MANITOBA PUBLIC UTILITIES BOARD

Re: MANITOBA HYDRO
2004 GENERAL RATE APPLICATION

Before Board Panel:
Graham Lane - Board Chairman
Lens Evans - Board Member
Robert Mayer - Board Member

HELD AT:
Public Utilities Board
400, 330 Portage Avenue
Winnipeg, Manitoba
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APPEARANCES

R.F. Peters	)Board Counsel
Patti Ramage	)Manitoba Hydro
Byron Williams	)CAC/MSOS
Michael Anderson (NP)	)Manitoba Kewatinook Ininew Okimowin (MKO)
Peter Miller	)TREE
Randall McQuaker (NP)	)
Garnet Boyd (NP)	)IBEW 2034
John Osler	)Manitoba Industrial
Patrick Bowman	)Power Users Group
Tamara McCaffery	)
Jurgen Feldschmid	)CCEP

TABLE OF CONTENTS

LIST OF EXHIBITS

LIST OF UNDERTAKINGS

--- Upon Convening at 9:05 a.m.

THE CHAIRPERSON: Good morning, everyone. I just wanted to -- to mention that in Mr. Peter's work we're -- we're hoping to touch on issues that the intervenors may have as they proceed through the process. So, we will see how they make out.

Mr. Peters...?

MR. BYRON WILLIAMS: Mr. Chairman, if I -- if I might, yesterday when the -- when Mr. Peters was asking for some information to be provided in confidence from Manitoba Hydro to the Board not to Board Counsel, I indicated I would speak with my consultant, as well as my clients, and I can just put on the record my client's position and we're not objecting or raising -- we're not objecting to the Board receiving that information as requested in this specific context.

But as we kind of move forward and we're -- we're having a fresh start -- start with this Panel, my clients are always uncomfortable with ma -- material that the Panel receives that -- that they don't get a chance to -- to look at.

In this case it's not relevant to the submissions that my clients are looking to -- to make so they don't feel it's prejudice -- prejudicing their position. It does go to the wider issue of confidentiality as it relates to Hydro's export market and also the -- the prices they're paying for -- for power.

And we do note as we noted in the Clean Environment Commission Hearing in terms of Wuskwatim that the practice in BC in terms of disclosure on the -- on the part of the Utility is much more liberal than it is here. And so that may be an issue that we raise at a later date.

So we just wanted to kind of not raise red flags. We are not objecting and we will not be seeking, kind of, disclosure of this material. But, both in terms of the practice that the Board's using and in terms of the greater issue of confidentiality it might be something that my clients will -- will raise at a later date on something that's more material to -- to their submissions.

THE CHAIRPERSON: Appreciate your comments, Mr. Williams. We'll take it under advisement but in the case of the specific information we provide our undertaking that we will receive information in confidence; we will do exactly that. Mr. Peters...?

MANITOBA HYDRO PANEL re Revenue requirement, Resumed

CONTINUED CROSS-EXAMINATION BY MR. BOB PETERS:

MR. BOB PETERS: Yes, thank you. Good

morning. Mr. Cormie and Mr. Surminski, at Tab 8 of the Book of Documents that was prepared, there is at Tab 8 a copy of an interrogatory MIPUG Manitoba Hydro first round 17 and it's page 205 and there's a similar one measured in energy on page 305 of the same one.

I gathered yesterday that this document does not serve as a template to determine what is available for export sale opportunities, am I correct?

MR. HAROLD SURMINSKI: This document includes dependable energy only which is the lowest, really the lowest flow condition. And so what is available for export is -- has always, almost always greater than that because flow conditions are -- are always greater.

MR. BOB PETERS: Mr. Surminski if what you see on document number 8 in the Book of Documents is dependable energy, that's the minimum amount that you expect in any given year to be available. Would that be correct?

MR. HAROLD SURMINSKI: That is correct. The minimum amount -- yes, and generally that's correct. It's -- it's pushing the system to the limit, so in -- in actual operation there may be more available because the system does not have to be pushed.

But this is -- or less actually. In actual operation we can have energy production less than this but that's because the system did not require it. But whenever this -- it is actually required to push the system, this is what we can get.

MR. BOB PETERS: So your -- would you agree with me that anything you want to commit to in a firm export would have to be over and above what your minimum availability is as shown on Tab 8?

MR. HAROLD SURMINSKI: Yes, that’s right.

MR. BOB PETERS: Can you tell the Board how you arrived at the number of gigawatt hours of energy available for firm export?

MS. PATTI RAMAGE: Mr. Peters, if I could just interject here. I’m going to -- I was confused and I just want to ensure that the Panel doesn’t share my confusion. I was looking at Tab 8 when in fact what Mr. Surminski is referring to is MIPUG Round 1, I believe it’s dash 17 not the document at Tab 8 which is a capacity document.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Thank -- thank you for that clarification, Ms. Ramage. And I do -- I do apologize. Page 3 of 5 of the interrogatory was not included in the brief. Page 2 of 5 was and you are correct, page 2 of 5 talks about capacity. The energy numbers are found on the interrogatory page 3 of 5.

But for discussion purposes I think we translate do we, Mr. Surminski, from the capacity document over to the energy document? Is that how you've -- you've done it?

MR. HAROLD SURMINSKI: I have -- yeah, we can generally talk about the concepts in the same way. But, I actually have pulled out the energy document I've got in front of me.

MR. BOB PETERS: Okay, well recognizing you have page 3 of 5 of interrogatory MIPUG Manitoba Hydro, First Round 17, can you explain to the Board how you arrive at the number of gigawatt hours or energy available for firm export?

MR. HAROLD SURMINSKI: Just -- first of all, for clarification, if you've got 3 of 5, I believe that's the part with DSM, not our forecast DSM, but no DSM. And I think 5 of 5 is really our -- for our more appropriate forecast.

MR. BOB PETERS: All right, thank you. Please continue then.

MR. HAROLD SURMINSKI: Sorry, what was the question now?

MR. BOB PETERS: The -- the question was for you to explain to the Board how Manitoba Hydro arrives at the number of gigawatt hours of energy available for firm exports?

(BRIEF PAUSE)

MR. HAROLD SURMINSKI: Yes, the firm exports are -- are the further firm exports available are the surpluses after the balance between our total supply is netted against our demand.

So, all our demand, including DSM, including existing firm export sales, are indebted against our firm resources. So, that's what the table does. And the bottom line is -- is the surplus that's available for further firm sales.

MR. BOB PETERS: Does Manitoba Hydro commit to firm sales in excess of the bottom line on Table 4, page 5 of 5 of MIPUG Manitoba Hydro, First Round 17?

MR. HAROLD SURMINSKI: No, Manitoba Hydro does not commit to anymore than that.

MR. BOB PETERS: Why is that?

MR. HAROLD SURMINSKI: Because those are -- are dependable, or are guaranteed surpluses that we may have available.

MR. BOB PETERS: Mr. Surminski, yesterday, if I recall, there was generated in the drought year, only eighteen thousand five hundred (18,500) gigawatt hours of energy. Did I recall that correctly?

MR. HAROLD SURMINSKI: Yes, that's correct.

MR. BOB PETERS: And if there were eighteen thousand five hundred (18,500) gigawatt hours of energy in 2004, I see from your Table again on page 5 of 5 of MIPUG Manitoba Hydro First Round 17, that there would be available approximately twenty-one thousand one hundred and seventy (21,170) gigawatt hours. Correct?

MR. HAROLD SURMINSKI: That’s correct. I can explain that.

MR. BOB PETERS: Well, that was my next question is, you’re telling the Board, just so we understand the context, that for dependable hydraulic energy, you have twenty-one thousand one hundred and seventy (21,170) gigawatt hours. So you can do that -- you can generate that in the -- in the worst year of water flows. Correct?

MR. HAROLD SURMINSKI: Yes. The twenty one one seventy (21,170).

MR. BOB PETERS: All right. And then in 2004, you didn’t generate that much. You generated only eighteen thousand five hundred (18,500) gigawatt hours. Why was that?

MR. HAROLD SURMINSKI: That’s relates back to what I was just talking about a few minutes ago. Where we did not have to push the system in 2004. We did not require having the additional energy and storage.

So, they are dependable situation is where we have a higher load than we had in 2004, a higher domestic load, plus firm sales. When we ever -- whenever we have that higher load situation, we have to protect our energy and storage and make sure that we have sufficient energy in storage before the onset of that worst case.

In 2004, we did not require that. We -- we had surplus in our system so we did not have to push the system to the limit. So that is why the generation was less.

MR. BOB PETERS: Could you have used some of that energy in storage and used that instead of going to the export/import market?

MR. HAROLD SURMINSKI: That is another way of operating the system. Is keeping water, is keeping water in storage but it is not necessarily the most economic because keeping water in storage places Manitoba Hydro at risk of having to spill it at a later time should high flows come along.

If you're -- if you've got higher reservoir elevations at all times, whenever you've got high inflows into your system you have the -- the chance that you will not be able to utilize all of your inflows coming into your system and -- and you may spill it. So, it -- it is not the most prudent thing to -- to keep storage in reservoirs high at all times.

MR. DAVID CORMIE: Mr. Peters, maybe I can help out here. The -- the numbers that are on the table that you've been referring to are the capability of the power system. And the analogy is, if you fill your gas tank in your car completely full, how far can the car go on a tank of gas and let's say it was a thousand kilometres.

It may be a very expensive ride now but -- so the capability of your car is -- with a full tank of gas is to go a thousand kilometres. So, the table that Mr. Surminski is saying is that if you have your reservoirs full at the onset of a drought and you're willing to empty the reservoirs or use up all the gas in the gas tank that the capability of the power system hydraulically is twenty-one thousand one hundred and seventy (21,170) gigawatt hours.

That assumes that -- presumes that at the end of your trip you want to have no gas in your -- in your gas tank; you want to have your reservoirs empty. And from the planning context, we have a historical flow record that only has one worst drought on record and the planning criteria says all we have to do is plan to protect against that drought.

And the planners have the ability to -- to say once that drought is over, we don't have to worry about it because the -- the next year after the worst drought on record is a recovery; 1941, 1942 river flows improve.

And so from a planning perspective, for the purposes of determining dependable capability they draw the reservoirs empty and because they have -- they have perfect knowledge that the next year will be a recovery.

From an operating perspective, we don't know what the next year will be. We don't know that this will be the -- whether this will be the worst year on record or whether actually next year will be the worst year on record and that the res -- the water that's in storage has to be hoarded so that you can get through next year.

We're lucky this year was only the third on re -- worst on record. What happened if it would have been the worst on record or a new wo -- worst record.

So, we cannot use up reservoir storages on the hope that the drought will be over at the end of the winter, that rains will come. We have to use reservoir storage as the last resort to serve load and -- and that's the planning people are also doing in their -- in their planning tables, they only draw that water out of storage because their computer model says I have no other choice, I have no other sources of supply available. I've already maxed out my import capability, my thermal generation and the only way I can serve load is to drain reservoirs.

From an operating perspective, we do exactly the same thing. We do not use the reservoir storage, the reserves that are held, unless we're absolutely forced to because -- because there is the risk that conditions will be worse in the subsequent year.

And so when we have an option of purchasing power rather than draining reservoirs, we use that and that's what we did this year. Had there been no import power available in the marketplace, had we not been able to purchase the 8 million megawatt hours.

Let's say, for example, that our purchases had been limited to 6 million megawatt hours. Manitoba Hydro would have been forced to draw 2 million megawatt hours out of storage. Hydraulic generation in that case, instead of being eighteen thousand five hundred (18,500) gigawatt hours would have been twenty thousand five hundred (20,500) gigawatt hours because we would have had no option except to drain reservoirs to keep the lights on in Manitoba.

But that would not be a decision that we would have any choice. We would have to say, well, is it better to have water in reservoirs or have -- keep the lights on in Manitoba.

In the case where we -- we didn't have the ability to purchase, we would have drawn reservoirs down, increased hydraulic generation. The -- the best that we could have done under that circumstance would have been twenty-one thousand one hundred and seventy (21,170) which is the capability of the system. We -- we couldn't draw more water out of storage than the system is capable of.

So eventually, if the drought had been worse and our import capability had been less, there's a scenario where there potentially been shortages of electricity in the Province.

MR. LEN EVANS: I wonder if I could just ask a supplementary question, just for my own edification.

