame.
5 So it's the same phenomena whether it's
6 a generating station, you know, a Bipole project.
7 There are shorter-lived assets in those projects and
8 longer ones. ELG is more precise in terms of breaking
9 those out and ensuring that the right generation of
10 customers pay for them under the inter-generational
11 equity principle.
12 So, yes, there is that up-tick in ELG
13 when our plant doubles, but our policy decision to
14 remove negative salvage value has more than taken care
15 of that by the tune of $50 million at the end of the
16 decade. So I -- I can't accept the front loading and
17 the fact that Manitoba Hydro has not been responsible
18 in -- you know, in try -- in terms of trying to manage
19 the impact to customers because we have.
20 THE CHAIRPERSON: Thank you. I'll turn
21 it over to you, Mr. Hombach. Thank you.
22 MR. SVEN HOMBACH: Thank you, Mr.
23 Chairman. Now, before I start, I understand that Me.
24 Hacault may have an administrative matter to speak to.
25 MR. ANTOINE HACAULT: Yes. Thank you

1 very much. It's more a question than an administrative
2 matter. As I understand it, we'll be expected to make
3 our final submissions on Wednesday. And there are, to
4 my count, a number of undertakings which have yet to be
5 addressed by Manitoba Hydro, including some that
6 they've taken today.
7 While I can work on the weekend, if I
8 don't receive that information relatively soon, I don't
9 know how I can even provide MIPUG's perspective on the
10 entire information in the case unless there's some kind
11 of time frame where I'm allowed to have that
12 information quick enough to incorporate it into my
13 comments.
14 And I understand the Board's not
15 available the week after, and we have really quick time
16 limits. But it's -- it's more the question of how is
17 this poor lawyer going to meet the challenge of trying
18 to provide useful comments on information that's being
19 provided in this hearing.
20 So I just raise this now, and we would
21 really appreciate -- and I know Hydro Manitoba (sic)
22 try -- Hydro tries hard to get its undertakings to us
23 quickly. But if we could get as many of them before
24 the weekend, that would be of assistance, and the
25 sooner, the better, generally.

1 So thank you for listening to my
2 comments and allowing me the chance to raise that
3 concern.
4 THE CHAIRPERSON: Would you like to
5 address that, Ms. Van Iderstine?
6 MS. HELGA VAN IDERSTINE: I think all I
7 can say is I know they're working on it. They're doing
8 their best to get them to you in a timely way.
9 And some of the people who are needing
10 to provide the information are in fact giving evidence
11 at the moment, so it makes it very difficult for them.
12 But we'll -- they're -- I know they're trying. That's
13 the best I can say at the moment.
14 THE CHAIRPERSON: Mr. Hombach, please.
15 MR. SVEN HOMBACH: Thank you, Mr.
16 Chairman. Good afternoon, members of the Manitoba
17 Hydro panel. Before I begin my examination, I'd like
18 to introduce two (2) exhibits on the record.
19 The first is Volume VI of Board
20 counsel's book of documents, which should be given
21 Exhibit Number 20-6.
22
23 --- EXHIBIT NO. PUB-20-6: Volume VI of Board
24 counsel's book of documents
25

1 MR. SVEN HOMBACH: The second is an
2 excerpt from NARUC's depreciation manual entitled
3 Public Utility Depreciation Practices. It has been
4 circulated and should be made PUB Exhibit 22.
5
6 --- EXHIBIT NO. PUB-22: NARUC'S depreciation manual
7 entitled Public Utility
8 Depreciation Practices
9
10 MR. KURT SIMONSEN: Noted. Thank you.
11
12 CROSS-EXAMINATION BY MR. SVEN HOMBACH:
13 MR. SVEN HOMBACH: If I could ask Diana
14 to turn to Volume III of Board counsel's book of
15 documents, page 38.
16
17 (BRIEF PAUSE)
18
19 This is a chart that among other things shows the
20 progression of Manitoba Hydro's annual revenue
21 requirement related to depreciation and amortization
22 from 2015 to 2034?
23 MR. DARREN RAINKIE: Yes, it is, sir.
24 MR. SVEN HOMBACH: And, Mr. Rainkie,
25 perhaps I'll address the question to you. What we see

here is a doubling of the annual depreciation expense between the test year and the year 2034?

MR. DARREN RAINKIE: Yes, sir. That -- that would be -- this is the change in depreciation expense net of any accounting changes. The increase would be even higher if we were making the accounting changes we were just talking about.

MR. SVEN HOMBACH: So this particular chart that we're looking at, Mr. Rainkie, does this assume a switch to IFRS and equal life group as of the 2015/'16 test year?

MR. DARREN RAINKIE: Yes. This assumes that $50 million reduction that I was just chatting with -- with the chairman a couple minutes ago.

MR. SVEN HOMBACH: And is the doubling primarily attributable to Bipole III and Keeyask coming into service?

MR. DARREN RAINKIE: Well, this is the twenty (20) year perspective. What I was just chatting about is the 2024 perspective. So it would include -- of course a large chunk of this is in the first number of years going out to 2021-ish is Keeyask and Bipole, but this also reflects sustaining capital expenditures and other expenditures on major new gen and transmission throughout that whole twenty (20) year

period, sir.

MR. SVEN HOMBACH: But this chart has been updated to exclude Conawapa?

MR. DARREN RAINKIE: Yes, it is but there are still six (6) or $700 million of sustaining capital expenditures each and every year after to -- to -- well, each and every year in the twenty (20) year forecast, sir. So it -- it's not like the investment in Keeyask and -- and Bipole are our last investments, but this does exclude -- exclude Conawapa, sir.

MR. SVEN HOMBACH: Thank you. If we could turn to page 5 of Board counsel's book of documents, Volume VI?

(BRIEF PAUSE)

MR. SVEN HOMBACH: We're looking at a continuity chart for depreciation expense, and if we go to the bottom of the document, Mr. Rainkie, it appears that those expenditures are expected to grow at the rate of approximately 5 percent annually?

MR. DARREN RAINKIE: Sir, I think you have to -- we have to be careful about how this table is constructed. The line that says, "Total D&A," depreciation and amortization, "Expense excluding" --

1 sorry, "Including accounting changes," is what we
2 actually expect to book in our financial statements.
3 And then the line that says, "Total D&A expense
4 excluding accounting changes," is the higher
5 depreciation we would have booked if we had not made
6 the accounting -- the accounting changes that we were
7 just talking about.
8 So if you go down to the two (2) last
9 rows on this -- this sheet, where the year over year
10 percentage change including accounting change is that's
11 what we expect to actually book. So you see that
12 there's a decrease of 1.5 percent in the first year, a
13 decrease of .9 percent in the second year, and then an
14 increase of 5.4 percent. So that's what we actually
15 expect to -- to have, is -- is two (2) decreases and an
16 increase.
17 If you were -- if we weren't making
18 these accounting changes that we just talked about, you
19 would see increases of four and a half (4 1/2), five
20 point six (5.6), and five point seven (5.7) across the
21 board.
22 MR. SVEN HOMBACH: If we could go to
23 the top of that page, please? It appears that the
24 lion's share of the depreciation expense relates to
25 generating assets?

1 MR. DARREN RAINKIE: Yes. It's -- they
2 are obviously some of the largest assets we have in our
3 varied fleet of assets.
4 MR. SVEN HOMBACH: Right. And you gave
5 an example earlier, Mr. Rainkie, about some of the
6 buildings at -- at Keeyask, for example, being lumped
7 in with the generating assets.
8 If I were to look at one of the asset
9 groups here, like hydraulic generating stations, does
10 that include all the components within those stations
11 including the dams, the turbines, the buildings, et
12 cetera?
13 MS. MICHELLE HOOPER: Yes, Mr. Hombach.
14 Yes, it does include all of the assets associated with
15 generating stations.
16
17 (BRIEF PAUSE)
18
19 MR. SVEN HOMBACH: And, Mr. Rainkie,
20 you mentioned earlier that the expected life of large
21 assets like the dams would be one hundred (100) to a
22 hundred and twenty-five (125) years, that's correct?
23 MS. MICHELLE HOOPER: Yes, we use a
24 life expectancy of a hundred and twenty-five years
25 (125) years for dams, dikes, and weirs.

1 MR. SVEN HOMBACH: And to the extent
2 that Manitoba Hydro is off in any of those life
3 expectancies, does that get taken into account each
4 time there's a new depreciation study prepared?
5 MS. MICHELLE HOOPER: Yes, if there's a
6 change in estimate there would be a depreciation
7 variance that would be calculated that would be then
8 amortized over the remaining life of the assets in
9 question.
10 MR. SVEN HOMBACH: How frequently does
11 Manitoba Hydro currently prepare depreciation studies?
12 MS. MICHELLE HOOPER: Approximately
13 every five (5) years.
14 MR. SVEN HOMBACH: Fine. If we could
15 go back then, please, to Manitoba Hydro Exhibit 85, the
16 chart on page 61 of 62. And, Ms. Hooper, I'm not sure
17 if you're the right person to -- to speak to this
18 chart, or perhaps I should address it to Ms. Bauerlein.
19 Page 61.
20 MS. MICHELLE HOOPER: Yes, I have it.
21 MR. SVEN HOMBACH: The -- the example
22 that Manitoba Hydro just walked the -- the Board
23 through does not take into account that there's a
24 number of depreciation studies in the interim before
25 losses or gains ultimately incurred -- accrued, does

1 it?

2 MS. MICHELLE HOOPER: The example on

3 page 61 is what would happen if you are required to

4 recognize gains and losses into income immediately and

5 not defer and amortize them.

6 MR. SVEN HOMBACH: Right.

7 MS. MICHELLE HOOPER: This is not the

8 current practice of Manitoba Hydro.

9 MR. SVEN HOMBACH: But to the extent

10 that gains or losses accrue because the actual

11 depreciation does not match the true asset life that

12 gets adjusted every five (5) years, does it not?

13 MS. MICHELLE HOOPER: Sorry, yes, it

14 does get incorporated. And I'm just locating the page

15 that shows that.

16 MR. SVEN HOMBACH: Certainly.

17 MS. MICHELLE HOOPER: If you flip to

18 page 54 of 62 it shows the impacts of depreciation

19 adjustments, true up adjustments at five (5) year

20 intervals over the -- the life of the asset pool.

21 MR. SVEN HOMBACH: And if we look at

22 that chart we see that that significantly removed some

23 of the peaks and valleys that you see once assets are

24 retired?

25 MS. MICHELLE HOOPER: Yes, it does, but

it still provides a wavy pattern of depreciation expense that is not reflective of the assets in service in each year.

MR. SVEN HOMBACH: Just to be clear, the -- the examples in Exhibit 85, those are for illustration purposes only, right? This does not reflect Manitoba Hydro's actual current asset base?

MS. MICHELLE HOOPER: No, this is a simp -- this is a simplified example.