How many -- this will show that my great ignorance of Manitoba Hydro, but how many storage reservoirs do you have? And what are the most -- two (2) or three (3) of the most significant storage reservoirs?

MR. DAVID CORMIE: There are three (3) major reservoirs in Manitoba that Manitoba Hydro controls. Those are -- are Lake Winnipeg, which contains about half the li -- half the storage in Western Canada that Manitoba Hydro depends on, Cedar Lake, at the Grand Rapids generating station and Southern Indian Lake in -- in Northern Manitoba.

There are eighteen (18) reservoirs across Western Canada that -- that contribute to the transfer of energy throughout the year. But there are only three (3) in Manitoba -- three (3) major ones in Manitoba that -- that Manitoba Hydro has complete and -- and full control over and we can manage -- manage for power system operation.

MR. LEN EVANS: Just a second supplementary then. Therefore without the significant reservoirs that we have in Manitoba, the export opportunities would be considerably different then they have been.

MR. DAVID CORMIE: Yes, the -- the reservoirs allow Manitoba Hydro to shift water from periods when it's surplused to periods when it's -- when we're -- when we're short.

And -- and we do that from a planning perspective, we assume that by holding water back in storage and only draining those reservoirs during periods of very low flow, that improves the dependable capability. And -- and by having a higher dependable capability allows us to enter into more long term firm export sales.

MR. LEN EVANS: Just by way of comment, and then I'll shut up. But there was a big controversy in Manitoba in the '60's and '70's whether to go with a high level or low level diversion. And Hydro was going to go with a high level diversion which would not have included Lake Winnipeg.

So, it's really interesting, going to the low level, has given us the Lake Winnipeg asset, if you will. And has contributed, I believe, to the export ability of Manitoba Hydro. I hope that's correct.

MR. DAVID CORMIE: Yes, with Lake Winnipeg regulation we're now able to utilize the storage and control the levels of Lake Winnipeg. With high level diversion and

Lake Winnipeg left unregulated, it would have been, you know, it wouldn't have been under control and we couldn't not -- we could not have used it to firm up our dependable capability.

MR. ROBERT MAYER: Mr. Cormie, why don't you count Lake Manitoba and Lake Winnipegosis as part of the reservoir? I -- I was looking again at the map and I -- I still think I'm correct that the only flow out of Lake Manitoba and Lake Winnipegosis is into Lake Winnipeg out through the Fairford River and etcetera.

And I know that there is a control structure at the Fairford River. I don't know who controls that, but I wonder why we don't consider Lake Winnipeg -- or sorry -- Lake Manitoba and Lake Winnipegosis as part of the water that may well be accessible to us?

MR. DAVID CORMIE: Manitoba Hydro recognizes that there is storage in those; Lake Manitoba as a reservoir and Lake Winnipegosis, it's not a reservoir. It's part of our -- our consideration when we look at the water supply.

However, the Province of Manitoba regulates Lake Manitoba and Lake Winnipegosis is not regulated. It's still in a natural -- natural condition. So, there -- we have no ability -- neither Manitoba Hydro or the Province to change the outflows in and in effect use -- utilize Lake Winnipegosis as a reservoir.

MR. ROBERT MAYER: Am I -- I am correct,

aren't I, that Lake Winnipegosis actually drains out through Lake Manitoba?

MR. DAVID CORMIE: Yes, you are correct.

MR. ROBERT MAYER: Thank you.

MR. HAROLD SURMINSKI: Mr. Peters. Just where we were, when I started the discussion and Mr. Cormie took over and it sounded like -- like there was two (2) different aspects and there actually were.

I was talking about the upper end of the storage range, when I'm saying, how much storage there is when you start the drought.

Mr. Cormie was talking about the end of the drought, where the level is when you -- after the end of the year.

So really, there are the two (2) factors of why the numbers of eighteen thousand five hundred (18,500) and twenty-one one seventy (21,170) are different.

I was talking about the -- we have in our planning, more storage at the start of the period and Mr. -- and -- and in our assumption, as Mr. Cormie has indicated, we drained down to a minimum, so that gives us a wider range. We start with more storage and we drain more out of the lakes, so it gives us more utilization of storage in that year.

Mr. Cormie is saying, well, in operations they can't even go down or they don't think it's prudent to go down to that lower limit. So, he's taking -- leaving some of that storage available for the future.

So, that's -- it's -- it's at both ends. It's at the upper range that some of the storage is not being utilized in that eighteen five (18,5) and also at the bottom end.

MR. DAVID CORMIE: And I think, Mr. Peters, maybe just to close on this or to try and clarify it simply is that we -- we -- we had the capability of generating twenty-one thousand one hundred and seventy (21,170) last year. We chose not to.

And we chose to hold back water and storage because of the uncertainty of the -- of future water supplies, that -- how long the drought would last and out of concern, you know, being able to meet the domestic load should the drought have continued.

So, I don't think there's an inconsistency. It's -- it's a choice as system operators that we make in managing the risk of future supply.

From an energy inflow perspective, if you were to -- if you were -- if you were not to consider reservoir storage, the water supply without manipulation through storage is around -- under the lowest flow conditions is around sixteen thousand (16,000) gigawatt hours a year.

We use storage -- the storage capability of the system to get the -- it up to twenty-one thousand one hundred and seventy (21,170) but there's only -- and in the worst case, there's only sixteen (16) -- about sixteen thousand (16,000) gigawatt hours of energy from inflows.

MR. ROBERT MAYER: Then isn't that your real dependable power?

MR. DAVID CORMIE: That's the -- that's the energy -- that's the water resource that's available. We can -- we can improve on that through the mer -- through wa -- by -- by operating the reservoirs to -- to take water out of reservoir storage to add to that.

MR. ROBERT MAYER: But that's dependable power only for one year because after that, if you don't replace those reservoirs, eventually you have nothing left but what is flowing into the -- into the reservoirs and out of the reservoirs on a -- on a flow through basis to the turbines?

MR. DAVID CORMIE: That's correct. Reservoirs do not create energy. They're just -- it's like a bank account. They're just -- they're just a pla -- they're just a holding. They don't create any -- any additional supply. The -- the water supply is only about sixteen thousand (16,000).

Now, you can move water from one year to the next through the storage but you can't create it with -- with

-- with storages.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: I think the point I want to focus on, Mr. Cormie, is that Manitoba Hydro chose to hold water in storage and import electricity rather than use the water in storage, correct?

MR. DAVID CORMIE: That’s correct.

MR. BOB PETERS: And that decision was made by the system operators which is your group?

MR. DAVID CORMIE: That’s correct.

MR. BOB PETERS: Can you just tell the Board briefly, how that decision is -- is made? Is that a daily decision? Is that weekly? Is it monthly? Is it seasonal?

MR. DAVID CORMIE: Manitoba Hydro uses a planning -- an operational planning process that I referred to the other day about weekly updating.

As we came into the spring of -- came through the winter of 2003, coming into the spring of 2003 and we were finalizing our operational plans, we consider the possibility that river flows in the -- in the year are -- are going to be low.

And we developed -- we have criteria that says that we need to survive the existing drought and we need to be able to carry on and serve load in the following year, as well. We planned for a severe winter in Manitoba.

The -- the load forecast that we're provided with is the load forecast assuming normal weather. It's -- it would be imprudent just to assume normal weather, so we assume an extreme winter.

So, we have a planning process that makes an assumption on extreme loads, makes an assumption on water supply. And -- and we have to be cert -- almost certain that under that set of extreme assumptions that we can serve the -- the load.

We don't make the assumption that the drought will be over at the end of the year. We assume that the drought will continue and so we -- we manage our reservoirs so that at the end of the current year that if the drought were to continue that we have the capability in the following year to continue to serve load at the -- at -- as requested.

That analysis is updated each week. We adjust our reservoir -- our targets each week, our reservoir releases each week and -- and we look at our requirements for purchase power each week and we start going to the forward markets and start covering some of those positions on a gradual basis.

For example, in -- at the first of June last year we were looking under our base case analysis for December deliveries and we were short one thousand eight hundred (1800) megawatts of electricity.

So, in June we don't go out and buy one thousand eight hundred (1800) megawatts of electricity for December delivery. We would lay on about one sixth of those positions in the month of June for December delivery, go through the analysis each week for the month of June and then in July reevaluate and go to the market again to cover off our position.

So, gradually laying on the purchases required so that once we do get to the winter, that we have sufficient resources available to serve load.

So, it's a routine rigorous analysis that takes place beginning with an update of water conditions and -- and that drives our -- our analysis that ultimately leads to the decision to purchase power, or in the years -- in most years when we have adequate water supplies the -- the sale of the surplus energy in the external market.

MR. BOB PETERS: That decision that you make is continuously reviewed as I understand from your answer. I take it you report that regularly through management up to the executive offices?

MR. DAVID CORMIE: Yes, our senior management is kept informed of our operational decisions through regular reporting.

MR. BOB PETERS: Does senior management ever overturn operational decisions of this magnitude?

MR. DAVID CORMIE: I'm in constant communication with -- with my vice-president and we discuss the risks of operating the power system and -- and I take my -- I take advice from my executive.

MR. BOB PETERS: Mr. Cormie, would I be correct -- and -- and let me preface this next question by saying, I appreciate you -- your office doesn't have a rear view mirror in it and that you can't operate what you do in hindsight. And I think we all are clear in this room that -- that you only see the movie from the beginning and you don't get to rewind it.

So, with all those qualifications you now have to consider whether or not the decision not to draw down the reservoirs was good, bad or indifferent. Correct?

MR. DAVID CORMIE: Correct. MR. BOB PETERS: And that's a process that Manitoba Hydro would do internally; is that also correct?

MR. DAVID CORMIE: That's correct.

MR. BOB PETERS: Is that something that you personally do or is it something that colleagues in your department do?

MR. DAVID CORMIE: I -- I think, Mr. Peters, the answer to that is that -- that we have an operation planning criteria that we've established that's not risk free. The -- in -- in setting our plans in place, the advice I gave to my executive is that I was 95 percent sure that we will have adequate supply to serve the load.

And that -- that -- and that's the level of certainty that I operated the power system to . There is residual risk there. There are -- there's catastrophic risks that's possible. But I told my executive that the lights with Manitoba will stay on. And -- and I indicated them -- to them the level of risk that I was taking in operating the power system.

Our customers need to know with certainty that -- that we will not get into an emergency situation. And that's -- you know, we -- we -- we've seen the problems that occur in Montreal with the ice storm a few years ago, how the loss of electric supply for an extended period of time creates a -- has a catastrophic effect on society.

And -- and so we do have -- we do operate in a very conservative mode recognizing the importance of -- of a continued supply, and that we should not be in crisis.

And to draw reservoirs down puts the power system in a state -- potential state of crisis if we guess -- if we've -- if we've assumed that the drought is over and it is not over.

And -- and so, going back to your question of -- of the criteria, we -- we review our planning criteria and our objectives with our executive. We’re -- we’re given the authority to operate the power system according to that. And then to look back in hindsight and say, did you do the right thing, is only valuable in -- in -- into the extent that are the criteria correct?

And -- and I think that’s what we’ve done. Everybody was comfortable with the criteria and -- and we followed the criteria rigorously and there were some financial impacts from that. But we believe that the trade-off of less reliability was unacceptable. And -- and I don’t think anyone has any regrets for -- for setting a very, very high standard of reliability of supply.

MR. BOB PETERS: Thank you for that answer. You say that operating is not without risk and to some extent what I hear you saying is that the -- the risk that Manitoba Hydro was prepared to expose itself to, had a financial consequence more so than a consequence of no lights working for your customers.

MR. DAVID CORMIE: Yes, that’s the -- that’s the trade-off.

MR. BOB PETERS: And the -- the trade-off was financial impacts versus reliability and that’s one that you have to make regularly, correct?

MR. DAVID CORMIE: We routinely operate the power system according to a consistent standard. We do not change the standard routinely.

MR. BOB PETERS: You do evaluate the standard routinely? Would that be true?

MR. DAVID CORMIE: We evaluate our operations routinely. I -- we're not -- we're not constantly reviewing our criteria, no.

MR. BOB PETERS: You say that you did have an opportunity to use hindsight and to make sure your criteria were correct. Did I understand that correctly?

MR. DAVID CORMIE: I said that, yes.

MR. BOB PETERS: Did -- did Risk Advisory of Calgary have an opportunity to also use their hindsight review on your criteria and your operations?

MR. DAVID CORMIE: No. Risk Advisory wasn't requested to give us their opinion on a -- the level of reliability that we operate the power system. They were only asked to look at the options that Manitoba Hydro might use to hedge some of the financial risk.

MR. BOB PETERS: In your review, Mr. Cormie, of the -- of the year passed, would it be correct to say that if you knew then, what you knew now, you could have moderated some of the financial consequences that befell Manitoba Hydro?

MR. DAVID CORMIE: I -- I think with perfect foresight, yes, absolutely. Because I would know now that the Red River was going to go into flood. That the Winnipeg River was going into flood and that my concern for a continued drought would -- would not be there.

It only started to rain on March the 28th of this year. Up to March the 28th, it looked like it was going to be -- the drought was going to continue. And Manitoba Hydro cannot operate the power system on hope. We have to have a plan that says under the worst reasonable set of conditions the lights are going to stay on. And so it's -- so -- I think that's -- that's the issue -- is if -- the responsible way for the power system is to always have a -- a plan that says under the worst reasonable set of circumstances, will service continue?

And -- and I don't think there's anyone would disagree that that would be the prudent way to operate the system.

Hindsight is perfect. It's -- it's interesting and -- and remember when you operate with 95 percent certainty, 95 percent of the time, you're going to have more resources available, but you're protecting against the 5 percent of the time when conditions are going to be worse than what you're assuming.

So, financially we knew that there was some tremendous costs to be incurred from -- for this -- but those costs were being incurred we wanted near certainty and that, in hindsight, some of those costs would -- could have been reduced, if -- if we had certainty about it -- perfect knowledge, but we don't.

And that's the cost of reliability.

MR. BOB PETERS: That's a -- that's a very good answer, from my perspective, Mr. Cormie. I take it that when you say "costs could be reduced" you've attempted to quantify how much that could be with your perfect 20/20 hindsight which we know didn't exist when these decisions have to be made.

MR. DAVID CORMIE: Well, I think the example is -- is going back to the tables that Mr. Surminski is looking at, where the capability of the power system is around twenty-one thousand (21,000) gigawatt hours. And we -- we only generated eighteen thousand four hundred (18,400).

So, clearly, there's another -- there was -- there were several thousand gigawatt hours in storage, let's say 2 million megawatt hours. If would have taken that to the market and avoided purchases, you could have avoided the costs of, you know, several -- maybe a $100 million dollars worth of -- of expense.

And -- you know, so there -- there is a significant cost to -- to doing what we did. But the -- but Manitoba Hydro has planned for that. We've built up reserves knowing that these are some of the costs that need to be incurred and we -- we have done our -- we have kept our house in order in that those reserves were there and the intent was to cover the cost of drought.

And it -- it's not that I've operated inconsistent with the financial plans of Manitoba Hydro. I think our operations and our financial planning are all -- are all linked together. They all assume that we will do what we did and...

MR. BOB PETERS: Just to follow back on a question, Mr. Cormie, that -- who's your vice-president, by the way?

MR. DAVID CORMIE: My vice-president is Mr. Ken Adams.

MR. BOB PETERS: All right. And you said that Mr. Adams was, in my words, kept in the loop as to what was going on from an operations perspective.

MR. DAVID CORMIE: And -- and not only Mr. Adams. I'm in routine communication with the Executive Committee and with the President.

MR. BOB PETERS: Is that through Mr. Adams or is that directly to those committees?

MR. DAVID CORMIE: I present to the Executive Committee as a whole.

MR. BOB PETERS: Can you -- can you tell this Board as to whether from the operations perspective you thought you would be consistent with the criteria established to operate in a certain function, but the -- but you were overruled on that from the Executive?

MR. DAVID CORMIE: I -- I wasn't overruled by the Executive. The Executive supported the -- the operational decisions that were being made and the risks that Manitoba Hydro were taking.

MR. BOB PETERS: What you're really saying is that you -- you establish the criteria and the blue print as to how to operate under various circumstances, and when those difficult circumstances arise, you stick to your plan that was prepared before that situation arose?

MR. DAVID CORMIE: Yes, we -- we take our risk tolerances to the Executive. The Executive has the opportunity to challenge those, to -- to direct me to take more risk or to take less risk.

I receive support for the risk levels that I was taking and I was told to continue following the plan and the criteria that were established.

MR. BOB PETERS: And does it follow then, Mr. Cormie, that the executive would have been aware from the financial impacts side of the occasion to protect the system reliability in future years?

MR. DAVID CORMIE: Yes, the executive was aware of the -- of the financial costs.

MR. BOB PETERS: And that is the executive would be aware that if there was two thousand (2,000) gigawatt hours left in storage or twenty-six hundred (2600) gigawatt hours left in storage that the cost of those -- of leaving that in storage was -- was quantifiable at the time those decisions were made?

MR. DAVID CORMIE: I can't speak for what the executive was aware of. I've --

MR. BOB PETERS: You -- you didn't inform them that by leaving twenty-six hundred (2600) gigawatt hours of energy in storage Manitoba Hydro is going to have to go to the market for that twenty-six hundred (2600) gigawatt hours. And the market's at five (5), six (6), seven (7), eight (8) cents and therefore it's $160 million dollars or $100 million dollars of additional costs?

MR. DAVID CORMIE: We -- we made the executive aware that our criteria was to get through 2003 and '04 and to have this power system in a state to survive continued drought in 2004/05 and -- and...

(BRIEF PAUSE)

MR. DAVID CORMIE: Mr. Peters, maybe a good example was the -- is the effect on storage. Ms. Wray had talked about how the drought started and that there were some costs incurred -- drought costs incurred in 2002/03. Manitoba Hydro could have drawn more water out of storage in 2002/03 and increase the bottom line.

Net revenues would have increased because we would have deferred some power purchases in the winter of 2002 but that would have meant that coming into this year, reservoirs would have been lower and so -- and so the expense this year would have been higher.

So, let’s say example that -- that there $50 million dollars of -- of power purchases incurred -- avoided in 2003 in the first year by drawing reservoirs down. That $50 million dollars is now not available in the second year of the drought.

So, it’s -- as I said before, this is -- this is an issue of cash flow. Storage does not create energy. It just affects the -- the time in which the expense hits the bottom -- in -- the year in which the expense hits the bottom line and so you can’t -- the costs are there, they have to be incurred. The question is do they get incurred in the first year or the second year or the third year. Storage does not -- does not come -- does not create energy that’s -- it -- the energy comes from the rain fall.

So, we could have -- we -- we could have mitigated -- we could have taken more risks in 2000 and -- in 2003/04 by drawing reservoirs down. And let’s do the hypothetical qu -- answer again and we avoided $50 million dollars worth of purchase. There would be then the $50 million dollars less water in reservoir storage coming into this year.

And so me -- and so if you had asked me, are we going to meet our $471 million dollar target this year under median flow conditions I would say no because we've already spent that water. That water was used last year. So, you can't increase the bottom line in one year without affecting the bottom line in the next year.

MR. BOB PETERS: Thank you for that. Since you brought up the previous years, can you indicate whether Manitoba Hydro drew down its Lake Winnipeg storage in 2002?

MR. DAVID CORMIE: We did.

MR. BOB PETERS: And do you know by how much?

MR. DAVID CORMIE: I -- I believe we came into the spring of 2003 with reservoir storages in the system approximately -- normally, energy in reservoir storage at the end of the year is around 10 million megawatt hours and we brought in storages at the end of 2002/03 at 6 million.

So, there were four (4) -- we were 4 million megawatt hours below average coming into the -- into the spring of 2003. And again, because Lake Winnipeg is about half the system's storage, most of that was because Lake Winnipeg was drawn in -- in the previous year.

MR. BOB PETERS: In terms of how much it was drawn down in feet, would you have that information? Or can you translate that into feet for me?

MR. DAVID CORMIE: We don't operate -- we operate based on an aggregate, Mr. Peters, so I think the relevant number is -- is in megawatt hours. And -- and we measure the storage in the system as a whole because we have the choice of either drawing Lake Winnipeg down or Cedar Lake down. And there's an interaction between our -- we -- we ensure that there's enough water in all the reservoirs.

And I believe Lake Winnipeg came into the spring last year at seven twelve point two (712.2). It was -- and it was drawn -- it was drawn throughout this year and it reached a low of a seven eleven point three (711.3) in January and we came into the spring probably around seven twelve point zero (712.0). So, we reached a low late in December and -- and it came up through -- through the late winter this last year.

MR. BOB PETERS: All right, since you're quite conversant to that, in 2003 you're -- you're indicating you also drew down Lake Winnipeg?

MR. DAVID CORMIE: Lake Winnipeg was drawn throughout the year and -- and it was only refilled in the late -- in the late winter.

MR. BOB PETERS: And again, do you know how much it was drawn from -- and I was just getting to learn gigawatts, but back to megawatt -- megawatt hours?

MR. DAVID CORMIE: Well we -- we started out at seven twelve point two (712.2) the reservoir was drawn to a low of seven eleven point three (711.3); that's about point nine (.9) feet. There's two -- 2 million megawatt hours per foot so that would be about 1.8 million megawatt hours was drawn out of Lake Winnipeg storage.

However, at the same time Cedar Lake was operated in a different fashion and so it's really the -- it's sum of all -- all the reservoir operations that's -- that's important.

MR. BOB PETERS: Okay. But while I'm sticking with Lake Winnipeg, then in 2004 was it kept relatively stable in the drought year?

MR. DAVID CORMIE: This is 2004, sir. Right now with the La -- right now Lake Winnipeg is up around seven fourteen point two (714.2).

MR. BOB PETERS: Okay. Ms. Wray has got me talking fiscal years, but I was thinking of -- I don't know if we can convert from fiscal year to megawatts. But let's start with -- but I meant -- I meant fiscal 2004, Mr. Cormie, I apologize.

MR. DAVID CORMIE: I -- I was referring to 2004 -- in '03/'04. At the beginning of '03/'04 Lake

Winnipeg was at seven twelve point two (712.2). It was drawn all summer long and it reached a low at -- at probably mid-winter. And then coming into this spring between January and -- and the end of March it was re-ponded a modest amount. And the Lake now is at seven fourteen point two (714.2) feet and...

MR. BOB PETERS: You mentioned to the Vice-Chair in some of your discussions that you have authority over the Lake in terms of how you draw it down; that is, Manitoba Hydro unilaterally makes those decisions?

MR. DAVID CORMIE: Manitoba Hydro has a license from the Province of Manitoba. The -- when the level is between elevation seven hundred and eleven (711) feet and seven hundred and fifteen (715), Manitoba Hydro has the right to regulate the outflows from the Lake for power purposes.

MR. BOB PETERS: And that tells me that you could draw the Lake down to seven hundred and eleven feet (711). I take that seven hundred and eleven feet (711) above sea level, is that a measurement?

MR. DAVID CORMIE: Yes. Yes. So, if the level of the Lake were to drop below seven hundred and eleven feet (711) at that point, authority for the outflows reverts to the Minister of Water Stewardship and he directs Manitoba Hydro as to what the outflows will be.

MR. ROBERT MAYER: Just following on that and

I was going to ask this question. When you're talking about your reservoirs and how much you actually have in reserve, are you counting all of Lake Winnipeg or are you counting Lake Winnipeg to seven eleven (711)?

MR. DAVID CORMIE: We -- we count it just to seven eleven (711). There's still -- that seven eleven (711) there's still sixty feet (60) of water in the lake so. But -- but what happens, Mr. Mayer, is if you -- if the level gets too low, the water can't go out of the lake because there's restrictions at the outlet.

MR. ROBERT MAYER: I'm aware of that but you fixed some of those restrictions when you did Lake Winnipeg regulation with the two (2) channels and so I'm assuming that you have some ability to get more water out of that Lake than ordinarily used to be there.

MR. DAVID CORMIE: Yes, we can get 50 percent more water out of Lake Winnipeg at almost -- at -- at seven eleven (711) or at seven fifteen (715) because of the channels.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Cormie, reflecting, during that answer that you and I may have disconnected in our -- in our years. When you answered my questions about drawing down of Lake Winnipeg storage, I think you were referring to the beginning of the fiscal year, instead of the end of the fiscal year; what I was referring to.

So, if -- I just want to take you back to 2002/03, I don't think you've answered my question as to whether you drew the lake down in that year. Did you answer that question?