MR. SVEN HOMBACH: And the Chair had asked Manitoba Hydro to comment on the -- the allegations of front-loading, or whatever the term that you choose might be. And I suffer from the fatal flaw that I'm not an accountant either, so I prefer the simple examples for illustrative purposes.

And if I could turn you to PUB Exhibit 22, page 14.

(BRIEF PAUSE)

MR. SVEN HOMBACH: We see a chart from the NARUC manual that does a very simplified comparison between equal life group on the left and the average service life methodology on the right.

Mr. Kennedy, vintage group, or VG,

1 that's the same as average service life?
2 MR. LARRY KENNEDY: Yes, I can do all
3 kinds of statistical work, but I have a hard time
4 turning my microphone on. Yes, it would be, sir.
5 MR. SVEN HOMBACH: Thank you, sir. So
6 what we see on the left is that -- well, you have an
7 asset in which there are three (3) -- well, you have a
8 group where there are three (3) assets and asset one
9 (1) has a life of one (1) year, asset B of two (2)
10 years, and asset C three (3) years. You have an
11 average service life in the group of two (2) years?
12 MR. LARRY KENNEDY: That's correct.
13 MR. SVEN HOMBACH: So if we look at the
14 current average service life methodology on the right,
15 we see that that leads to a 50 percent depreciation
16 rate for each of the assets?
17 MR. LARRY KENNEDY: That is correct.
18 MR. SVEN HOMBACH: Whereas, if we look
19 to the left, the equal life group, we see the first
20 item being fully depreciated in year 1?
21 MR. LARRY KENNEDY: Consistent with its
22 one (1) year of service life.
23 MR. SVEN HOMBACH: Ms. Hooper, what is
24 Manitoba Hydro's current asset base? The number in my
25 head is approximately 14 billion.

1 Am I in the ballpark?
2 MS. MICHELLE HOOPER: Yes, subject to
3 check.
4 MR. SVEN HOMBACH: And those assets
5 have been accumulated over approximately a hundred year
6 time frame?
7 MS. MICHELLE HOOPER: Yes, that is
8 correct.
9 MR. SVEN HOMBACH: So for this hundred
10 year time frame the utility has essentially used
11 average service life or has it used a different
12 methodology at some point in the past?
13 MS. MICHELLE HOOPER: My understanding
14 is that since about 1988, it has used average service
15 life methodology. Prior to that it appears from the
16 records that it was some other straight line
17 depreciation method, but we're not certain exactly what
18 method was used.
19 MR. SVEN HOMBACH: Has Manitoba Hydro
20 considered the generational equity of switching the
21 methodology to equal life group so late in the game if
22 -- if for an extended period of time the methodology
23 has not been used and the higher front-loaded charges
24 haven't been recovered? Mr. Rainkie?
25 MR. DARREN RAINKIE: Sir, we're going

1 to get right back into that discussion I just had.
2 Yes, we have through the removal of negative salvage
3 value which reduces depreciation expense by $50
4 million. The net of those two (2) in the year 2024.
5 MR. SVEN HOMBACH: Right.
6 MR. DARREN RAINKIE: Unless I'm
7 misunderstanding your question.
8 MR. SVEN HOMBACH: You're not
9 misunderstanding the question and I'm actually
10 heartened by the fact that there are three (3)
11 accountants on the panel because I -- I'd like to get
12 clarity on one (1) issue.
13 Does IFRS allow net salvage or does IFRS
14 mandate that net salvage be removed?
15 MR. DARREN RAINKIE: IFRS doesn't allow
16 net salvage, but we're talking about rate setting here,
17 sir. So we have to -- when we have these discussions
18 we have to be very careful. Are we talking about
19 financial reporting or are we talking about rate
20 setting?
21 MR. SVEN HOMBACH: Right. And --
22 MR. DARREN RAINKIE: We're thinking in
23 this forum we're talking about rate setting so...
24 MR. SVEN HOMBACH: And, Mr. Rainkie,
25 what that means is that the policy decision that

1 Manitoba Hydro has made that you spoke about is not to
2 apply for a separate rate-regulated deferral account to
3 deal with net salvage?
4 MR. DARREN RAINKIE: Well, that would
5 be the accounting manifestation of it I suppose. I
6 think really on a policy level what we've indicated is
7 we understand that the move to ELG will cause an
8 increase in depreciation. So in balancing out that
9 factor with removing negative salvage we believe that
10 it's on -- it's on balance in favour of the customer so
11 it's a reasonable saw-off if you like. This isn't --
12 this is a policy decision. It isn't a technical, you
13 know, calculation to the third decimal point, sir.
14 MR. SVEN HOMBACH: Right. But as far
15 as the Board is concerned if Manitoba Hydro wanted to
16 retain that salvage the only way to do so would --
17 would be to set up a rate-regulated deferral account?
18 MR. DARREN RAINKIE: Yes, as would be
19 the case if we wanted to maintain AS -- CGAAP ASL, we
20 would have to set up a -- that would -- sorry. If we
21 wanted to maintain negative salvage value we would set
22 up a regulated liability. If we wanted to maintain
23 average service life under Canadian GAAP we would set
24 up a regulated asset. We don't see the need to do that
25 in that the two (2) are going to offset each other and

1 get back to the same thing. So why would we go through
2 the cost and expense of having two (2) sets of sub-
3 ledgers for a company who have, as you noted, $14
4 billion of assets that's going to double in the next
5 ten (10) years?
6 MR. SVEN HOMBACH: And, Mr. Rainkie,
7 Ms. Bauerlein earlier walked through an example and
8 indicated that if there is a rate-regulated account the
9 difference between IFRS and the rate-regulated account
10 would have to be amortized over a period of time.
11 Did I understand that correctly?
12 MR. DARREN RAINKIE: That's correct
13 because you cannot have an asset on your books or a
14 liability on your books for that matter that just sits
15 there forever. There has to be some amortization
16 period.
17 MR. SVEN HOMBACH: So please explain to
18 the non-accountants in the room, myself included,
19 whether that would also apply to net salvage if
20 Manitoba Hydro chose to retain it.
21 MR. DARREN RAINKIE: Yes, I -- I -- as
22 I just said I think whether you have a regulated asset
23 or a regulated liability, regardless of which side of
24 the ledger it sits on, you would have to find some type
25 of an amortization period to recover or refund that as

1 the case may be. Otherwise, I mean, any cost that the
2 Company has eventually becomes an expense. You can't
3 keep assets or liabilities on your books forever, sir.
4 MR. SVEN HOMBACH: Mr. Kennedy --
5 THE CHAIRPERSON: Could you clarify for
6 me, please. I -- I'm a bit confused now. For
7 financial reporting purposes, you will be providing an
8 exception because you're not using net sal -- net
9 salvage value?
10 MS. SANDY BAUERLEIN: I believe, if I'm
11 understanding your question correctly, IFRS does not
12 permit net salvage. So for financial reporting
13 purposes, our decision, our policy decision, complies
14 with that.
15 So we do not need to set up a -- a
16 regulatory liability account because we are complying
17 with financial reporting requirements.
18
19 CONTINUED BY MR. SVEN HOMBACH:
20 MR. SVEN HOMBACH: Once net salvage is
21 removed, it's going to form part of the book of the
22 accumulated surplus, and it's going to be recovered
23 over the remaining service life of the assets, correct?
24 MS. MICHELLE HOOPER: Yes, that is
25 correct.

1 MR. SVEN HOMBACH: And, Ms. Bauerlein,
2 the example you gave earlier between ELG and ASL made
3 the assumption that the difference between those two
4 (2) would be recovered over a ten (10) year period.
5 Can you explain why Manitoba Hydro made
6 the choice to provide an example over a ten (10) year
7 period as opposed to the remaining service life of the
8 assets in that case?
9 MS. SANDY BAUERLEIN: It was an
10 illustrative example. And we chose the ten (10) years
11 because it was representative of most of our regulatory
12 deferral accounts.
13 MR. SVEN HOMBACH: Like DSM, for
14 example?
15 MS. SANDY BAUERLEIN: Correct.
16 MR. SVEN HOMBACH: So if this Board
17 were to not approve equal life group and were to set up
18 a -- an ESL-based methodology, there would be an option
19 to recover the difference over a longer or shorter time
20 frame?
21 MS. SANDY BAUERLEIN: That is correct.
22 MR. SVEN HOMBACH: Mr. Kennedy, the
23 next question goes to you. Under either of the two (2)
24 methodologies, over the total life of an asset, the
25 amount recovered is the same, is it not?

1 MR. LARRY KENNEDY: Under both -- both
2 methodologies would be consistent with the example you
3 put before me from the -- the NARUC manual. In my
4 simplest example, yes. Both would be fully recovered
5 assuming that the losses -- oh, I'm just going to stop.
6 The -- the -- both methods or both
7 procedures will fully recover the -- the original cost
8 of the asset.
9 MR. SVEN HOMBACH: So the question is
10 really: At what point in time do you recover the
11 money? Do you recover it early or do you recover it
12 late?
13 MR. LARRY KENNEDY: I think the
14 question's more appropriately: How do you best align
15 the consumption of the service value of the assets to
16 the depreciation expense?
17 MR. SVEN HOMBACH: Right. Staying with
18 the example in front of us from the NARUC manual, Table
19 12.8 on page 14 of the PDF, we see that if the asset
20 base stays the same, there's ultimately a crossover
21 point where the total depreciation expense under ELG is
22 less than it would be under average service life?
23 MR. LARRY KENNEDY: Correct.
24 MR. SVEN HOMBACH: If we could turn to
25 page 52 of Volume VI of Board counsel's book of

1 documents, please.

2

3 (BRIEF PAUSE)

4

5 MR. SVEN HOMBACH: This is a response

6 to PUB/MH Information Request I-37(b) in which Manitoba

7 Hydro was asked to provide a schedule until 2033/'34

8 that shows the impact of the differences.

9 You see that, Mr. Kennedy?

10 MR. LARRY KENNEDY: I do.

11 MR. SVEN HOMBACH: Did you have any

12 input in this chart, or is this something you leave to

13 the accountants?

14

15 (BRIEF PAUSE)

16

17 MR. LARRY KENNEDY: Yeah, this was

18 predominantly prepared by Manitoba Hydro, sir. And I -

19 - I say "predominantly" only because I likely reviewed

20 it for it to have been submitted, but the document

21 itself was prepared by Manitoba Hydro.

22 MR. SVEN HOMBACH: Right. And we see

23 in the second white line from the bottom the emil --

24 elimination of provision for asset removal that Mr.

25 Rainkie alluded to already. And below that we see the

1 impact of the change in methodology from average
2 service life to equal life group.
3 Mr. Rainkie, is it fair to say that, in
4 terms of the methodological change, there's not going
5 to be a crossover over the next twenty (20) years?
6
7 (BRIEF PAUSE)
8
9 MR. DARREN RAINKIE: If you isolate
10 that one (1) variable, I would suggest to you there's a
11 crossover in 2015/'16 of $24 million reduction when you
12 look at the removal of negative salvage values. So I
13 guess it's a matter of perspective, sir. I -- I think
14 Manitoba Hydro is trying to manage the overall revenue
15 requirement for customers.
16 We can pick apart every little tiny
17 tidbit of every line item in our financial statements
18 if you want, but in the end, what's -- what we are left
19 with is the total revenue requirement, and trying to
20 match revenues over time with that total revenue
21 requirement. If we don't, we'll have losses. We'll
22 borrow more money, and we'll have to raise rates even
23 further.
24 So, you know, that's -- that's what we
25 have to talk about. Are we here -- are we diving for

1 dollars, or are we talking policy in terms of overall,
2 you know, rate impacts to customers and what the future
3 holds?
4 MR. SVEN HOMBACH: I appreciate your
5 position, Mr. Rainkie.
6 Depreciation itself is a non-cash
7 expense to Manitoba Hydro at the time it is incurred,
8 correct?
9 MR. DARREN RAINKIE: That's correct.
10 But I don't think the positions of Intervenors stop
11 there. I think the posit -- the positions of
12 Intervenors are, Well, let's change the accounting
13 policies and let's reduce the rate increase as a
14 result. So that becomes a cash expense -- or sorry,
15 that becomes a loss of revenue, which very quickly will
16 go to our bottom line, so we have to understand that.
17 If -- if all we're talking about is
18 playing around with how our books are -- are kept, two
19 (2) different methodologies, there's no change in the
20 rate increase, then that's one (1) thing, but if you're
21 using -- if you're going to say, Well let's do
22 something different than what the Company is proposing
23 in order to justify a lower rate increase, then that is
24 cash, and cash in 2015/'16, not cash in -- start --
25 starting in 2015/'16, not cash in 2033/'34.

1 MR. SVEN HOMBACH: So is what you're
2 suggesting, if I'm hearing you correctly, Mr. Rainkie,
3 that a -- a switch to equal life group, or the outcome
4 of a switch to equal life group would be to generate a
5 -- a revenue requirement to support a cashflow need?
6 MR. DARREN RAINKIE: No. What I'm
7 suggesting to you is that there's a $24 million
8 reduction in our depreciation expense between the
9 removal of negative salvage value and the switch to
10 ELG, so in fact, what Manitoba Hydro is really doing is
11 understating its revenue requirements. But we
12 recognize that was a fair thing to do for customers.
13 MR. SVEN HOMBACH: Purely with respect
14 to the change in depreciation methodology, Mr. Rainkie,
15 Manitoba Hydro was asked when and whether there would
16 be a crossover point. And an answer was provided in
17 response to PUB/MH Information Request II-27, which
18 isn't in the book, and the Utility could not provide an
19 answer as to when there would be a crossover point.
20 Is that your understanding, as well?
21 MR. DARREN RAINKIE: Yes. For that
22 select item, that's -- that's what the -- I think this
23 chart is telling us --
24 MR. SVEN HOMBACH: Right. What we see
25 in the chart is that both the added revenue requirement

from ELG and the reduction as a result of the elimination of net salvage keep growing at least for twenty (20) years.

Do you know, or does Manitoba Hydro know, whether there is a point in time when the reduction in revenue requirement for the elimination of net salvage will decrease?

MR. DARREN RAINKIE: Well, given that net salvage is a percentage add-on to various customer classes, if you assume over time that our balance sheet will grow as Manitoba grows, I don't think there'll ever be a reversal of this. As we look at 2033/'34, the differential is up to 60 -- $62 million, so I don't think that's -- that's going to turn around, if I understand your question correctly.

MR. SVEN HOMBACH: You wouldn't be applying that salvage to new assets, like Bipole III or Keeyask, though, from this point forward, would you?

MR. DARREN RAINKIE: Well, sorry, sir, that's our recommendation, is to move to ELG and to eliminate net -- eliminate net salvage, and if you accept the net impact of that -- and so if the Board accepts that, we won't apply any more net salvage into our depreciation expense. But it depends if you're making a comparison between two (2) things or -- or

1 not. You know, I -- I'm not sure I'm being clear, sir.
2 MR. SVEN HOMBACH: And -- and maybe I'm
3 not clear either. My question was, We -- we don't know
4 whether there's a crossover point with respect to ELG,
5 but -- MS. SANDY BAUERLEIN: I think I would
6 just like to add to that, the -- this assumes our
7 current depreciation rates. We don't necessarily know
8 -- because again, we do a depreciation study every five
9 (5) years, what those depreciation rates will be, what
10 additions, retirements may be happening twenty (20),
11 thirty (30) years out. So it's very difficult for us
12 to predict what -- when that exact crossover period
13 will -- will occur.
14 I also wanted to make it clear that it's
15 not really the change to go to ELG, it's the change to
16 be IFRS compliant. That is what that bottom row is
17 representing. So as long as we take the position that
18 we want to maintain for financial reporting the same
19 for rate setting, then there will be an increase in
20 depreciation expense regardless, because again, back to
21 the requirement that IFRS requires a greater degree of
22 precision.
23 So it's that degree of precision where
24 you're depreciating your asset over its consumption
25 period that is driving that, given that it's

1 asymmetrical, your -- your shorter lived assets are
2 causing this increase in depreciation. But if you have
3 a longer-lived asset, so if we build Keeyask and you've
4 got the -- the spillway or the -- the powerhouse
5 structure, those are long-lived assets, so they are
6 still amo -- depreciated over their amortization
7 period.
8 So each -- ELG reflects the -- the
9 consumption of that particular component or asset
10 group.
11 MR. SVEN HOMBACH: Ms. Bauerlein, in
12 response to a MIPUG Information Request that's
13 reproduced at page 69 of Board counsel's book of
14 documents, Manitoba Hydro provided a historical example
15 based on a starting point of the year 1923.
16 Are -- are you familiar with this one?
17 Were you involved in preparing this?
18 MR. LARRY KENNEDY: Mr. Hombach, at --
19 on this one (1) you can -- you can probably point to
20 one --
21 MR. SVEN HOMBACH: Refer to you?
22 MR. LARRY KENNEDY: Yes.
23 MR. SVEN HOMBACH: And -- and, Mr.
24 Kennedy, am I reading this chart correctly to mean that
25 the crossover point, in this case, between average

1 service life and ELG, would have happened in 1998? We
2 go to the bottom of page 70.
3 MR. LARRY KENNEDY: That -- that's
4 correct, sir. That's -- for this account it's, I
5 think, an average service life of approximately a
6 hundred and twenty-five (125) years. And given the
7 curve shape that -- that's included here, that
8 crossover point under that set of circumstances occurs
9 in 1998.
10 MR. SVEN HOMBACH: And that's about a
11 seventy-five (75) year time frame?
12 MR. LARRY KENNEDY: In this particular
13 circumstance, sir, yes.
14 MR. SVEN HOMBACH: Mr. Rainkie, a -- a
15 question was put to Manitoba Hydro in Information
16 Requests as to what rate increase the Utility would
17 seek if it had to stay with average service life. And
18 Manitoba Hydro's response was that it would continue to
19 seek 3.95 percent, correct?
20 MR. DARREN RAINKIE: That's correct.
21 Jimmying around with accounting policies will not
22 change the rate requests of Manitoba Hydro.
23 MR. SVEN HOMBACH: And the cashflow
24 requirement?
25 MR. DARREN RAINKIE: Well, that's

1 right, sir, like as -- as we talked about earlier, if
2 you assume the same -- same rate increases, it won't
3 change the cashflow, but if you reduce the rate
4 increases because of fooling around with accounting
5 policies, it will reduce the cashflow, so.
6 MR. SVEN HOMBACH: Right. If Manitoba
7 Hydro switches to equal life group at this point in
8 time, the added revenue from that -- or the added
9 revenue requirement from that switch would still be
10 applicable after the new major assets come into
11 service, would it not?
12 MR. DARREN RAINKIE: Sir -- sorry, sir,
13 I -- I guess we're on a different plane. You're being
14 selective, and you're asking me questions about one (1)
15 particular item. I'm -- I -- we manage and look at it
16 from an overall basis. And as I'd indicated several
17 times, there's a net decrease -- there's a huge
18 decrease in depreciation.
19 If you look at the net effect of the
20 last depreciation study, this depreciation study, and
21 these changes in accounting policies, there's a huge
22 decrease in depreciation. That's why our audit
23 community is concerned about this, that in a time when
24 Manitoba Hydro has to increase its investment and
25 assets, it's making it look on the street like its

1 depreciation is reducing and that things are -- are
2 getting better when they're -- when they're not.
3 So, you know, that's why we have to look
4 at it from an overall perspective and not be selective
5 on one (1) component.
6 MR. SVEN HOMBACH: I fully understand
7 and appreciate that position, Mr. Rainkie, but my
8 question still stands. The impact of that switch would
9 not disappear once the new assets come into service.
10 It would continue? MR. DARREN RAINKIE:
11 Well, of course, sir. We're not planning on moving to
12 ELG and then moving away. We're -- we're planning to
13 use this methodology on a go-forward basis.
14 MR. SVEN HOMBACH: Right. And I
15 understand Manitoba Hydro to indicate that for the
16 financial health of the Utility, it would be preferable
17 to make the switch as a package, switch to ELG and
18 eliminate net salvage, correct?
19 MR. DARREN RAINKIE: 'Preferable' is a
20 strong term. I think -- I think what we were trying to
21 do in this period of changing accounting policies is
22 find an overall package that makes sense both for
23 financial reporting and rate-setting purposes. I'm not
24 sure that a reduction in depreciation expense out of
25 the net is preferable, but it's a trade-off we're

1 willing to take, given the circumstances we've been
2 dealt.
3 MR. SVEN HOMBACH: All right. From a
4 rate regulation perspective, though, and from an
5 accounting perspective, it doesn't have to be taken as
6 a package?
7 MR. DARREN RAINKIE: No, the Board has
8 various options, but I suppose the Board has to --
9 well, I -- not 'suppose'. I -- I think the Board has
10 to think about the future ramifications of selecting
11 half of the equation and whether or not that's going to
12 be in the long-term interest of customers.
13
14 (BRIEF PAUSE)
15
16 MR. SVEN HOMBACH: I heard somebody use
17 the term 'vertically integrated' earlier this morning,
18 and I don't recall who it was.
19 But is it fair to describe Manitoba
20 Hydro as a vertically integrated hydraulic utility?
21 MR. DARREN RAINKIE: Yes, it is, sir.
22 Because we have generation, transmission, distribution,
23 all of the above.
24 MR. SVEN HOMBACH: And I took you to
25 the chart earlier, Mr. Rainkie, that indicates that the