MR. DAVID CORMIE: I -- I did answer that question. I indicated that at the end of fiscal year 2002 and '03, that res -- energy and reservoir storage is approximately 4 million megawatt hours below average. And -- and so I think -- I think I did answer.

MR. ROBERT MAYER: What is average? Average isn't at seven fifteen (715), I take it?

MR. DAVID CORMIE: No, average is -- is just the -- since Manitoba Hydro was able to control the flows out of Lake Winnipeg and Southern Indian Lake in about 1977, so we -- we start -- our -- our period of record for measuring the contents of all the reservoirs goes back to that period of time. So, we have about a twenty-eight (28) year record.

So, it's -- it's the average compared to the twenty-eight (28) years since 1977.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: If I can just take you back to the 2002/03 year, Mr. Cormie, and can you give us what happened to the lake levels during that year, if you know them off by heart?

MR. DAVID CORMIE: In the -- in the Spring of -- of 2002, lake levels were relatively low. I think Lake Winnipeg was probably at about elevation seven twelve point one (712.1). And reservoir storage and the water sheds were -- was -- was very low.

And then, as I indicated, the other day in my testimony, on the weekend of June the 8th to 11th, we had eleven (11) inches of rain in Southern Manitoba and in the month of June we had a record -- a record recharge of reservoirs and that brought Lake Winnipeg up to about seven fourteen point one (714.1) by mid-July.

That was great, except that it stopped raining in -- in July and we had very little rain fall thereafter through -- and that resulted in reservoirs being drawn down coming into the Spring of 2003.

MR. BOB PETERS: Thank you for that, Mr. Cormie. I'm taking from -- from these discussions that the impact on financial -- financially on Manitoba Hydro, I think as Ms. Wray had -- had mentioned, was it yesterday, really started before the drought year. And that's how you saw it as well.

MR. DAVID CORMIE: Yes, the -- the financial impact of -- of the current drought -- the drought started in the Summer of 2002 and that’s when we -- we stopped having normal rainfalls.

And when we prepare our IFF in the Summer, we assume that we will have normal rain throughout the Fall and one (1) of the variations in our financial forecast in 2002 and ’03 was as a result of having extremely low rainfall during the fall of 2002. And so, that -- those dry conditions carried over into 2003 with -- with the lack of snow across Western Canada and the failure of the snow melt run-off in the spring.

MR. BOB PETERS: Are you able to quantify in -- in general terms again, for the Board, how the operations and planning with the criteria that were in place to protect reliability, may have had a financial impact on the corporation?

(BRIEF PAUSE)

MR. DAVID CORMIE: I -- I think, Mr. Peters, it’s too soon to do that. You don’t know if the -- if the drought is really over. And, you know, we could -- we could probably do some estimates. But the question is, what’s the value of the water that was left in reservoir storage?

And if the water in reservoir storage ends up being spilled, the financial cost of the -- of the drought will be -- of the reliability will be very high.

If the drought continues and we end up using those storages to keep the lights on in Manitoba, the value of -- there will be no cost. It will be -- it will have been a wonderful foresight on my behalf to have held that water back because it kept the lights on in the Province and the value at that point would be infinite.

So, really we need to give -- we need to -- we -- we can only say that the story isn’t over year.

MR. BOB PETERS: What you can say is that as the story develops, you continue to assess your criteria to make sure that the planning and operations are complying with the criteria that’s been set out.

MR. DAVID CORMIE: I -- I think, Mr. Peters, we -- we are all learning as we are going here and -- and there are lessons to be taken from what we did in the last year and -- and we will build that knowledge into our future decisions.

MR. BOB PETERS: Mr. Cormie, it may be helpful for the Board if -- if they could see the criteria for your operational planning. Is -- is that available in a document or a -- a brief of some kind that would be available to the Board?

MR. DAVID CORMIE: We can prepare something, yes.

MR. BOB PETERS: All right. Thank you. And I'll ask that as an undertaking from Ms. Ramage.

--- UNDERTAKING NO. 9: Preparation of document showing financial planning.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Also it may be helpful to understand the process that you go through, Mr. Cormie, and I have to confess I don't -- I don't have committed to memory your organizational chart of your company, but to understand the -- the organizational path in which those decisions go through and the -- the people involved in it would be also probably helpful. Could that also be prepared?

MR. DAVID CORMIE: I can provide a general organizational chart, yes.

MR. BOB PETERS: Thank you.

MS. PATTI RAMAGE: Mr. Peters, are you looking for an org. chart or one specific to that decision making function?

MR. BOB PETERS: Ms. Ramage, you -- your latter part of your question is what I was looking for. The -- the company has filed, in -- I think it was in Figure 2.2.1 an organizational chart at Page 9 of 12 and it's -- Tab 2 of your application is a -- is a general overview of the organizational chart.

But in terms of the -- I'm getting more into this area of system operation and -- and planning that I think would be helpful to understand from the Board's perspective.

Can I have an undertaking, Ms. Ramage?

MS. PATTI RAMAGE: Certainly.

MR. BOB PETERS: All right, I appreciate that.

--- UNDERTAKING NO. 10: Provision of general organizational chart

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Cormie, I'm looking at my notes and -- and what you've told me and it -- am I correct that Manitoba Hydro reduced its reservoirs prior to the drought setting in, in summer of 2002 -- 2002/03?

MR. DAVID CORMIE: During -- during fiscal 2002 and '03 Manitoba Hydro drew the reservoirs down lower than what we had anticipated in our -- in the IFF in order to help offset some of the reductions in water supply that occurred during the fall of 2002.

And so, that's one -- one way you can -- if you have surplus energy in reservoir storage and that -- that energy is available for economic dispatch.

We -- we set our I -- we set our IFF targets in the summer of 2002. The rains that we had assumed would occur in the fall of 2002 didn't occur, so we drew the reservoirs to some extent, to help offset that reduction in water supply, to help the Corporation achieve its financial targets.

But there -- we weren't -- we -- we did not draw them to -- to the point where it would threaten the reliable supply of water in 2003. We drew them to the extent that it was -- it was just a financial matter.

But having taken that water out of storage, in -- in fiscal 2002 and '03 it was now no longer available to help mitigate the cost of drought. And that was one of the considerations that you -- you take is that you may take that water to market and avoid some thirty dollar ($30) purchases, only to be faced with the following year, being a sixty dollar ($60) market and -- hmm, you know, hindsight is a -- is 20/20.

But again, when we make that decision, we look at the expected value of the water in storage. And nine (9) years out of ten (10) that water had -- would have much less value than thirty dollars ($30).

So, it -- on an expected value basis, it's the right thing to do is to take the water out of storage early than to leave it, because if you leave it, you always run the risk of spillage and -- and the probability of drought is low.

That’s one of the factors that we considered when we chose to take water out of storage in the spring in -- in 2002 and ’03 and -- and that replacing it in -- in 2003 and ’04 if -- in a really a severe drought conditions, it could be very expensive. But we don’t know what the water conditions are going in the future, so we can only look at the expected value which considers the possibility of all flow conditions occurring.

MR. BOB PETERS: All right and -- and you’re right, you don’t know in advance. But to replace the water that was drawn down in those reservoirs the subsequent year, in 2003/04, I guess the financial records show that did -- that did prove to be costly?

MR. DAVID CORMIE: Yes, it did. Yes, yeah.

MR. BOB PETERS: And that was one of the risks that was known in advance but again you -- you say that you were within the criteria that you’ve established for your planning purposes and that’s how you continued?

MR. DAVID CORMIE: Right. We -- it’s a calculated and in a calculated risk, there are -- there are outcomes that are positive and there are outcomes that are negative and -- and on average, if it’s -- under all conditions, if the decision on an expected value basis makes economic sense, we would -- we would operate that way, knowing that you can make a good decision and at times have a bad outcome.

MR. BOB PETERS: That's fair. Do I take from the answers you've given me, sir, that -- that in the last few years you haven't had an independent review of how you operate under various flow conditions to see if your criteria are -- are considered by somebody independent to be appropriate?

MR. DAVID CORMIE: No, we have had no independent review. No.

MR. BOB PETERS: You indicated to me a few minutes ago that -- that the Corporation is -- is learning from the past year, correct?

MR. DAVID CORMIE: Yes.

MR. BOB PETERS: Can you indicate, when you say learning, what -- what types of things are -- are you learning from the experience that you had last year?

MR. DAVID CORMIE: Well, one of the risks that we had not anticipated was the risk of shortage pricing that -- that a lack of transmission capacity in southern MAPP to bring power into the region to help serve our needs and which would lead me to be more conservative in the future with regard to my assumptions on my ability to import power.

MR. BOB PETERS: Just help me to understand that. I'm going to use a little analogy here to gas and Mr. Derksen and Mr. Warden might be the people who can help you out on this but -- but generally, in Manitoba if we want gas in Manitoba, we can get the molecules here the only question is at what price and that's something that -- that Centra has to consider in terms of its portfolio development and I won't ask Mr. Derksen or Mr. Warden if they agree with that or not.

But if you generally take as an assumption that on the gas side of -- of the business, the molecules can be delivered to Winnipeg; they may have a very expensive price tag but they can be delivered. Can you tell me in the electrical business, can the electrons be delivered to Winnipeg with, again, the only question being the price?

MR. ROBERT MAYER: And never mind the rest of us, just worry about Winnipeg.

(BRIEF PAUSE)

MR. DAVID CORMIE: The -- the analogy to the electrical transmission system in North America is the natural gas transmission system and -- but the -- the -- and you can bring -- you can bring natural gas to Winnipeg from almost anywhere through displacement or it -- it the transport capability is bringing it in and it's really a matter of price.

When the electricity in North America -- North America is made up of several regions, one of which is the MAPP region to which we are connected. Within the regions there is a very strong interconnected transmission system, so it usually is possible to bring electricity to Winnipeg from almost anywhere within our local region but once you reach outside of -- of our region into adjacent regions, Maine, Ekhar (phonetic), Texas, California, it's not possible to buy electricity in California and bring it to -- bring it to Winnipeg and -- and -- and a good illustration of that problem a few years ago when the prices in California were three thousand (3,000) dollars a megawatt.

I was selling electricity in MAPP for thirty (30) dollars. Well, why would I do that? Because I can't reach out into the market because the transmission system is not capable of moving electricity across North America where with natural gas, you can move natural gas almost anywhere. So we don't have as efficient transportation system in electricity as we have gas.

We have very local regional markets and so to assume that we can go to -- out of our region, for example to Chicago, and buy power in Chicago and bring it home, there is some ability but that -- it's very, very limited.

So the -- the electrical studies that have been done in the past for power flows in our region had assumed that Manitoba Hydro was almost always exporting electricity and to assume that instead of being an exporter, we would be an importer was not a situation that we had experienced before in recent times to the extent that we were exposed to last winter.

Normally in the wintertime we export eight hundred (800) megawatts. This winter we were an importer of a thousand megawatts. So there was one thousand eight hundred (1,800) megawatts of flows of electricity in a different direction and that put a strain on the transmission system, not only to other regions but also within the region -- within the Ma -- within the Ma -- the MAPP region itself and -- and this was one of the -- one of our biggest concerns when we were doing our planning for winter operation.

Is it -- was it -- was it a fair assumption to assume that the market and the transmission system could fully deliver that eighteen hundred (1,800) megawatts to northern MAPP to serve our export sales as well as serve the thousand megawatts we needed to serve Manitoba load and that was the one that terrified me the most and that’s the reason that we prepared to use our gas turbines because we had -- we thought that most times that we would be able to bring the power in but not all the times.

And so we were fully prepared to base load our gas generation resources in -- in Manitoba as a contingency plan against those transmission constraints and -- and at times last winter that's what happened. The transmission system was incapable of meeting our demands and we had to purchase much more expensive generation in northern MAPP and we couldn't bring the contracted power home.

I forgot your question.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: I was asking if -- if electricity was transmission constrained whereas gas appears not to be and I think your answer is yes?

MR. DAVID CORMIE: Yes and so --

(BRIEF PAUSE)

MR. DAVID CORMIE: -- so whereas -- whereas -- whereas you would think that you might be able to go to the market and -- and -- and shop around to thousands of sellers, we -- at times last winter, we were captive to two (2) sellers and those are the sellers who are closest to Manitoba Hydro.

MR. BOB PETERS: Mr. Cormie --

MR. DAVID CORMIE: Because of transmission constraints.

MR. BOB PETERS: Yeah. Yes, thank you. I just want to pick up a comment, California was paying an arm and a leg for electricity, you were selling it for a tenth or less of what you maybe could have -- 1 percent of what you maybe could have gotten out there.

Is it possible, sir, that you could sell it into your MAPP customer friends and they could take it and flip it through different transmission arrangements and get it closer to the -- to the high paying markets?

MR. DAVID CORMIE: Some of that is possible but the -- the transmission connections between our region and -- and western United States are very, very small so -- and -- and those people who own those transmission rights I'm sure profited from that -- that basis spread across the regions but the amount of interconnected capability across to the western United States is almost trivial.

MR. BOB PETERS: Just because we've now talked a little bit internationally here, Mr. Cormie, are the rules governing the transmission system of MISO evolving and changing to the point where maybe sometime down the road, Manitoba will be required to generate power regardless of its cost to meet a North American shortage?

(BRIEF PAUSE)

MR. DAVID CORMIE: Manitoba Hydro’s arrangements with MISO is that it will always be in control of its generation assets. We have chosen a relationship that maintains our sovereignty.

MR. BOB PETERS: If you don’t want to produce and provide to MISO, then -- then you don’t have to, it’s voluntary?

MR. DAVID CORMIE: I -- go ahead then.

MS. PATTI RAMAGE: This might be something better less -- left to Mr. Poff (phonetic), but if I could help out there; MISO is a transmission organization. And as Mr. Cormie alluded to, they don’t in any way, control Manitoba -- or it’s my understanding they don’t control Manitoba Hydro’s generation.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: You accept that answer from Ms. Ramage?

MR. DAVID CORMIE: In -- in addition to that, the -- the rules are changing though, and -- and MISO is an independent system operator, and their -- their plans are to dispatch all the generation within the MISO footprint. And -- and Manitoba Hydro has chosen not to have MISO dispatch their generation. We will dispatch our own generation, we will not turn control of our assets over to a foreign authority.

(BRIEF PAUSE)

MR. BOB PETERS: You're not aware then, Mr. Cormie, that -- that MISO may at some point insist on having some dispatch authority over all generation of its members?

MR. DAVID CORMIE: Well, I think that's MISO's objective, and for those utilities who are FERC jurisdiction in the United States, they've been ordered by the FERC to turn their -- their generation assets over to the MISO for dispatch, and that that -- that is now planned to occur next spring, on March the 1st, 2004.

But Manitoba Hydro has an arrangement with the MISO through a coordination agreement, and -- and we are in the process of negotiating and finalizing that coordination agreement. And the basis of our -- our relationship with MISO will not -- will be one (1) that does not turn control over to MISO.

Manitoba Hydro will dispatch our own generators to serve our loads in Manitoba, and to participate in the MISO markets. But we will not turn our generators over to their -- or our transmission system over to their control.

MR. BOB PETERS: All right. Thank you for that. I want to shift gears a little bit here and we've talked about firm export energy, and, Mr. Surminski, and, Mr. Cormie, I think you've told us that on -- on page 5 of 5, of MIPUG Manitoba Hydro first round 17, you get a surplus calculation of energy, and your exports are not -- are not to exceed the surplus; did I get that right?

MR. HAROLD SURMINSKI: Yes, that's what I had indicated.

MR. BOB PETERS: Is that -- is that firm exports, Mr. Surminski, or is that opportunity exports?

MR. HAROLD SURMINSKI: That is firm, because the table is based on firm capability.

MR. BOB PETERS: Can you explain to the Board, briefly, how you determine, and when in a calendar year you would determine your opportunity export capabilities?

MR. DAVID CORMIE: The opportunity capabilities are determined on a weekly basis, based on our -- our operating plans that get updated week -- weekly, Mr. Peters.

And the -- our water resources people do their water supply forecasting, and -- and our -- our computer models then indicate to us how best they operate the power system.

When surplus energy that's available and the power system is best taken to market, it's made available as on a forecast basis to our power traders. And our power traders then, in discussion with the water resource people, decide whether that is a -- whether there's -- with what level of confidence that surplus is available.

And when there's sufficient confidence that that sale -- that energy is surplused to Manitoba's needs, and we will take it to the forward markets and sell it either -- we will take it to the markets either as a forward -- under a forward contract, or we will choose not to take it to the forward markets, if the -- if there's a price advantage not to do so.

(BRIEF PAUSE)

MR. BOB PETERS: When you -- when you look at these opportunity sales on the -- on the forward basis, is that analogous to -- to your gas side of the -- the Corporation's business, in terms of whether or not to place derivatives that you're doing it with physical product?

MR. DAVID CORMIE: Yes, all the -- all the forward contracts -- sales contracts are for physical delivery and our ex -- our expectation is that -- that we will have that energy to sell and we will enter into a contract in order to hedge the price risk.

MR. BOB PETERS: Do you ever buy yourself out of those positions with financial instruments so you don’t have to physically deliver?

MR. DAVID CORMIE: We do -- we do not use financial instruments. We make -- create an offsetting purchase that, in effect, nets out the sale. So, if I were to sell you a hundred (100) megawatts, Mr. Peters, today and for December delivery and November comes along and I need a hundred (100) megawatts because I’ve now lost a generator or the weather is changed and now I’m short a hundred (100) megawatts, you and I may settle fina -- we -- we may -- you may have surplus power and you may sell it back to me.

And so I -- I owe you a hundred (100, you owe me a hundred (100), physically no power will flow, I may have to cut you a cheque though.

MR. BOB PETERS: Did that happen last year?

MR. DAVID CORMIE: For the long term export sales we did -- we did that quite a bit. We settled -- in affect we bought down our positions. Buying down our positions is -- is advantageous for two (2) reasons; it frees up transmission lines and it also avoids the transaction cost.

My sale to you incurs transmission costs and losses. My purchase from you incurs transmission losses and -- and a cost. And if we can settle financially we don’t have to in -- incur those transaction costs. So it's -- it's much better for me to settle with you, avoid going to physic -- delivery even though the two (2) schedules are offsetting.

And -- and then it frees up the transmission system for other opportunities.

MR. BOB PETERS: But, that -- that didn't happen for opportunity sales, did it?

MR. DAVID CORMIE: We -- we had no opportunity sales last year. We had no opportunities sales to the extent that they were done in the forward markets. There were times throughout the winter when, you know, during periods of very warm weather where we had short term surpluses and it -- it would have been advantageous for us to do hourly or daily trading.

MR. BOB PETERS: Mr. Cormie and Mr. Surminski, there's a table found at Document 10 of the Brief of Documents that was put together. It's CAC/MSOS-MH 2nd round 28 question where you provided the costs -- the cost of imports in the on-peak and off-peak periods.

Can you now update that table for actual information? And I appreciate you may not be able to do it from the microphone but if not, provide a -- provide a written update to this interrogatory?

MR. DAVID CORMIE: Mr. Peters, I believe that is already actuals. But let me just check.

THE CHAIRPERSON: Mr. Peters, are you coming to a point in which we could have a -- a break?

MR. BOB PETERS: As soon as I get Mr. Cormie's answer, this would be a perfect place.

MR. DAVID CORMIE: Mr. Peters, let me check on that after and I'll get back to you after the break.

MR. BOB PETERS: Thank you. And thank you, Mr. Chairman.

THE CHAIRPERSON: We'll stand down for ten (10) minutes.

--- Upon recessing at 10:25 a.m.
--- Upon resuming at 10:47 a.m.

THE CHAIRPERSON: I think we'll call the hearing back to order now, if we may. Tempus fugit. Mr. Peters...?

MR. BOB PETERS: Mr. Chairman, just apologise. Mr. Williams has a client to introduce.

MR. VINCE WARDEN: Yeah, just Ms. Desorcy's back here. She heard Mr. Cormie was up for the bulk of the morning and she couldn't resist the temptation, so, Ms. Gloria Desorcy from the Consumers' Association is -- is here, checking on the show.

THE CHAIRPERSON: Welcome again. Mr.

Peters...?

MR. BOB PETERS: Mr. Chairman, before the break, Mr. Cormie and I were -- were talking about updating document 10 in the brief of documents, which is CAC/MSOS-MH-II-28, and I wonder if I could just have that left as an undertaking, or a matter to be taken under advisement by the witness, if that suits his counsel?

--- UNDERTAKING NO. 11: To update document 10 in CAC/MSOS-MH-II-28.

MR. BOB PETERS: I would likewise ask that Ms. Ramage take under advisement, or as an undertaking, providing the forecast for -- on document number 11 in the brief, which is a PUB-MH-II-39, asking if by way of undertaking or under advisement, if Ms. Ramage would ask her witnesses to provide a revised copy, which contains the forecast for 2004/05?

--- UNDERTAKING NO. 12: Provide a revised copy which contains the forecast for 2004/05.

MR. BOB PETERS: And then there were two (2) other Information Requests that I'd like to have Ms. Ramage undertake, or at least take under advisement the revision of them. And they're not in the brief of documents, it is PUB-MH-I-64-A.

There is a table there that has historical and forecasted energy sales, and I'm looking to update to actuals, the fiscal year ending in 2004. It's presently disclosed as a forecast, but it's the actual information that I'm asking the Corporation to -- to provide or at least provide their position on whether they will provide it.

--- UNDERTAKING NO. 13:   To provide updated actual information for the forecasted information contained in PUB-MH-I-64-A.

MR. BOB PETERS: And then I believe lastly, there is an Interrogatory cited as CAC/MSOS-MH-I-37-A, and it has attached at table number 2, which contains actual and IFF-MH-03-1, Electrical Supply and Demand, gigawatt hours at generation. And I'm asking if that could also be updated for actuals for the fiscal year ending 2004.

--- UNDERTAKING NO. 14:   To provide actuals for forecasted amounts of Electrical Supply and Demand, gigawatt hours of generation, contained in

CAC/MSOS-MH-I-37-A, for the
fiscal year ending 2004.

MR. BOB PETERS: I appreciate that's a little wordy, and but I would ask the Corporation to have a look at those requests, and for Ms. Ramage to come back to me with her position, when she is able to do that. Thank you.

MR. DAVID CORMIE: Well, Mr. Peters, for clarification, you asked us to update the table in Tab number 11, forecast for '04/05, which forecast would you like? The one (1) that's in IFF-03? Could you clarify for us so we can be responsive.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Cormie, this isn't meant to be non-responsive, but do you have a more current forecast than IFF-03-1?

(BRIEF PAUSE)

MR. DAVID CORMIE: IFF-03-1, has Manitoba Hydro's official forecast, and that's what we can provide.

MR. BOB PETERS: That will be sufficient then, thank you.

MR. VINCE WARDEN: Mr. Peters, perhaps I can be responsive to those questions at this time. That is with respect to the energy amounts, we can certainly provide that information, and that is contained on -- in Tab 10, which is CAC/MSOS-II-28, we can update the imported energy on that.

In fact, we can give you that number now if you like? The eight thousand (8,000) gigawatt hours that's indicated on that table is -- was actually ninety-six twelve (9612), nine thousand six hundred and twelve (9,612) gigawatt hours.

However, I would rather not update the amount -- the cost of those imports, because as you recall, behind Tab 1, we discussed net extra-Provincial revenue as being the only variable to get to our financial -- or bottom line number for '03/04. So, disclosing that number would in fact do that.

However, understanding the Board's desire to have a -- a -- a updated forecast of what our '03/04 results are, we will provide that through -- by way of an undertaking which would be a range, a reasonable range that is relatively close to what our natural results were for -- for '03/04.

Similarly, if we look at PUB-I -- I believe, 64A, the table there, updating to actual contains financial results which I would prefer not to do at this time for the reasons I just gave and the CAC/MSOS-37A table, however, we can update to provide the energy estimates, or at least an update to the actual to '03/04 for that table.

I hope that's sufficient.

MR. BOB PETERS: Thank you for that answer, Mr. Warden. Just one clarification, sir, on the PUB-MH-I-64, rather than dealing with the dollar amounts, I wonder if you'd be prepared to update the energy amounts for 2004 or whether you have a concern about doing that for the reasons that you've already put on the record.

MR. VINCE WARDEN: We could -- we could do that.