1 largest component of depreciation relates to generating
2 stations?
3 MR. DARREN RAINKIE: Yes, sir.
4 MR. SVEN HOMBACH: And currently,
5 Manitoba Hydro's generation is approximately 95 percent
6 hydraulic?
7 MR. DARREN RAINKIE: That number sounds
8 reasonable, sir.
9 MR. SVEN HOMBACH: I'd like to take the
10 panel to page 278 of Board counsel's book of documents.
11
12
13 (BRIEF PAUSE)
14
15 MR. SVEN HOMBACH: Mr. Kennedy, I see
16 the name 'Gannett Fleming' all over this page, and I
17 think that speaks well for your firm. This page was
18 provided in response to a PUB Information Request to
19 MIPUG. It's PUB/MIPUG-I-17. And it indicates which
20 other Canadian utilities are using the average service
21 life method.
22 Mr. Kennedy, when it states 'Gannett
23 Fleming' does that mean Larry Kennedy?
24 MR. LARRY KENNEDY: No, it doesn't,
25 sir. Gannett Fleming's a firm of about twenty-two

1 hundred (2,200) employers (sic). Gannett Fleming --
2 no, effectively for depreciation studies performed in
3 Canada, that may largely be Larry Kennedy, although we
4 do have some of our US analysts that occasionally do
5 studies in Canada, as I do occasional studies in the
6 United States. But effectively, I -- I do most of our
7 Canadian clients.
8 MR. SVEN HOMBACH: Right. You see that
9 there's a number of other hydroelectric utilities like
10 BC Hydro, Newfoundland and Labrador Hydro, Northwest
11 Territories Power, OPG, that use average service life.
12 Are you in a position to advise this
13 Board whether those utilities are currently using GAAP
14 ASL or IFRS-compliant ASL?
15 MR. LARRY KENNEDY: I am in a position
16 to tell you about the ones that I know of off -- if you
17 can go down the list, and if I'm not aware, I'll be
18 very upfront about not being aware, because some of
19 these studies were done a few years ago. BC Hydro, at
20 the time the study was done, where we selected the
21 average service life method, did not use IFRS. They
22 have since converted to a hybrid IFRS methodology that
23 I can best describe as BC-Hydro GAAP. Maybe others on
24 the panel could speak to that more.
25 That would be the same circumstance as -

1 - as BC Hydro or BC Transmission Corporation.
2 Newfoundland and Labrador Hydro, or Nalcor, use average
3 service life more on a unit basis than on a group
4 accounting basis. SaskPower is, I think --
5 MS. SANDY BAUERLEIN: SaskPower is
6 IFRS.
7 MR. LARRY KENNEDY: Yukon Energy
8 Corporation, I am not sure. I did not do that study,
9 so I -- I wouldn't -- I think -- I -- to my -- to the
10 best of my knowledge, they were -- gee, I -- you know
11 what, I'm -- I'm not sure what Yukon Power -- or Yukon
12 Energy's doing.
13 Qulliq, I think is actually following
14 governmental accounting standard policies rather than -
15 - than either IFRS or CGAAP. There's a -- some
16 municipal and governmental agencies can follow a
17 standard known as -- it's a -- it's a governmental
18 accounting standard policy. I can't remember the exact
19 acronym for it.
20 Northwest Territories Power Corp., off
21 the top of my head, I think -- I -- I wouldn't want to
22 put it on the record, because I'm not sure. FortisBC is
23 USGAAP. Ontario Power Generation is USGAAP. Nova
24 Scotia Power is USGAAP. And Hydro One, I am not sure
25 about, just a sec.

1 I'm informed by others on the panel that
2 it's USGAAP.
3 MR. SVEN HOMBACH: The next question
4 will have to go to one (1) of the accountants. The
5 Canadian utilities that are currently using the USGAAP,
6 will they have to switch to IFRS as well, effective
7 next year?
8
9 (BRIEF PAUSE)
10
11 MS. SANDY BAUERLEIN: I'm not entirely
12 sure, based under the requirements of the SEC, whether
13 or not they'd be allowed some type of an extension to
14 stay with USGAAP. I think they're all evaluating as to
15 whether or not they -- it would be possible to stay
16 with USGAAP or to go to IFRS or -- or something else.
17 I can't really speak clearly for each one (1) of them.
18 MR. DARREN RAINKIE: It would also
19 probably, Mr. Hombach, be waiting to see the outcome of
20 IASB, International Accounting Standards Board's
21 deliberation on their rate-regulated accounting project
22 to see if that is something more than int -- interim on
23 it.
24 Right now, the -- we're operating under
25 an interim standard that would allow us to continue

1 rate-regulated accounting. But there is a project to
2 review that and determine whether that will be
3 permanent or not. So they're probably also, you know,
4 watching that very carefully.
5 MR. SVEN HOMBACH: So let's stay on the
6 subject of rate-regulated accounting for a minute. Ms.
7 Bauerlein, you advised earlier that if, for rate-
8 regulation purposes, the Utility would continue to use
9 average service life, two (2) sets of books would be
10 required, correct?
11 MS. SANDY BAUERLEIN: We would require
12 -- two (2) sets of asset sub-ledgers would be required.
13 And we would recognize a regulatory asset to -- for the
14 difference and amortize that over some period of time.
15 MR. SVEN HOMBACH: And if the Utility
16 had chosen to retain net salvage, would it be the same
17 requirement, a separate asset sub-ledger?
18
19 (BRIEF PAUSE)
20
21 MS. SANDY BAUERLEIN: Yes, it would,
22 and we would have a regulatory liability.
23 MR. LARRY KENNEDY: Sir, maybe -- just
24 speaking from experience, I can tell you that there is
25 a number of utilities in this country that use -- that

1 have net salvage that are -- that are under IFRS
2 accounting, and they do it through -- through a
3 deferral account treatment.
4 Now, in fact, the Alberta regulator in
5 Rule 26 in Alberta, and the Ontario regulator have both
6 reviewed that and -- and issued orders in -- in -- to
7 deal with that circumstance.
8 MR. SVEN HOMBACH: Right. Ms.
9 Bauerlein, how much approximately would it cost the
10 Utility on an annual basis to keep such a second asset
11 sub-ledger? You advised how much it would cost to
12 prepare a new depreciation study, but not the annual
13 cost of proceeding on that basis.
14 MS. SANDY BAUERLEIN: We don't have an
15 estimate for that. But again, I would like to
16 emphasize that, especially if we're moving to a -- a
17 different approach such as ASL method that would be
18 compliant with the requirements of IFRS, again, that we
19 have our opera -- we have to also think about the
20 operational areas and how that impacts them as well in
21 terms of the costs to capture information at a greater
22 level of detail.
23 So again, I'm -- it depends which item
24 you were selecting to be different.
25 MR. SVEN HOMBACH: I was specifically

1 asking about any type of a secondary asset sub-ledger.
2 And I appreciate you can't give a detailed estimate but
3 I'm just wondering about the number of zeros involved
4 in that -- in keeping that. And if you're not in a
5 position to answer it right now, I'd certainly take it
6 by way of undertaking.
7
8 (BRIEF PAUSE)
9
10 MS. SANDY BAUERLEIN: We would have an
11 undertaking to -- to think about that. It may be
12 difficult for us to quantify exactly what that would
13 cost. Perhaps we could provide some type of a range
14 estimate.
15 And again, Would it be two (2) asset
16 sub-ledgers as a result of negative salvage, or two (2)
17 asset sub-ledgers as a result of keeping with Canadian
18 GAAP? Again those have two (2) different implications.
19 MR. SVEN HOMBACH: If you can, provide
20 approximations for either or both, it would be useful.
21 MS. SANDY BAUERLEIN: Okay. Thank you.
22
23 --- UNDERTAKING NO. 76: Manitoba Hydro to provide
24 two (2) asset sub-ledgers
25 as a result of negative

1 salvage as well as two (2)
2 asset sub-ledgers as a
3 result of keeping with
4 Canadian GAAP
5
6 CONTINUED BY MR. SVEN HOMBACH:
7 MR. SVEN HOMBACH: I'd like to go back
8 for a moment to PUB Exhibit 22, page 14, the greatly --
9 grossly simplified example of the differences between
10 ELG and ASL.
11 Mr. Kennedy, if the groups are
12 identical, is the depreciation identical under either
13 of those methods?
14 MR. LARRY KENNEDY: I'm not sure if I
15 understand your question, sir. The -- the table 12-8
16 at page 14 of your exhibit I think makes the
17 assumptions that the groups are identical, and we -- we
18 see a different depreciation pattern on that table.
19 MR. SVEN HOMBACH: This is one group
20 with three (3) assets, isn't it?
21 MR. LARRY KENNEDY: Well, I thought
22 your question was -- you took me to the example and
23 that's the one I was following, sir.
24 MR. SVEN HOMBACH: Okay. Let me -- let
25 me try to make myself clear. If Manitoba Hydro used

1 the exact same asset groups for ELG versus ASL, would
2 the depreciation results be identical?
3 MR. LARRY KENNEDY: In the
4 circumstance, if you take an account from Manitoba
5 Hydro, any account, and you were to apply the ELG
6 procedure to that account you would get a different
7 answer than you would as compared to using the ASL.
8 Overall, you -- both methods will recover all the
9 original cost, but at any point in time the
10 depreciation rates would be different.
11
12 (BRIEF PAUSE)
13
14 MR. SVEN HOMBACH: And Manitoba Hydro
15 advised this morning that for IFRS compliant average
16 service life, additional componentization is required.
17 And Manitoba Hydro provided some excerpts from
18 accounting standards and papers by the big four (4)
19 accounting firms in response to MIPUG/Manitoba Hydro
20 Information Request I-17(a).
21 Did Manitoba Hydro ask its auditor
22 whether the existing groupings are IFRS compliant?
23
24 (BRIEF PAUSE)
25

1 MS. SANDY BAUERLEIN: We did hire a
2 consultant, KPMG, that worked with us in -- in our
3 initial analysis of what would be required, and we
4 recognized and KPMG recognized that our existing
5 component groupings would not meet the requirements of
6 IFRS.
7 MR. SVEN HOMBACH: Did -- did KPMG
8 provide you with a written report?
9 MR. DARREN RAINKIE: Sir, maybe I can
10 just jump in. I've been at this game a little longer
11 on this front.
12 MR. SVEN HOMBACH: Certainly.
13 MR. DARREN RAINKIE: In fact, there was
14 a report that was filed with the Board some time ago, I
15 think in -- I'm going to go out on a limb, as somewhere
16 between 2009 and 2010. The first part of the KPMG
17 engagement was what we called a quick scan.
18 So that's where they went through our
19 financial statements as they -- as they stood, and
20 provided us a quick -- that's why it's called a quick
21 scan -- they provided us a quick rundown of areas that
22 they felt we would have to be careful of in terms of
23 IFRS transitioning. And, of course, the property plant
24 and equipment through depreciation was one of the items
25 on their list.

1 But, I mean, if you look at any of the
2 big four (4), you look at the advice from Mr. -- Mr.
3 Kennedy --and, yes, maybe Mr. Kennedy isn't a
4 professional accountant but I think -- as opposed to
5 referring to his experience as a limited, I would
6 suggest to the Board that its broad. He has worked
7 with a large number of utilities in Canada, and he
8 often works with the big four (4) accounting firms.
9 They look to him for thoughts on this, so.
10 You know, we -- we've looked at the best
11 advice. We have our own folks that look at the IFRS
12 accounting standards and we can read standards just as
13 well as anybody else. We don't have to pay somebody
14 four hundred dollars ($400) an hour to read the
15 standards. We have some very good professional
16 accountants at Manitoba Hydro.
17 MR. SVEN HOMBACH: And -- and --
18 MR. DARREN RAINKIE: We've looked at --
19 we've looked at our IFRS conversion advisor, KPMG.
20 We've had discussions with ENY. We had discussions
21 with Gannett Fleming. We've looked at the reports and
22 publications of a number of other big four (4) firms
23 and smaller firms that you refer to in that IFRS IR
24 that you just referenced.
25 They're all telling us the same thing.

1 I have seen nothing contrary to that on this record or
2 any other publication that I've ever seen.
3 MR. LARRY KENNEDY: And, sir, if maybe
4 I can follow up on that a little bit, notwithstanding
5 the ruling this morning that I -- I don't have an
6 accounting designation, I've -- I've been engaged by
7 each of the large firms for advice on Standard 16 and
8 how -- and specifically how Standard 16 can be applied
9 to a rate-regulated company.
10 Not only have I been engaged by the big
11 four (4) firms, I've been engaged by most of the
12 Canadian utilities with regard to working with their
13 audit and their audit consultants. And in fact, I have
14 prepared a paper that -- it was presented to the IASB
15 as part of the diversions of rate-regulated accounting
16 on Standard 16.
17 So while I'm not a professional
18 accountant, I do think I understand Standard 16 very
19 well. And the -- as -- as stated by -- by Mr. Rainkie,
20 this -- the advice and the -- and the -- the
21 information received by Manitoba Hydro from -- from
22 their auditors is identical to the advice that the
23 large four (4) firms have given to virtually every
24 utility looking at converting to IFRS in that in order
25 to -- to convert there would be an additional

1 componentization request to specifically comply to the
2 IAS 16.
3 It's not unique. It's not somebody's
4 kind of one (1) time view. And I -- I've spent many
5 hours in -- in the Toronto offices of all the large
6 four (4) firms trying to convince them otherwise. And
7 as close as we've been able to convince them otherwise
8 is that componentization can be reduced through the use
9 of the equal life group.
10 And that -- that's a very consistent
11 story amongst all the firms and the story they've given
12 to most of their clients.
13 MR. SVEN HOMBACH: So having this
14 accounting experience and IFRS experience on the panel,
15 it might be helpful to actually go to the standard
16 quickly, because you certainly understand it better
17 than I do. It's MIPUG/Manitoba Hydro Information
18 Request I-17(a), page 2 of 9.
19
20 (BRIEF PAUSE)
21
22 MR. SVEN HOMBACH: That additional
23 componentization requirement, is that due to section 45
24 of IAS-16?
25

1 (BRIEF PAUSE)

2

3 MR. SVEN HOMBACH: Which standard is
4 Manitoba Hydro referring to when it says additional
5 compon -- componentization is required?
6 MS. SANDY BAUERLEIN: We are looking at
7 the collective wording in IS -- IAS 16 under paragraphs
8 43, 44, 45, as well as 68, as well again, from many of
9 the interpretations and conclusions that have come from
10 many of the big four (4) firms as referenced, and the
11 advice of -- of KPMG, of course, is one (1) of the big
12 four (4) firms.
13 MR. DARREN RAINKIE: And I might also
14 indicate that Manitoba Hydro is a member of the
15 Canadian Electrical Association and there's a finance
16 sub-committee that met regularly at the front end of
17 the whole IFRS conversion when everybody was deciding
18 what to do. Now, a lot of the companies have gone to
19 USGAAP, so that's not as in -- the committee hasn't
20 been perhaps as active on issues as it was at the front
21 end of this, but every indication that we've had, every
22 piece of advice, our reading of all the material is the
23 same.
24 MR. SVEN HOMBACH: Ms. Bauerlein, you
25 were on the record on June 1st, and I'm referring to

1 transcript page 1,641, as stating that the issue
2 appears to primarily be related to discrepancies in the
3 expected service lives within the same groups.
4 Is that Manitoba Hydro's primary concern
5 when it comes to the grouping? I'm referring to lines
6 15 onwards.
7
8 (BRIEF PAUSE)
9
10 MS. SANDY BAUERLEIN: So what I was
11 getting at in that transcript was referring to again
12 that level of precision that's required under IFRS.
13 And again you can do -- you can choose to use the
14 average service life method with AF -- IFRS. IFRS
15 doesn't pro -- prohibit average service life method.
16 What is does require, though, is that level of
17 precision and to get that level of precision you
18 require additional componentization. So that within
19 that component group the average service life more
20 represents what the actual service life will be.
21 MR. SVEN HOMBACH: So the key issue
22 then still is the discrepancies in service lives within
23 the same group?
24 MS. SANDY BAUERLEIN: It's the
25 dispersion of service lives within the group.

1 MR. SVEN HOMBACH: M-hm. And -- and,
2 Mr. Kennedy, again going back to that simplified
3 example I gave at the beginning of my examination, the
4 closer the service lives are aligned under average
5 service life, I assume the closer the annual
6 depreciation charges would be under either methodology?
7 MR. LARRY KENNEDY: Yes, and when you
8 have a tightly dispersed retirement schedule, if you
9 will, both methodologies will result in a -- a closer
10 bind. There still will be differences, but the
11 differences will be more minimized between. In other
12 words -- and I'm gong to put that in some language that
13 -- that may come up a big later. The higher that mode
14 of the Iowa curve -- the Iowa curve has a mode. The
15 mode represents the tightness of dispersion. So if you
16 have a -- a curve that's a mode 4, like an R4 or an R5,
17 that -- that has a tightening impact on the differences
18 between ASL and ELG. Where you see bigger differences
19 is when that mode, an L1 or an R1, is low, i.e. a one
20 (1), or a two (2), or a three (3), you get larger
21 differences.
22 MR. SVEN HOMBACH: Mr. Rainkie, you
23 recall that in Order 43/'13 Manitoba Hydro was directed
24 to prepare an IFRS compliant average service life
25 methodology for comparison?

1 MR. DARREN RAINKIE: Yes, I remember
2 that directive, sir.
3 MR. SVEN HOMBACH: And while there is
4 no complete comparison study on the record there is Mr.
5 Kennedy's extrapolation study?
6 MR. DARREN RAINKIE: That's correct,
7 sir. This is a little bit like the discussion that I
8 have with my dental surgeon. I asked him if the
9 surgery I've had, Does it help me? And he says, Well,
10 I have to pull your teeth out to tell you. So -- so
11 unfortunately we'd have to spend the two (2) or three
12 (3) years and the millions -- the couple of millions of
13 dollars to prove the point. So we try to do that
14 efficiently through an extrapolation.
15 MR. SVEN HOMBACH: I'm not sure if you
16 just compared cross-examination to pulling teeth, but
17 I'll assume you didn't. So the end result --
18 MR. DARREN RAINKIE: When it relates to
19 depreciation, sir, it might be -- there might be a
20 rough equivalent there. I shouldn't say that with Mr.
21 Kennedy in the room, but...
22 MR. SVEN HOMBACH: Especially if it's a
23 non-accountant doing it. So, Mr. Rainkie, the -- the
24 end result then is Appendix 11.49?
25 MR. DARREN RAINKIE: Yes, it is, sir.

1 And probably very quickly I'll pass you to other
2 members that have put -- put it together, but yes it is
3 11.49.
4 MR. SVEN HOMBACH: Right. Mr. Kennedy,
5 it's -- it's fair to assume that you had primary
6 responsibility to prepare that extrapolation study?
7 MR. LARRY KENNEDY: Definitely the
8 study was prepared by myself. We -- we worked very
9 closely with Manitoba Hydro in -- in doing the study
10 because of, as Mr. Rainkie suggested, to go to the full
11 depth version of all the accounts and all the
12 componentization was -- would be a very long -- long
13 period of time. So we depended on each other a little
14 bit in the circumstance where we -- we consulted to
15 make sure that we had a fair representation of accounts
16 and a fair representation of forces of retirement. And
17 -- and really the ones that we could get that provided
18 that fair representation on a timely basis in order
19 that we could do this report without completely funding
20 my retirement fund.
21 MR. SVEN HOMBACH: Right. And, Mr.
22 Kennedy, if we could go to page 209 of Board counsel's
23 book of documents.
24 You concluded based on your
25 extrapolation study that the difference between the ELG

1 and IFRS compliant ASL is only about $3.5 million per
2 year, correct, looking at -- sorry, line 5 on page 209?
3 MR. LARRY KENNEDY: Yes. That -- that
4 was the conclusion we reached that we had an
5 approximately seven hundred thousand dollar ($700,000)
6 difference on the sample group that we selected. And
7 when we extrapolated that to the -- to the whole asset
8 base, that -- that came out to the 3.5 million.
9 MR. SVEN HOMBACH: Does that sound
10 intuitively correct to you? Because that's only
11 approximately one-tenth (1/10) of the difference
12 between current ASL and ELG, correct?
13 MR. LARRY KENNEDY: In fact, it does,
14 and in fact, it's consistent with the testimony I
15 provided before this commission in 2012, I think it
16 was. I'm trying to remember back. It is, and it is
17 because the -- as -- the further you componentize those
18 -- those accounts, the closer you're going to get to
19 ELG matching that -- that further componentized ASL.
20 MR. SVEN HOMBACH: Have you seen
21 similar results in other IFRS-compliant ASL studies
22 you've prepared for other clients?
23 MR. LARRY KENNEDY: I'm going to need
24 you to say that again. I'm -- I lost track of that
25 question somewhere. I don't know.