MR. BOB PETERS: Then if you could do that, sir, I think that'll address my request at this point in time, Mr. Chairman. I think what we will do is we will await for the revised forecast from Mr. Warden which we understand will contain a range of -- of net income for 2004 that maybe sufficient as we -- as we move forward.

MR. VINCE WARDEN: Yes, thank you.

MR. DAVID CORMIE: Mr. Peters, I have a response to Undertaking Number 8 from yesterday, if you would like to hear that now. It was with regard to the Manitoba energy demand last year net from energy and that was shown -- you were referring to the table in Tab 6 and the forecast for 2003/2004, the annual net firm energy from Manitoba Hydro was forecast to be twenty-two thousand, one hundred and seventy-one (22,171) gigawatt hours.

The actual net firm energy was twenty-one thousand, eight hundred and ninety (21,890) gigawatt hours, approximately 1 percent lower than forecast.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Thank you for that information, Mr. Cormie. Mr. Cormie, in terms of preparing the integrated financial forecast that Ms. Wray's department handles, can you indicate what assumed export prices are embedded in the IFF?

MR. DAVID CORMIE: In -- in the short term, for the current year and the second year of the IFF, there are three (3) -- three (3) forecasts of -- of export prices provided.

The first is the export prices under our long term firm export sales contracts, and those are computed annually and they're tied to indices and -- and we -- we update those -- those rates and -- and build those rates into our long term extra-provincial revenue forecast.

The second prices are those prices that have been fixed under short term opportunity sales, so it reflects actual contracted rates for the balance of the -- of the current year.

And the third area is where Manitoba Hydro has opportunity sales that haven't -- are indicated but the -- that the price hasn't been established under a contract and so they are considered to be spot market sales in the forecast.

Manitoba Hydro uses industry available forecasts to establish a forward price curve, and -- and those -- those prices are based on -- on the market's current view of what energy will trade at, both in the on and off peak periods.

For the longer term after the second year, Mr. Surminski is responsible for establishing prices in the export markets, and I'll let him respond to that.

MR. BOB PETERS: Before you do, Mr. Cormie, do you -- do you blend the price with Mr. -- for those years, or do you weight a price and -- and embed it. Is it one (1) that you can give us as a discreet number?

MR. DAVID CORMIE: Mr. Surminski's group and -- and our group work closely in this area, and so there is a -- the long term reflects the short term trends as well, so there's no discontinuity in our view of the market.

MR. BOB PETERS: Can you give me the -- how many cents per kilowatt hour you've embedded then for the current and second year of the IFF?

MR. DAVID CORMIE: I'm not -- I'm not understanding what you're asking for?

MR. BOB PETERS: I'm looking for a -- how many cents per kilowatt hour have been used as an assumption?

MR. DAVID CORMIE: For which -- for which sales?

MR. BOB PETERS: I'm looking for them -- I'm looking for them for all years, but with particular reference to the current year and the next two (2) years?

MR. DAVID CORMIE: Manitoba Hydro's forward price view is considered commercially sensitive information, Mr. Peters, and we would prefer not to provide you with that information.

MR. BOB PETERS: But do you blend a number for the purposes of IFF, so it's not -- it's an aggregate number as opposed to disaggregated so that it can't be -- can't be broken down to sensitive information?

MR. DAVID CORMIE: But that would -- that would be an aggregate of all sales, including the firm sales and the opportunity sales and the spot market sales.

MR. BOB PETERS: Yes, I understand that. Is that what's done and then given to Ms. Wray for the IFF?

MR. DAVID CORMIE: Ms. Wray is not given a rate, Ms. Wray is given our forecast of revenues, as well as our volume. We don't -- it's not simp -- it's simplified to that fashion, she doesn't -- she's given our -- our estimates of total revenue. And total expenses, and -- and volumes, but we -- we do that work on her behalf.

(BRIEF PAUSE)

MR. DAVID CORMIE: And it's complicated by the fact that we have more than just a single price, we have a price volume relationship. For example, if all we had was one (1) megawatt hour to sell, we would price that very high. If we had ten thousand (10,000) gigawatt hours to sell, the last megawatt hour would sell at a very low price, and there's a relationship between the volume and the price.

And -- and quite a bit of work is done to come up with those price volume curves. And those are used in our computer models, because the volume that is available for sale in any particular year, depends on water conditions.

And so in Mr. Surminski's analysis, he looks at the price/volume relationship, depending on the flow year, on a monthly basis.

And so not only is he looking at -- he's looking at volume variability, but also our expected price variability, associated with that.

MR. BOB PETERS: Thank you for that, Mr. Cormie, as I am now understanding. Maybe I can simplify it. On Tabs 12 and 13 of the book of documents that I prepared, which I included the TREE-RCM-MH-I-16 question, and the PUB-

MH-II-59 question, you were able to -- to provide an average price of imports and exports, do you see that?

MR. DAVID CORMIE: Yes, we do.

MR. BOB PETERS: Are you able to provide something on the same type of level for the export prices that are embedded in the IFF?

MR. DAVID CORMIE: Overall aggregate, yes, we can.

MR. BOB PETERS: And just for information sake then, do you know what assumed export price Hydro used at the Wuskwatim hearing before the Clean Environment Commission?

MR. HAROLD SURMINSKI: Yes, but they were the -- for Wuskwatim, all that -- what's important was prices out in time and -- and the 2010 period and on.

MS. LYN WRAY: And we also provided essentially a low price -- low export price and a high export price so that we could show the range of prices we might expect. We didn't show the expected price for the reasons of confidentiality that have been eluded to.

MR. BOB PETERS: Is the IFF, Mr. Surminski, does it contain the expected price or does it contain some other determination of the long range once you get out past two (2) years?

MR. HAROLD SURMINSKI: It is the expected price, yes, as Ms. Wray has just suggested.

MR. BOB PETERS: Can you indicate then to the Board, what -- what the high and low range was, Ms. Wray, at the CEC Hearings?

MS. LYN WRAY: I can't recall. It obviously varied from year to year. It was upward sloping for both the low and the high but I can't recall the range off-hand. I could find that out for you.

MR. ROBERT MAYER: If I recall correctly, Ms. Wray, that was an enquiry from CAC/MSOS.

It came by way of motion for disclosure and Mr. Williams and to your lawyers agreed on -- on this upper and lower range. So I'm assuming there's an answer to an interrogatory to Mr. Williams from the previous hearings -- CEC hearings that might actually have all those numbers.

MR. HAROLD SURMINSKI: I can give the general indication of that range in a later time period. The lower price -- that low price was about fifty dollars ($50) a megawatt hour Canadian. And that's the average of all export sales. And the upper end ramp tep (phonetic) or slow tep (phonetic) but it reached somewhere in the order of seventy-five to eighty dollars ($75 to $80) per megawatt hour.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Can you tell the Board, Mr.

Surminski, if that same expected price that's used in the -- that was available or used by the Corporation at the Wuskwatim Hearing, is that the same information as used in the IFF that's before the Board in this Hearing?

MR. HAROLD SURMINSKI: Yes, we have not modified our -- our export forecast at this time.

MR. BOB PETERS: All right. Thank you. To deal with the impact on your capital expenditures forecast by your acquisition of Winnipeg Hydro. Point Du Bois was one of the generating stations that Manitoba Hydro acquired in that transaction; is that correct?

MR. VINCE WARDEN: That is correct, yes.

MR. BOB PETERS: And as I understood it there was a plan to double the capacity of that generating facility?

MR. VINCE WARDEN: The -- Winnipeg Hydro had plans to increase the capacity of Point Du Bois and Manitoba Hydro has not reached a conclusion on that yet.

MR. BOB PETERS: All right. There was some money put aside in the capital expenditures forecast. I thought it was in the neighbourhood of $421 million dollars of total cost for that project. So are -- are you telling the Board that that's not a -- that's not committed yet?

MR. VINCE WARDEN: That's right.

MR. HAROLD SURMINSKI: And in addition, it may not be required or -- it’s not necessary to expand the plant. Just to keep the plant running will require sufficient expenditures.

We expect after 2010 that the license actually -- when our power license expires in 2011 and it would take significant dollars to upgrade the plant just to keep it running.

So that’s one of the reasons why the -- the capital budget includes a number in that area.

MR. BOB PETERS: So, the capital expenditures forecast amount is not to increase capacity but to retain existing capacity? Is that the correct answer, Mr. Surminski?

MR. HAROLD SURMINSKI: It is an expectation that one or the other will take place. But it may not be quite as high to -- to maintain the plant. It may not cost 400 million but it could be very near to that.

MR. VINCE WARDEN: Yes, I think, Mr. Peters, the capital expenditure forecast document was -- was filed and at page 20 of that forecast document it describes what is included in the $421 million dollars.

So, it is a rehab of Point Dubois, including an extension of its useful life for -- for seventy-five (75) years.

MR. BOB PETERS: But as I understood the answer from Mr. Surminski, there's not been a decision made on whether or not to -- to extend its useful life?

MR. VINCE WARDEN: That's -- there's been no commitment at this point in time. That -- that would be the capital costs of -- of doing that, but it has not been committed at this date.

MR. BOB PETERS: Did Manitoba Hydro take into account the $421 million dollar capital costs, when it -- when it purchased Winnipeg Hydro's assets?

MR. VINCE WARDEN: Yes, we had a range of capital expenditures for Winnipeg Hydro, that we considered in the evaluation; yes, we did.

MR. BOB PETERS: Well, what about the Slave Falls Generating Station; are there any plans to upgrade that?

MR. HAROLD SURMINSKI: The Slave Falls Plant generally is in much better condition, and a newer vintage of -- of turbines, and in general, we do not have plans specifically, and the costs would be much lower. It would not be a very significant cost, relative to Point Dubois.

MR. ROBERT MAYER: This number that Mr. Peters is mentioning, four hundred (400) odd million, that's -- you would need to spend that much money just to retain the sixty-six (66) megawatts to -- the little map over there tells you we produce out of Point Dubois?

MR. HAROLD SURMINSKI: Yes, generally, that is our first estimate.

MR. ROBERT MAYER: Wuskwatim's starting to look pretty good.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Surminski, I don't know that I recall -- actually I -- let me word it this way, don't recall anything in the capital expenditures forecast, and I may be wrong about the Slave Falls rehab or upgrading; do you recall if anything has been put in there?

MR. VINCE WARDEN: No, there's nothing in there -- specifically in the capital expenditure forecast for -- for Slave Falls.

MR. BOB PETERS: In terms of the -- the new head office building, can you just clarify for the Board, by way of your contractual agreement with the City of Winnipeg, by what date does a shovel have to be placed in the ground to start your construction?

MR. VINCE WARDEN: Yes, in accordance with the agreement -- the purchase agreement, construction on the new downtown office tower would have to commence five (5) years after the date of purchase. So, the commencement date is five (5) years after September the 3rd, 2002.

MR. BOB PETERS: And just refresh my memory as to what are the current plans for that construction? So -- so you'd have to start it by September 3rd, 2007, is what I'm hearing your answer to be?

MR. VINCE WARDEN: That's right.

MR. BOB PETERS: And but you -- you have a -- are you planning to construct sooner than that?

MR. VINCE WARDEN: Yes, if everything goes according to -- to our current plans, deconstruction of the existing site -- site will start this file and construction will be in the spring of 2005.

(BRIEF PAUSE)

MR. HAROLD SURMINSKI: Maybe, Mr. Mayer, I could just -- you mentioned the Point Dubois was sixty-six (66) megawatts, it's -- it's seventy-seven (77) or seventy-eight (78), yes. And with rehab it could be up to about ninety (90) megawatts through rehabilitation. So, is a little more -- it makes it a little more attractive relative to Wuskwatim.

MR. BOB PETERS: Mr. Surminski, what's the capacity of Slave Falls?

MR. HAROLD SURMINSKI: That's about seventy (70) megawatts.

MR. BOB PETERS: And when you acquired the assets of Winnipeg Hydro, did you consider any capital expenditures that would have to be made to either refurbish or rehabilitate Slave Falls?

(BRIEF PAUSE)

MR. HAROLD SURMINSKI: We did not expect that there'd be -- there would be significant costs at that plant. Re-ruddering, that is replacing the turbines, normally is an economic decision, and -- and we do review that, because new technology can -- can be more efficient in -- in producing power.

So, we -- that's part of our supply side enhancement program. We -- we review older plants and -- and look at the economics of -- of replacing turbines, if it can be justified, especially if there's an outage for other reasons.