1 MR. SVEN HOMBACH: Have you -- have you
2 seen similar differences where you've had to move to
3 IFRS-compliant average service life for other clients?
4 Nova Scotia perhaps comes to mind.
5 MR. LARRY KENNEDY: Well, yeah. And --
6 and unfortunately, that wasn't -- one (1) of my
7 counterparts at Gannett Fleming did the Nova Scotia
8 study, so the -- that's one (1) of the ones that I
9 personally was not involved in.
10 But I would say that, based on my
11 experience -- and it depends on the -- the level and
12 the size of assets -- that would be consistent with
13 what I would expect, given the increased level of
14 componentization.
15 MR. SVEN HOMBACH: For purposes of this
16 extrapolation, you looked at about 20 percent of the
17 total asset base, correct?
18 MR. LARRY KENNEDY: That's correct.
19 MR. SVEN HOMBACH: And you chose a
20 number of accounts, or a number of accounts were
21 chosen. Those are indicated on page 203 of the book of
22 documents.
23 Did you choose those account groupings,
24 Mr. Kennedy, or were those given to by Manitoba Hydro?
25 MR. LARRY KENNEDY: The answer to your

1 question is yes. It was a collaborative effort between
2 myself and Manitoba Hydro. We went back and forth on a
3 number of occasions as to trying to find accounts that
4 would make sense. And they went back to find out if
5 they had sufficient data that we could do this analysis
6 on a timely basis. So it -- it was a bit of a back and
7 forth. I would suggest that some of the
8 accounts were ones I was pretty adamant we should look
9 at, and some of the ones were ones where the -- that
10 really made sense when they came to me and said, Hey,
11 these ones make sense, what do you think? So it was --
12 it was a bit of a combined effort.
13 MR. SVEN HOMBACH: So these were not
14 random statistical samples. These were chosen for a
15 very specific criteria or their specific properties?
16 MR. LARRY KENNEDY: It was not a random
17 statistical sample, no, but they were selected on the
18 basis of some criteria that we outlined in our report.
19 I think if you go up slightly higher on the page that -
20 - that we have in front of us, we -- and if we could
21 get the -- we have the last three (3) there. And I
22 think if you go up one (1) more page, you'll see a few
23 others there. Exactly.
24 It was on the -- we -- we had set a set
25 of criteria for use in selecting the sample. In other

1 words, we -- we didn't try to cherry pick to get a
2 result. We -- we tried to make sure that we had a
3 representative sample in the -- in the development of
4 these criteria.
5 MR. SVEN HOMBACH: When you say,
6 "representative samples," is it fair to say that one
7 (1) aspect of being a representative sample is to have
8 an asset group that is sufficiently large to ade --
9 adequately represent the asset group -- the asset base
10 of a utility?
11 MR. LARRY KENNEDY: I think you mean is
12 your sample group sufficiently large to represent the
13 base?
14 MR. SVEN HOMBACH: Or is your account
15 group sufficiently large, yes.
16 MR. LARRY KENNEDY: I think that would
17 be a fair comment, yes. I think 20 percent of the
18 investment being analyzed is -- is --
19 MR. SVEN HOMBACH: Right.
20 MR. LARRY KENNEDY: -- getting me into
21 that criteria level quite easily.
22 MR. SVEN HOMBACH: Yeah. Well, one (1)
23 example would be the buildings group that was indicated
24 on page 209. If we go to page 259...
25

(BRIEF PAUSE)

MR. SVEN HOMBACH: As I understand it, buildings in total are only about 3 percent of the total asset base of Manitoba Hydro, is it not?

MR. LARRY KENNEDY: I'll take that subject to check, sir.

MR. SVEN HOMBACH: Sure. And -- and you chose to examine the Manitoba Hydro building, which I understood to be unique in the world. I could be wrong.

MR. LARRY KENNEDY: Well, I think, sir, we -- we selected that building to indicate that many component groups have -- have very divergent asset -- asset characteristics. That building in particular, 1) we had information. It's new. We could quite easily put our fingers on the contractual documents.

It -- it's a building that's got some very dispergent (sic) subcomponents like some of the generation plants. For example, we'd have some twenty (20) year life assets, and some hundred year assets. So we -- we -- again, we looked at the availability of the data, the ability to put our hand on costing data, and on accounts that -- that would show some dispersion of assets within when -- when it made sense to look at them.

1 (BRIEF PAUSE)

2

3 MR. SVEN HOMBACH: Will you accept,
4 subject to check, that that building, that was only
5 about half a percent of the total asset base?
6 MR. LARRY KENNEDY: I'm trying to do
7 the arithmetic in my head, sir, and that's dangerous,
8 so I will take that subject to check.
9 MR. SVEN HOMBACH: And for this
10 particular account, if we go to page 214 of the book of
11 documents, the rate under equal life group actually
12 appears to be less than for average service life. Page
13 214, two one four (214), Diana.
14 It's a bit small, but if you have it in
15 front of you, sir, given the Chairman's comments with
16 respect to the -- the allegations of front-loading and
17 the example that we looked at, why would the -- the
18 rate a very new asset like this be less under ELG than
19 under ASL?
20 MR. LARRY KENNEDY: I -- two (2)
21 predominant reasons, sir. One (1) is the component
22 groups of -- of that account where -- where the life
23 was significantly shorter than the average life
24 prescribed were large invest -- or fairly large
25 dollars. And there was a number of large dollar

1 subgroups with short lives. So when you componentize
2 those out, they had a -- a large impact on that -- on
3 that phenomenon that you see, in where the ASL, once
4 componentize, gave you a higher number.
5 The second reason is that building is
6 new, and -- relatively new, and it has not built up a -
7 - an opportunity to be under-depreciated using ESL --
8 ASL when you move to ELG. In other words, one (1) of
9 the -- the large hits when you convert to ASL is the --
10 the fact that all of a sudden, you may appear to be
11 under-depreciated because of the use of the average
12 service life method.
13 And so when you have an old asset that's
14 been working under ASL for a large number of years, you
15 may appear to be quite under-depreciated by the time
16 you convert, whereas with the newer asset, it was
17 really just the true mechanism of the calculation. You
18 don't have that true-up to deal with to bring forth to
19 -- to ELG-wise.
20 MR. SVEN HOMBACH: Well, you were --
21 you were asked in a PUB Information Request to just
22 factor out this one account grouping, which was only
23 half a percent of the asset base, and we can see that
24 if we go to page 222.
25 And in the extrapolation study, just

that one (1) change in assumption appears to increase the difference from 3.6 million per year to four point four (4.4), or about eight hundred thousand (800,000).

(BRIEF PAUSE)

MR. SVEN HOMBACH: Do you see that?

MR. LARRY KENNEDY: I have it in front me, sir, yes.

MR. SVEN HOMBACH: Does that suggest to you that it might be more representative to choose statistical random samples as opposed to selecting relatively new asset groups?

MR. LARRY KENNEDY: In a perfect world where I could depend on the results of my statistical sample to be achievable, and the -- the ability to -- to find data and have information on. And as we heard this morning, we're talking a couple year process to -- to appropriately separate the groups and -- and get the data.

We -- or we didn't have a couple years to undertake this project. I would have loved to have that assignment for a couple years, and -- and maybe a seven (7) digit fee for it. We -- we don't have that, and we didn't have that.

1 And so the use of a -- a pure random
2 sample -- in fact, when we looked at it, it had a high
3 probability of -- of resulting in having the Company
4 chase down something that they would not be able to
5 find in a timely basis.
6 MR. SVEN HOMBACH: Didn't Ms. -- I
7 thought I heard Ms. Hooper say earlier that Hydro spent
8 about five (5) years trying to get the records read in,
9 that Man -- you indicated that Manitoba Hydro's records
10 are significantly better than what you've seen?
11 MR. LARRY KENNEDY: Well, absolutely,
12 but now they've got to go through another whole
13 iteration to get this further componentization.
14 MR. SVEN HOMBACH: Okay.
15 MR. LARRY KENNEDY: And so we have
16 another two (2), three (3), four (4) year, five (5)
17 year project to get this further level of
18 componentization that we would require.
19 THE CHAIRPERSON: Mr. Hombach, could
20 you give me an estimated amount of time that you'll
21 need, because we've been at it for over an hour and a
22 half now, so I think probably we should break --
23 MR. SVEN HOMBACH: I -- I expect to
24 need about fifteen (15) minutes, although I have been
25 wrong in the past, so it might be an opportune time to

1 just take a five (5) to ten (10) minute break.
2 THE CHAIRPERSON: We'll take a break,
3 then. Yeah, let's take a break, a ten (10) minute
4 break, please.
5
6 --- Upon recessing at 2:35 p.m.
7 --- Upon resuming at 2:46 p.m.
8
9 THE CHAIRPERSON: I believe that we're
10 ready to resume the proceedings on the understanding
11 there's some matters to attend to. So, Ms. Van
12 Iderstine.
13 MS. HELGA VAN IDERSTINE: Yes, if I --
14 if I may, Mr. Chair, panel members. Ms. Bauerlein
15 would like to answer the question relating to the
16 annual cost of keeping two (2) sets of ledgers and the
17 -- the undertaking which was requested and which we had
18 taken under advisement. So, Ms. Bauerlein.
19 MS. SANDY BAUERLEIN: So thank you.
20 Over the break, Mr. Chairman, I -- I was thinking about
21 your -- your request, and -- and I'm struggling a
22 little bit to how to actually quantify that for you.
23 We have -- there's ninety-three thousand (93,000)
24 financial asset records in -- in our system right now.
25 So we would be actually duplicating that ninety-three

1 thousand (93,000).

2 On top of that, we have thousands of

3 transactions a month that -- that process through our

4 system. So again, it's -- I can tell you the work

5 effort will be significant, but to be able to actually

6 quantify for you what that would be, I'm -- I'm finding

7 it -- I -- I'm not sure that I could do -- do that at

8 this point to really understand what that work effort

9 would be.

10 I can just let you know that, again, we

11 have a significant volume of assets and we have a

12 significant volume of transactions that go through. So

13 I -- I am having a difficult time wondering if I can

14 actually really respond adequately to your request.

15 THE CHAIRPERSON: This is in relation

16 to maintaining a separate sub-ledger?

17 MS. SANDY BAUERLEIN: The -- the two

18 (2) asset sub-ledgers, yes. And what the ongoing costs

19 would be.

20 MS. MICHELLE HOOPER: If I could just

21 add to that comment. Our current SAP -- is it on? Our

22 current SAP accounting system is not set up in such a

23 way to be able to capture costs that -- for two (2)

24 sets of asset sub-ledgers. So there would be a cost to

25 convert our accounting syst -- like, just to change the

way our accounting system works. And as soon as you're talking SAP and modifications, I suspect we'd have to upgrade our asset accounting functionality. It would be fairly costly to modify SAP.

CONTINUED BY MR. SVEN HOMBACH:

MR. SVEN HOMBACH: Thank you for that clarification.

Just to be clear, does that answer hold true regardless of whether there's a regulatory deferral account for average service life or for retaining net salvage?

MS. MICHELLE HOOPER: System modifications would be required to incorporate either or both of those changes. The nature of the system modifications would differ depending on what the -- what it -- the different costs and accumulated depreciation that had to be tracked.

MR. SVEN HOMBACH: Thank you, Ms. Hooper. Mr. Kennedy, we were discussing your assumptions in the extrapolation study just before the break. There's just one (1) more account I wanted to have a look at with you before we move on.

You included a Bipole III account, correct?