When there is a rehabilitation of other equipment and the unit has to be taken out of service for up to six (6) months; that is an appropriate time to -- to rehabilitate and replace the turbine with a more efficient one.

MR. BOB PETERS: You didn't consider re-ruddering Slave Falls when you did your analysis on purchasing Winnipeg Hydro's assets?

MR. HAROLD SURMINSKI: No, that was not required.

MR. BOB PETERS: And just on the head office building, if I can ask this maybe of Mr. Warden; as I understood your answers to me, sir, you're going to commence construction about two and a half (2 1/2) years before you may be legally required to. Would that be correct?

MR. VINCE WARDEN: Yes, as I indicated the -- the schedule -- according to the agreement was we would commence within that five (5) year period. It doesn't say at the end of that five (5) year period, it says within that five (5) year period and that's what we're doing.

MR. BOB PETERS: And can you tell the Board whether you -- what your plans are for the Taylor Avenue current headquarters?

MR. VINCE WARDEN: Still no firm decision has been made on that as to whether we'll retain 820 Taylor. That will have some influence on the size of the building downtown if we decide to dispose of that.

At this time, they're looking at what the potential disposal value of 820 Taylor may be. So, that'll factor into that decision.

MR. BOB PETERS: All right, thank you. While you had the capital expenditure forecast out, Mr. Warden, I recall that one of the directives from the Board in Order 7/03 was for Manitoba Hydro to segregate their capital expenditures that could be attributed to export related activities.

Do you recall that directive in general terms?

MR. VINCE WARDEN: In general terms, yes, I do recall that.

MR. BOB PETERS: And subject to being corrected by your colleagues or your Counsel, I don't know that's been filed yet with the Board. Do you know if it has?

MR. VINCE WARDEN: No, it has not.

MR. BOB PETERS: Is that something that the Board can expect from the Corporation soon?

MR. VINCE WARDEN: Well, it really speaks to the -- the cost of service issue that we'll be perhaps discussing later on with the -- the other panel as to how costs are being allocated to an export class if we choose to go that direction.

MR. BOB PETERS: So, we should discuss it with that panel?

MR. VINCE WARDEN: I think that would be more appropriate, yes.

MR. ROBERT MAYER: I -- what I heard earlier is that we're looking at this NERA report and so we really haven't separated out those costs that the Board asked for in its previous Order.

MR. VINCE WARDEN: At this time that is -- that is correct.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Ms. Wray --

MR. VINCE WARDEN: You see it would be -- if I could just elaborate, perhaps, a little bit on that -- that answer. It would be pretty much impossible to take our existing assets and separate them saying what -- which specific asset was for export.

Because there were really no assets that were constructed specifically for export purposes.

So, when the Limestone generation -- generating station was put into service, for example, in 19 -- the last June it was put into service in 1992, we had a surplus capacity because the whole capacity of the Limestone was not required to serve the Manitoba load.

So, it could be argued that anything over and above the requirement for the Manitoba load could be allocated to the export class, if we were to have an export class.

But, that has not been done at this point in time.

MR. ROBERT MAYER: I -- I recognize that, and

I'm expecting that it isn't going to be done by the time we get to the other panel either, so I'm not sure why we would be waiting for that.

MR. VINCE WARDEN: Well the other panel, we can speak when we get to the NERA report there are meth -- there's a methodology in there as to how the cost could be allocated to a -- to an export class if we go that direction.

To be clear, though, we have not set up an export class for purposes of this Rate Application.

(BRIEF PAUSE)

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Warden, maybe we'll -- we'll come at this again with the other panel, but on your Capital Expenditures Forecast, you're talking into the future into -- into new capital programs, correct?

MR. VINCE WARDEN: Yes, the capital expenditure forecast covers the ten (10) year period to 2014.

MR. BOB PETERS: And some of those future forecasts are going to expressly be used for export purposes, would that also be correct?

MR. VINCE WARDEN: Well, the Wuskwatim is -- is the one (1) major capital expenditure that's in the forecast that would be used -- constructed solely for export at this point in time, yes.

MR. BOB PETERS: Well, what about -- the same could be said for Gull Generating Station, could it not?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And likewise Conawapa?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: The Bi-Pole 3 would also be for that purpose?

MR. VINCE WARDEN: No, no, that's a reliability issue that Bi-Pole 3 is being constructed for.

MR. BOB PETERS: Are any of the transmission lines that are in the Capital Expenditures Forecast, going to expressly and only be used for export?

MR. VINCE WARDEN: Well, there -- there's a small amount of transmission that's associated with Wuskwatim, and if Conawapa proceeds, and I don't know, I'd have to check as to whether or not -- I don't think we have any transmission -- transmission associated with Conawapa, specifically in this -- in this forecast.

MR. BOB PETERS: All right. I'll come back to that perhaps at another time. I think, Ms. Wray, and Mr. -- Mr. Derksen, it's maybe time we talked -- talked numbers, and hopefully keep the attention of those -- those listening to us.

Ms. Wray, there's going to be another Panel of witnesses for Manitoba Hydro come on to talk about cost of service and rate design, and as a starting point for that second Panel, that Panel starts with a dollar amount of revenue requirement, that it needs to recover from the consumers in rates, would you agree with that?

MS. LYN WRAY: Yes.

MR. BOB PETERS: And really, notionally, if we could then, this revenue requirement Panel of which you are a member, is to make the case to this Board as to what revenue requirement this Board should approve for the Corporation, for the test years and then leave it to the Cost of Service Rate Design Panel to determine which customers pay what amount?

MS. LYN WRAY: That's correct.

MR. BOB PETERS: And can you tell this Board from a starting point, what dollar amount of Manitoba Hydro -- is Manitoba Hydro's revenue requirement; let's start off for the 2003/04 year, actually I guess that's probably that should be out of bounds, until we hear further from Mr. Warden, but maybe we should go then to the test years, in terms of the revenue requirement that you're seeking?

MS. LYN WRAY: Well, in terms of the incremental rate increases in 2004/5, we're seeking approximately $28 million dollars in additional revenues, and in 2005/6, taking into account that rate increase for 2004/5,

$51 million dollars, approximately, in incremental revenues. And they relate to proposed rate increases of 3 percent and 2.5 percent, respectively.

MR. BOB PETERS: And in terms of the total amount of the revenue requirement, that is not just a deficiency, or the -- the additional portion that you're mentioning; how much do you calculate that to be?

MS. LYN WRAY: Well, the total revenues and expenses, which -- is that what you're -- you're asking for?

MR. BOB PETERS: Yes.

MS. LYN WRAY: Total revenues would be 1.403 million -- millions of dollars in 2004/5, and what -- sorry, one four zero three ($1403) millions of dollars, one four one-one (1411) for 2005/6.

MR. BOB PETERS: Would I be correct in understanding the $1.403 billion dollars to being -- that's the revenue requirement that you want recovered from -- included in the recovery of -- from the rates of consumers?

MS. LYN WRAY: I suppose that's true, we don't tend to view it quite in that context for the electricity operations, but I think technically that would be our total revenue requirement, recognizing that a fair chunk of it is being supplied through export revenues.

MR. ROBERT MAYER: So, then the revenue requirement from rates is 1.403 billion, less your expected net export?

MS. LYN WRAY: And also -- well, actually, we're looking at the gross line, so it would be less the gross exports, less also about $7 million dollars in other revenues.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Ms. Wray, when the Corporation was before the Board at the Status Update Hearing, the Board had an opportunity to review the IFF, Manitoba Hydro 01-1; is that correct?

MS. LYN WRAY: Yes and there was also an update to that presented at the time which had some further adjustments.

MR. BOB PETERS: And subsequent to that, you were also responsible for preparing the Manitoba Hydro IFF 02-1?

MS. LYN WRAY: Yes, that would have been in the fall of 2002.

MR. BOB PETERS: And you've also done the Manitoba Hydro IFF 03-1 that's file as part of this Application before the Board?

MS. LYN WRAY: That's correct.

MR. BOB PETERS: Ms. Wray, I wonder if I could with you walk through the IFF 01 to 02 to 03 on a couple of selected areas. And I'm going to try to not bog down in the numbers, so I'm looking more for qualitative answers maybe than specifically quantitative and I know that's maybe sometimes difficult when we deal with dollars and cents.

So -- but with that goal of mine in mind, I do note that document number 21 that is included in the brief of documents is a -- is a document that was not in Manitoba Hydro's materials. It was a document that was generated and provided to your Counsel, purportedly being a comparison of Manitoba Hydro IFF 02-1 with Manitoba Hydro 03-1.

MS. LYN WRAY: Yes.

MR. BOB PETERS: Have you had a chance to review that?

MS. LYN WRAY: Yes, I have.

MR. BOB PETERS: All right. And let's assume the -- the numbers are -- are accurate then unless we come across something that doesn't seem to fit and you'd also be aware generally then of your Manitoba Hydro IFF 01-1?

Would that be correct?

MS. LYN WRAY: Yes.

MR. BOB PETERS: Now, in terms of the general consumer revenue, the first item under disclosure, back -- and if we look to -- if we look to 2004 we see that the forecast in IFF 01 was about 762 million; that was update to 880 million and now it's updated to 801 million, if I've --

I’m sorry, 901 million, if I’ve followed correctly the materials?

MS. LYN WRAY: Yes, I -- the page I have before me just has the IFF 02 numbers but certainly that versus IFF 03 is as you indicated.

MR. BOB PETERS: All right. If you can just take my numbers as assumed to be correct and -- and that way if there’s any complications, it’s because I gave you the wrong number.

But can you indicate to the Board why general consumer revenue would have jumped from your IFF 01 to your IFF 02?

(BRIEF PAUSE)

MS. LYN WRAY: It would have been largely to do with the load forecasts since there was no rate increase at that time.

MR. BOB PETERS: And would you also agree with me that -- that Winnipeg Hydro became part of the Manitoba Hydro customer base and their revenue would have been added as general consumers revenue?

MS. LYN WRAY: Yes, in fact, that would have been the lion’s share for that particular forecast.

MR. BOB PETERS: All right. And -- and before

Winnipeg Hydro was -- I'm sorry, before the Winnipeg Hydro customers were converted to Manitoba Hydro customers, how, if at all, were Winnipeg Hydro customers reflected in your IFF?

MS. LYN WRAY: We used to receive a copy of the City's load forecast and then our own load forecasting department would apply its own analysis and add that to the load forecast for Manitoba Hydro's customers to derive a total system load forecast.

MR. BOB PETERS: And --

MS. LYN WRAY: We also had a cost sharing agreement with Winnipeg Hydro and accordingly, there was a line in the IFF that reflected the revenues that we would receive from them under that agreement.

MR. BOB PETERS: And moving this consumer's revenue then to increase from the $880 million dollars to $901 million dollars in the last two (2) IFFs that we're talking about; your answer before was mainly related to the load forecast as I understood it?

MS. LYN WRAY: Ye -- yes and the -- the movement from IFF 02 to 03, there were two (2) factors. One was the load forecast was up and the other one there was somewhat of a decrease in our revenues as a result of PUB Order 154-03 which had a rate reduction.

MR. HAROLD SURMINSKI: What did you quantify the -- the PUB Order rate reductions to be?

MS. LYN WRAY: I believe in the first year the impact was about 6.5 million and then it grew thereafter in around the 7 million a year range, I believe. It may have grown more in subsequent years just because of compounding.

MR. BOB PETERS: And that $7 million revenue reduction was as a result of not only the rate decreases to the general service customers but also the impacts on the winter ratchet?

MS. LYN WRAY: I believe so.

MR. BOB PETERS: Ms. Wray, on Document 21 that you and the Board Members will have, the next line talks about additional monies. This additional monies line comes as a result of the revenues to be recovered through additional rate increases or other matters, correct?

MS. LYN WRAY: Yes.

MR. BOB PETERS: And not only additional dollars but there's a table that has additional percentage and the percentage rows deal with the percentage of rate increases that Manitoba Hydro imbedded in their IFF's when they were being prepared?

MS. LYN WRAY: Yes. So for example, in 2000 -- in the 2002 IFF we had anticipated a 2 percent rate increase for 2004/05. Actually in a number of preceding IFF's we had always assumed some sort of rate increases and then usually in about the 2 percent range recently and in many cases did not -- on most cases in the past did not go forward and asked for those rate increases.