1 MR. LARRY KENNEDY: Yes, sir. We were
2 trying to -- to deal with the -- the question about
3 what happens going forward and how does the ELG versus
4 ASL scenario play out in the circumstance of large
5 capital additions going forward. So we did include
6 Bipole III in that.
7 MR. SVEN HOMBACH: Intuitively when I
8 think about a transmission line, I'm thinking about the
9 towers or I'm thinking about the cable. It's not the
10 synchronous condensers.
11 Why did you choose that item as opposed
12 to, let's say, poles and towers?
13 MR. LARRY KENNEDY: I think we looked
14 at synchronous condensers because we thought they were
15 a group that could be broken out of the -- of the asset
16 group or would need to be broken out of the asset group
17 of -- of transmission lines. So that -- that's an
18 example perhaps -- or not an example -- of where --
19 where the -- the synchronous condensers and the -- the
20 unit transformers in the -- in the stations have a --
21 have a -- perhaps had a fairly different life.
22 So we were looking at units where the --
23 the probability that there would be a dispersion of the
24 -- of the components or the -- the need for additional
25 componentization would -- would fall out. And that --

1 that appeared to be one (1) that fell out of the
2 analysis we did with the internal operation experts of
3 the Company.
4 MR. SVEN HOMBACH: Will you accept,
5 subject to check, that those condensers represent about
6 15 percent of Bipole III assets?
7 MR. LARRY KENNEDY: You said fifteen
8 (15)?
9 MR. SVEN HOMBACH: Fifteen (15), one-
10 five (15).
11 MR. LARRY KENNEDY: I'll take that
12 subject to check.
13 MR. SVEN HOMBACH: Will you accept that
14 the transmission assets represent about 36 percent?
15 MR. LARRY KENNEDY: I'll take that
16 subject to check, sir.
17 MR. SVEN HOMBACH: I can take you to
18 the numbers if you prefer.
19 MR. LARRY KENNEDY: That's fine. We'll
20 -- we'll check it.
21 MR. SVEN HOMBACH: If we could go to
22 page 218 of Board counsel's book of documents. By
23 choosing the condensers, you chose an asset for which
24 the depreciation right under ELG is less than for
25 average service life? And I'm looking at the top items

on that page. Diana, can you scroll the right please a bit?

You'll see that the depreciation rate is about 1.9 percent under ELG compared to 2 percent under ASL?

MR. LARRY KENNEDY: Yes. I'm not sure we chose it because of that. We -- we -- as we identified, we chose an item that we thought would have a disparate average service life. You'll see where, based on that, we -- we ended up with one (1) group having a sixty-five (65) year life and the -- the smaller, shorter group having a life of forty (40) years.

MR. SVEN HOMBACH: Right. But if we look at the difference in rates for the transmission assets as opposed to the condensers, those are found -- found on page 224.

(BRIEF PAUSE)

MR. SVEN HOMBACH: If we go to sub-item (d), it's the opposite for that, right, the depreciation right under ASL is higher than -- sorry.

(BRIEF PAUSE)

1 MR. SVEN HOMBACH: It's significantly
2 lower under ASL than under ELG?
3 MR. LARRY KENNEDY: That's correct,
4 sir.
5 MR. SVEN HOMBACH: One point one-six
6 (1.16) versus one point two-three (1.23)?
7 MR. LARRY KENNEDY: That's correct.
8 MR. SVEN HOMBACH: And that's an asset
9 that represents approximately twice the percentage of
10 the condensers, 15 percent versus 36 percent?
11 MR. LARRY KENNEDY: That -- your
12 arithmetic is correct, sir.
13 MR. SVEN HOMBACH: So by utilizing that
14 asset rather than the condensers, the discrepancy would
15 be increased again, would it not?
16 MR. LARRY KENNEDY: Again -- again, it
17 would be, sir, but I think we need to understand that
18 in the case of the metal towers ver -- and concrete
19 poles, we -- we didn't see, or we didn't recomponentize
20 those into further component groups. That's not a --
21 that's not a -- a class that -- that we thought had to
22 be recomponentized.
23 MR. SVEN HOMBACH: Without going back
24 into detail and running the analysis, would you be able
25 to provide a ballpark as to how much that would

1 increase the discrepancy?
2 We saw the switch from 3.6 million to
3 four point four (4.4) based on the one (1) change in
4 assumptions. How much would this change it?
5 MR. LARRY KENNEDY: I'm not sure I
6 could answer that, sir, without doing a little bit of
7 work. And -- and my fear -- I think your next question
8 is, Can you undertake to do it? And I don't think I
9 can undertake to do that to meet Mr. Hacault's
10 concerns. It's -- it's not -- it just isn't a -- a one
11 (1) night work or -- it's -- it's a fair bit of work.
12 It's a matter of days of work for us.
13 MR. SVEN HOMBACH: Okay. So you'll
14 accept it would increase the difference. I will not
15 ask you to -- to undertake to quantify that.
16 MR. LARRY KENNEDY: I would accept it
17 would likely directionally increase the difference,
18 yes.
19 MR. SVEN HOMBACH: Right. Mr. Kennedy,
20 I'd like to take you to a slide from your direct
21 evidence this morning. If we could go to page 71 of
22 the presentation, please?
23 You made reference to the fact that
24 Manitoba Hydro has detailed actual installation dates.
25 You'll recall that, sir?

1 MR. LARRY KENNEDY: I do, sir.
2 MR. SVEN HOMBACH: Again, I'm not an
3 accountant, but it was my understanding that the
4 Intervenor's concern was not so much that there isn't
5 sufficient installation data, but rather that there's
6 insufficient retirement data.
7 MR. LARRY KENNEDY: You're correct,
8 sir, you're not an accountant. What we're getting at
9 there is on the retirement transactions, the -- the
10 install date on a retirement transaction is recorded,
11 such that we know historically how old an asset was at
12 the time it retired. So the -- the retirement
13 transaction includes the original cost, the account, et
14 cetera, but importantly in -- includes the year that it
15 was physically retired, but also the year that it was
16 physically installed. And that allows us to do our
17 actuarial analysis to -- to look at how old assets are
18 that have retired.
19 And so it's that original installation
20 date on the retirement transactions that -- that I'm
21 saying the Company has, and -- and has done a very good
22 job of -- of going back and -- and getting in a very
23 reliable manner.
24 MR. SVEN HOMBACH: I'm glad I asked
25 you, then. Thank you for clarifying that. We

1 established earlier, Mr. Rainkie, that the biggest
2 asset group that Manitoba Hydro has is the generation
3 group in terms of depreciation?
4 Do you recall that?
5 MR. DARREN RAINKIE: Yes, sir.
6 MR. SVEN HOMBACH: How many dams has
7 Manitoba Hydro retired to date?
8
9 (BRIEF PAUSE)
10
11 MR. DARREN RAINKIE: None to my
12 knowledge, sir.
13 MR. SVEN HOMBACH: So will the
14 retirement of certain Pointe du Bois assets be the
15 first time that a dam will actually be retired?
16 MS. MICHELLE HOOPER: The retirement of
17 Pointe du Bois assets will be the first time an entire
18 dam has been retired, but we have pos -- booked some
19 smaller retirements associated with dams in our -- in
20 our historical records.
21 MR. SVEN HOMBACH: You -- Mr. Kennedy,
22 you provided some examples of actual retirement data,
23 and I don't believe it's in the book of documents, but
24 Diana, if I could ask you to open the MIPUG/Manitoba
25 Hydro Information Requests, and go to I-19(c)?

(BRIEF PAUSE)

MS. HELGA VAN IDERSTINE: Mr. Hombach, in your last question, can you just clarify, when you were talking about dams, were you talking about the dams, or spillways, or what components were you talking about?

MR. SVEN HOMBACH: I was talking about the concrete structures, predominantly. The ones with the longest asset lives.

MS. MICHELLE HOOPER: And --

CONTINUED BY MR. SVEN HOMBACH:

MR. SVEN HOMBACH: I believe dams, dikes, and weirs is the category that it used to be listed in.

MS. MICHELLE HOOPER: Yes. That was -- was the --- the same context as my response.

MR. SVEN HOMBACH: All right. Thank you. If we could go to page 2 of 192? There's an attachment.

(BRIEF PAUSE)

MR. SVEN HOMBACH: As I understand it,

1 Mr. Kennedy, that shows the concern that some of the
2 Intervenors have raised about actual retirement data
3 being available compared to the Iowa curves chosen?
4 MR. LARRY KENNEDY: Yes, this would
5 represent a -- a stubbed Iowa curve where you don't
6 have the -- the black observed dots going all the way
7 down.
8 MR. SVEN HOMBACH: Well, you've only
9 got about the first 12 percent of it?
10
11 (BRIEF PAUSE)
12
13 MR. LARRY KENNEDY: That'd be about
14 correct, sir.
15 MR. SVEN HOMBACH: So is it fair to
16 say, sir, that the selection of curves is significantly
17 a factor of judgment?
18 MR. LARRY KENNEDY: Definitely. And
19 that's -- as I identified this morning, that the use of
20 historic data is only one (1) of many inputs into the
21 choice of that Iowa curve. We spent many hours
22 interviewing the internal operational experts. We
23 spent many hours reviewing industry data.
24 Gannett Fleming is a member of the
25 Canadian Dam Association, and we have a -- one (1) of

our senior partners in our firm is one of the leading experts in dam safety reviews and safety reports, and we rely on some of his expertise within our firm when we do these type of assignments. So we -- we rely on, as I mentioned this morning, a number of -- of other -- of other inputs, not only the historic data.

Had we fit this curve to only the historic data, you would have been fit to something significantly shorter than a hundred and twenty-five (125) years.

MS. SANDY BAUERLEIN: I was also wondering if I could add, and bring up slide 59 from the presentation this morning?

(BRIEF PAUSE)

MS. SANDY BAUERLEIN: As Ms. -- Ms. Hooper had indicated, within all our account groups, we have three hundred and sixty-five (365) component groups where the -- the installation year is known, and therefore we can factor in what the -- the asset retirements are. And we're looking at only twelve (12) where we have to estimate it, and ten (10) component groups where it's statistically derived.

MR. SVEN HOMBACH: So you're saying the

1 example that are provided is one (1) of those ten (10)
2 groups?
3 MR. LARRY KENNEDY: No, it -- it was
4 not. That -- we -- in the case -- on the example that
5 we were looking at, it's a -- a function of that there
6 was a limited number of physical retirements. The ones
7 that we did have, we did have appropriate age data for.
8 MS. MICHELLE HOOPER: I can confirm
9 that. We have full retirement data for all our
10 generating station transactions, which includes the
11 original installation year associated with every
12 retirement transaction that's been booked.
13 MR. SVEN HOMBACH: For the partial
14 retirements, you mean?
15 MS. MICHELLE HOOPER: For every
16 retirement transaction that's been booked, so every
17 dollar of investment that has been removed from the
18 plant accounts.
19 MR. SVEN HOMBACH: Let's go to page
20 259 of the book of documents, please?
21
22 (BRIEF PAUSE)
23
24
25 MR. SVEN HOMBACH: If we scroll to the

1 bottom of that chart -- Mr. Rainkie, perhaps I'll
2 address that question to you -- it indicates that the
3 accumulated book surplus -- scroll to the right,
4 please, Diana -- is about 474 million to date?
5
6
7 (BRIEF PAUSE)
8
9 MS. SANDY BAUERLEIN: That is correct.
10 MR. SVEN HOMBACH: The current practice
11 is to refund any over- or under-contribution over the
12 remaining service life of the asset?
13 MS. MICHELLE HOOPER: The current
14 practice is to amortize that difference into
15 depreciation expense over the remaining life of the
16 associated assets.
17 MR. SVEN HOMBACH: If you take into
18 account net salvage that has been contributed to date -
19 - perhaps let's flip to page 260 of the book of
20 documents. The over-contribution runs to approximately
21 1 billion, correct?
22 MS. MICHELLE HOOPER: The figure of 1
23 billion is correct, but I wouldn't characterize it as
24 an over-contribution. That was appropriately charged
25 into depreciation expense based on the policies that

1 were in place and approved at the time.
2 MS. SANDY BAUERLEIN: I would just like
3 to add that the $1 million also includes the removal of
4 negative salvage in depreciation rates.
5
6 (BRIEF PAUSE)
7
8 MR. SVEN HOMBACH: Ms. Bauerlein,
9 please clarify. The chart on page 260, that's based on
10 average service life, or is that based on ELG?
11
12 (BRIEF PAUSE)
13
14 MS. MICHELLE HOOPER: The -- the table
15 that you're showing on the screen here on page 260,
16 this is the accumulated depreciation variance that was
17 calculated using the average service life methodology
18 with -- without net salvage.
19 MR. SVEN HOMBACH: As opposed to the --
20 the previous page, the 474 million, with net salvage?
21 MS. SANDY BAUERLEIN: Yes, that is
22 correct.
23 MR. SVEN HOMBACH: So that's a
24 difference of approximately 600 million attributable to
25 net salvage?

1 MS. SANDY BAUERLEIN: Approximately 540
2 million.
3 MR. SVEN HOMBACH: I beg your pardon?
4 MS. SANDY BAUERLEIN: It will be
5 approximately 540 million.
6 MR. SVEN HOMBACH: And this is a --
7 this is an amount that would have to be refunded to
8 ratepayers over time?
9 MS. SANDY BAUERLEIN: No. If you think
10 about net salvage, what it is doing, it is recovering
11 the costs associated with retirement and -- and
12 replacement. So if you think about it, over the years
13 we've been replacing our assets.
14 So it's not that there's this large
15 surplus there. We have been replacing and removing
16 assets. So this is just a reflection of that from a
17 depreciation perspective.
18 MR. SVEN HOMBACH: Right. But you
19 can't under IFRS, nor are you proposing to continue to
20 recover net salvage, are you?
21 MS. SANDY BAUERLEIN: No. So it will
22 be factored in over the remaining life of the assets.
23 MR. SVEN HOMBACH: What is Manitoba
24 Hydro's rationale for refunding it over the remaining
25 life of the asset rather than a shorter period of time?

1 MR. LARRY KENNEDY: Sir, the -- any
2 accumulated depreciation surplus is a -- is a function
3 of many factors. And -- and we're talking about the --
4 the factor, if you will, or the -- the occurrence of
5 the net negative salvage.
6 The -- that's -- that's accumulated over
7 the last hundred (100) years or for whatever period the
8 -- the Company's been in operation.
9 To -- to refund that I think it is
10 equally appropriate to refund it over a period of time
11 over the -- the customers that will be using those --
12 those assets, remembering that the net negative salvage
13 component of the depreciation expense that currently
14 exists was -- was charged and -- and implemented on the
15 basis of the Company policy of those days, every day
16 prior to today, basically, to -- to book neg --
17 negative salvage in its depreciation rates and then
18 removing that negative salvage or that -- that build-up
19 by debiting the accumulated depreciation accounts when
20 you have a net negative salvage occurrence.
21 So the -- the going forward accumulated
22 -- or the going forward depreciation rates will be
23 adjusted appropriately in the most common manner that's
24 done throughout North America and that's over the
25 remaining life of the -- of the composite groups, to --

1 to reduce the -- the burden of the depreciation expense
2 to those -- to the -- to those toll-payers.
3 Very seldom, although there is some
4 cases where the -- the variances have been amortized
5 over a differing period, but the most common basis by a
6 long ways through regulatory jurisdictions has been the
7 use of the composite remaining life.
8 MR. SVEN HOMBACH: Mr. Rainkie, does
9 Manitoba Hydro concur?
10 MR. DARREN RAINKIE: Yes, we concur.
11 And when we go back to the earlier discussions we had
12 at the front end of your cross-examination if we bunch
13 this up once again we're already decreasing
14 depreciation significantly through all of the policy
15 choices that we've made. Once again it would be just
16 further decreasing depreciation and making it look in a
17 year where Manitoba Hydro is spending more on assets
18 suddenly that, you know, things were -- were better
19 where they're not.
20 And if you took that the next step to
21 saying, Well, hey, let's -- let's have a lower rate
22 increase then less cash flow to Manitoba Hydro, more
23 debt, and once again building up more pressure for
24 higher rates in the future. So, I mean, I think that -
25 - that's the other -- that's the policy consideration.

1 Mr. Kennedy talked about the technical
2 aspect of this and the common practice in depreciation.
3 Depreciation is an estimate. You quite normally take
4 those variances in over the remaining life of the -- of
5 the assets. But from a policy perspective I think we
6 already have gone very far in terms of trying to manage
7 this impact and -- and then bunching it up even more is
8 even going to further exasperate that -- the -- the
9 issue that we have, sir.
10 MR. LARRY KENNEDY: And -- and, sir,
11 one (1) other point I'd like to -- to add that I
12 neglected off the top of my head when answering the
13 question. The -- this variance that you see at -- at
14 page -- on the -- on the page in front of us here is a
15 -- is -- it's not as if there's a bank account sitting
16 there with that kind of money. It's an estimate. And
17 it's an estimate that's using -- or assuming that the
18 parameters of today have been in place from day 1.
19 And we have not had a constant rate of
20 net salvage recovery in the depreciation expense equal
21 to the -- the rates that we had as part -- that are
22 currently being used by the Company. And in fact I
23 think for a number of years the Company didn't have any
24 net negative salvage in its rates. And so this is
25 really just a -- a snapshot in time on the basis of a -

1 - of an assumption that from day 1 the Company had been
2 including the -- the level required -- or could have
3 been re -- recovering at the level that we're currently
4 recommending, in other words these depreciation rates.
5 It wouldn't reflect the fact that the
6 Company had recovered no negative salvage for a number
7 of years. So it's not as if the Company has collected
8 these amounts. It's the amount that should be -- have
9 -- have been collected versus what we have in the
10 accumulated depreciation account.
11 MR. SVEN HOMBACH: Ms. Bauerlein, given
12 that Manitoba Hydro agrees with the rationale just
13 presented by Mr. Kennedy could Manitoba Hydro please
14 undertake to refile the example that you walked the
15 Board through this morning, found in PUB/MH Information
16 Request I-21, to assume that the deferral account is
17 recovered not over a ten (10) year period, but over the
18 remaining service life of the assets?
19
20 (BRIEF PAUSE)
21
22 MS. SANDY BAUERLEIN: We have done an
23 analysis if we would assume a forty (40) year
24 amortization which would represent the average of all
25 of our assets across all our asset base. But again, a

1 point I'd want to make in doing that is you will -- the
2 longer you have for an amortization period the greater
3 that balance in that regulatory deferral account will
4 grow.
5 And I believe at some point in these
6 proceedings Mr. Rainkie talked about some of the
7 balances that are sitting on the books of BC Hydro. So
8 we do have to be cautious, especially given that we
9 have an interim standard for rate regulation as to what
10 happens in the future and how -- what happens with that
11 balance and as that balance continues to grow.
12 MR. SVEN HOMBACH: Can you advise the
13 Board how high that balance would be after forty (40)
14 years?
15
16 (BRIEF PAUSE)
17
18 MS. SANDY BAUERLEIN: We may just come
19 back with that in a little bit. We'll just take a few
20 minutes to call up that analysis that we've done.
21 MR. SVEN HOMBACH: It might make more
22 sense to just file the analysis in writing by way of
23 undertaking. This way it doesn't have to be done on
24 the fly right now.
25 MS. SANDY BAUERLEIN: That would be

1 fine.

2 MS. HELGA VAN IDERSTINE: Just to be

3 clear, the undertaking you requested was for the life

4 of the assets, and Ms. Bauerlein has stated that she'll

5 provide it for forty (40) years, because that analysis

6 has been done.

7 MR. SVEN HOMBACH: Correct. I retract

8 the undertaking requesting a change in assumption to --

9 to depreciate the deferral account over the remaining

10 service life of the assets. However, I would like to

11 know what the balance of the deferral account would be

12 after the forty (40) year period.

13 MS. SANDY BAUERLEIN: And we can

14 provide that. We can undertake to provide that.

15

16 --- UNDERTAKING NO. 77: Manitoba Hydro to provide

17 what the balance of the

18 deferral account would be

19 after the forty (40) year

20 period

21

22 CONTINUED BY MR. SVEN HOMBACH:

23 MR. SVEN HOMBACH: Mr. Kennedy, I just

24 have one (1) last question for you, given that the

25 lawyer for the City of Winnipeg isn't here. We had an

1 examination earlier on a new LED rate class.
2 Did you, in your depreciation study,
3 make any change in assumptions for LED lighting
4 standards rather than existing ones, or are they all
5 lumped together?
6 MR. LARRY KENNEDY: No, I didn't, sir.
7 MR. SVEN HOMBACH: Sorry, I beg your
8 pardon?
9 MR. LARRY KENNEDY: No, we did not.
10 MR. SVEN HOMBACH: Okay. Do you know
11 if other jurisdictions are treating that separately?
12 MR. LARRY KENNEDY: I would suggest
13 that I haven't -- I can't think of off the top of my
14 head of anybody that has yet. I do know the -- the
15 discussions I've had with operational personnel in
16 various -- various utilities, we've talked about the
17 influence of the LED and -- and the LED lighting and
18 the -- the fact it -- it involves a different standard
19 and a different -- it's a slightly different
20 configuration, if you will.
21 We haven't yet broken that out into a
22 different clati -- category that I can remember off the
23 top of my head. But it definitely would not be common
24 practice. And if there is somebody out there that's
25 done it in Canada, it might be one (1) utility where

we've talked about it at a bit more length, but I can't think of it off the top of my head.

MR. SVEN HOMBACH: Thank you, Mr. Kennedy, and members of the panel. Those are all my questions.

THE CHAIRPERSON: I believe those are all the questions of the -- for today. So with that we'll adjourn the proceedings for today and resume them tomorrow morning when we hear from both counsels from CAC and -- and MIPUG.

So with that, have a great evening everyone and we'll see you tomorrow morning. Thank you very much.

(PANEL RETIRES)

--- Upon adjourning at 3:15 p.m.

Certified correct,

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Sean Coleman, Mr.