MR. BOB PETERS: The additional revenues comes only then from the rate increases that were imbedded into the IFF's?

MS. LYN WRAY: Yes. And again, just by way of caution anything after the first two (2) test years is nothing more than an assumption.

MR. BOB PETERS: And the assumptions that you have used in IFF-01 and the one they used in IFF-02 was always for a 2 percent rate increase starting in approximately 2005 and going out, correct?

MS. LYN WRAY: Yes. The -- for the IFF 2002 forecast assumed 2 percent going out whereas our current forecast in the so-called assumptions years is 2.5 percent.

MR. BOB PETERS: Okay. And you did have a 2 percent assumed rate increase in the IFF-01 for the 2004 fiscal year?

MS. LYN WRAY: Yes.

MR. BOB PETERS: That never came to pass?

MS. LYN WRAY: No.

MR. BOB PETERS: And why do you embed in your IFF's an assumed rate increase?

MS. LYN WRAY: It's a reasonable assumption that we would have modest rate increases to cover our costs.

Obviously we have overstated our rate requirements in the past. But nonetheless I -- I think to have a forecast with zero rate increases leads to a result in which our financial targets aren't even approached.

So for realism we -- we have some form of rate increase even beyond the years where we're asking for -- for specific rate increases.

MR. BOB PETERS: And why has your assumed rate increase in the assumption years as you've called them, that would be 2007 and beyond, why has that gone up half a percentage point to 2.5 percent?

MS. LYN WRAY: We -- we look at the impacts on our long range financial targets and if we continued with the 2 percents I -- I think the results would have been -- I can't recall them exactly but it would have been debt ratios at the end of the period that would have been higher than we felt comfortable with.

MR. BOB PETERS: Can you indicate to the Board whether the assumed rate increases in your IFF's have ever been above the rate of assumed inflation?

MS. LYN WRAY: Not to my recollection. Obviously back in the -- I think probably the 1980's we have had rate increases significantly in excess of inflation or at least very high -- very rate increases compared to what we have in the current day.

But our planning assumptions have generally had rate increases at or below the rate of inflation, on an annual basis.

MR. BOB PETERS: And we know for the last approximately eight (8) years there have been no rate increases?

MS. LYN WRAY: That's correct, so on a cumulative basis, even though you have rate increases in this forecast that are somewhat above projected inflation, certainly on a cumulative basis you're a lot less than -- than what inflation would be for that time period.

MR. BOB PETERS: That's still a difficult sell to the consumers, I suspect, when you go door-to-door to explain what's happening with their rates, they don't get much comfort out of the fact that this is cumulatively below accumulative inflation.

MS. LYN WRAY: I suppose that if -- if one was looking at public relations, the best thing to have done would have been to have had rate increases at inflation, in a steady state, for the last ten (10) years and we would be in a very strong position at that point to never go above the rate of inflation.

MR. BOB PETERS: And the -- just so we're clear, the assumed rate of inflation in your materials is 2 percent, going forward. Is that correct?

MS. LYN WRAY: Yes.
MR. BOB PETERS: All right. Moving down to the -- the line items on the IFF comparisons, dealing with extra provincial revenue, here we see a different trend and that is the -- the extra provincial forecasts in IFF-01 were about 515 million. They were about 520 million in ’02 and then in ’03 they were down to three hundred and ninety-four (394).
Do you agree with that?
MS. LYN WRAY: Yes.
MR. BOB PETERS: Can you indicate to the Board the major reasons for that assumption revision?
MS. LYN WRAY: Well in -- certainly going from IFF ’02 to ’03, we had lower export volumes due to the drought. There were also some impacts at the tail end of the forecast in terms of higher volumes because of Wuskwatim being assumed in the IFF ’03 forecast.
And there were also, as there is in all forecasts, some changes in market prices assumed.
Another factor affecting extra provincial revenues in the recent two (2) forecasts is that with higher domestic load growth, there is less to sell on the export market.
So there’s a series of puts and takes but the major two (2) would be the drought at the front end and then

Wuskwatim coming on at the tail end of the forecast.

MR. BOB PETERS: Can you indicate to the Board the -- what impact, if any, have you attributed to the drought when you're forecasting out for 2005 and 2006 under the extra provincial revenue?

MR. HAROLD SURMINSKI: Generally out in time, the forecast consists of all eighty-six (86). The consequences of all eighty-six (86) flow conditions so the consequences of severe drought are -- are built into the average.

MR. BOB PETERS: You're basically -- you're not giving any extra weight to the fact there was a drought as you move out?

MR. HAROLD SURMINSKI: No, we do not.

MR. BOB PETERS: If I could just have a minute, please.

(BRIEF PAUSE)

MR. BOB PETERS: Ms. Wray, while we're looking at this extra provincial number, I just wasn't clear as to what impact you attributed to the lower US exchange rate in your IFF?

MS. LYN WRAY: The major change, and it's a combination of the exchange rate and the drought is that in importing more power at a lower exchange rate, actually, had a benefit on the forecast in the early period.

(BRIEF PAUSE)

MR. BOB PETERS: Ms. Wray, looking to the finance expense, which is on the top of the second unnumbered page under Tab 21, it appears that overall finance expense in 2004, was initially forecast in IFF '01 to be around 494 million, it's gone up to 513 million, and then 472 million; am I correct?

MS. LYN WRAY: Yes.

MR. BOB PETERS: And if we follow out those line items, just comparing IFF '02 and '03, we see that finance expense will increase by about $494 million over the ten (10) year planning horizon?

MS. LYN WRAY: Yes, that's correct.

MR. BOB PETERS: And that would be mostly due to the capital projects that are being planned by the Corporation?

MS. LYN WRAY: Yes, in the later years. You'll see in the early years though, we actually have some favourable variances, and that's due to a combination of the lower US exchange rate and lower short term interest rates on -- on our floating debt, as well as on our longer term debt.

MR. BOB PETERS: Looking at the comparison in 2003, you don’t have the IFF-01-1 on your sheets, and I understand that, but that number was $492 million, and then it ended up in IFF-02 at $477 million.

Can you indicate to the Board what impact, if any, did the special payment to the Province have on those financing costs?

MS. LYN WRAY: Well, it went down -- the -- in that particular year, finance expense went down from the previous forecast, so there was a combination of things happening, but one (1) of them was again, lower interest rates, I believe and I think also foreign exchange impact.

MR. BOB PETERS: Just to refresh my memory, was 2003 the year in which the bulk of the special payment was made to the Province?

MS. LYN WRAY: Yeah, I think at the beginning of the year.

MR. BOB PETERS: And so the impact of that -- that payment would actually affect the 2004 fiscal year?

MS. LYN WRAY: Well, I think the -- the payment was made actually at the beginning of the 2002/03 fiscal year. So it would have affected that year. And that was the year in fact in which our finance expense went down from the previous forecast.

MR. BOB PETERS: As a result of favourable

interest rates on -- on the debt?
MS. LYN WRAY: Well, it's very hard when you look at our finance expense, to -- to say what's attributable to what. There's things moving in different directions, but on a net basis, I would think that the -- the major change was US -- partly an accounting issue with respect to US exchange, and partly interest rates.
MR. VINCE WARDEN: I might just add, we had some very favourable gains on sinking fund investments in that year as well, that we took into income.
MR. BOB PETERS: All right. Thank you for that, Mr. Warden.
On this finance expense when we see the impact over the ten (10) year planning horizon, would it be correct, Ms. Wray, that incurring the additional debt over this horizon will also impact the income statement by about the same amount?
MS. LYN WRAY: I don't really understand your question? You're saying, will the 494 million show up on the income statement? And the answer is, yes, because these are comparisons of -- of income statement items.

(BRIEF PAUSE)

MR. BOB PETERS: On the depreciation line item, there was a depreciation rate change implement, I think in April of 2002, is that correct?

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

MR. BOB PETERS: Can you explain briefly what happened then, Mr. Derksen?

MR. WILLIE DERKSEN: Periodically the company per -- has a depreciation study performed and what that does is takes a review of the company's experience in terms of retirements of its assets and recommends updated depreciation rates based upon the experience.

The result of that depreciation study was generally a reduction to depreciation rates which related to longer asset lives expected although in the earlier years there was an increase that was also reflected due to accelerating depreciation on some computer assets.

MR. BOB PETERS: So the impact from approximately April of 2002 through to April of 2006 has been about $4.7 million, Mr. Derksen? Or roughly a million dollars a year?

MR. WILLIE DERKSEN: I don't think that would be fair, a million dollars a year. I think in the early years it was up $4 million and in the later years, it's down about $4 million as a result of the depreciation study. The cumulative amount could be the amount that you're referencing.

MR. BOB PETERS: Was there anything significant that came out of that new study?
MR. WILLIE DERKSEN: Well, other than what I've indicated which is generally longer service lives expected, no.
MR. BOB PETERS: And Mr. Derksen, do you find your depreciation rates are relatively consistent with other jurisdictions? Have you -- have you looked into that?
MR. WILLIE DERKSEN: Yes, basically they are. There are some anomalies, I think, that we pointed out on motor vehicle costs but I think everything else is in line with -- with other jurisdictions.
MR. BOB PETERS: Mr. Derksen -- just a minute.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Derksen, can you confirm that the $119 million of additional depreciation expense is attributable to -- to the higher capital expenses rather than the change in depreciation rates?
MR. WILLIE DERKSEN: The main factor would be the higher capital expenditures, that's correct. The change in depreciation rates would, in fact, provide a little bit of an offset to that.
MR. BOB PETERS: In turning to the cost of

operations line item, is this the line item where the Board would expect to see productivity gains surface?

MR. WILLIE DERKSEN: It would be primarily in that line item, yes.

MR. BOB PETERS: Am I correct in looking at the document at Tab 21, Mr. Derksen, that over the forecast period the costs have increased since IFF MH 02-1 was done by about $44 million?

MR. WILLIE DERKSEN: That's the cumulative amount, yes.

MR. BOB PETERS: In the IFF-01 of '01 for the year 2004, the cost of operations was forecast at about 266 million and then we see here in Tab 22 that it shows up in IFF-02 at 303 million and is roughly 304 million in IFF-03.

Mr. Derksen, can you tell the Board what were some of the factors that gave rise to the -- to the increase from 266 million to 303 million?

MR. WILLIE DERKSEN: Yes, the main factor is the acquisition of Winnipeg Hydro which added $33 million to the operating costs. The other significant factor that has been included in here is an increase in pension and benefit costs in the order of approximately $10 million.

MR. BOB PETERS: Can you explain why the pension benefit costs went up approximately $10 million?

MR. WILLIE DERKSEN: There were a few factors that contributed to that. One of -- one of them had to do with a reduction to the discount rate that's being used to value the liability. The discount rate relates to the -- a long term borrowing rate that the company is able to achieve. As the borrowing rate and general interest rate reduces, it's appropriate to also reduce the discount rate.

Another factor has to do with some actuarial updates. I believe the mortality tables were changed since the last go around.

And lastly, there was some -- lastly there was an impact of the fund performance, the funds as many other pension funds had done, had taken a significant hit in was it 2002?

MR. BOB PETERS: Was that actuarial report, and internal report, Mr. Derksen, or was that generated externally?

MR. WILLIE DERKSEN: The actuarial recommendations are performed by an independent actuary.

(BRIEF PAUSE)

MR. BOB PETERS: Mr. Warden, one (1) of the -- one (1) of the expectations on the Corporation may be that they would find internal efficiencies to pay for the rate increases that they're otherwise asking of the Board, and that would be a reasonable expectation, would it not?

MR. VINCE WARDEN: I'm sorry, a reasonable expectation that we would find internal efficiencies to offset any rate increases that we might otherwise request?

MR. BOB PETERS: Let me -- let me reword it. Would it be a reasonable expectation that Manitoba Hydro would -- would first exhaust internal efficiencies, rather than -- before coming to the Board, seeking rate increases?

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

MR. BOB PETERS: And in the expenses in IFF-03-1, for 2004, expenses in the neighbourhood of over a billion and a half dollars. Can you explain to the Board why Manitoba Hydro couldn't find approximately a 2 percent efficiency gain there, to pay for the $28 million that you're seeking in the first year of the rate increase?

MR. VINCE WARDEN: Because we run a very lean organization, there just aren't efficiencies there, or otherwise we would have already captured them.

MR. BOB PETERS: How regularly do you review that, and how -- how do you -- how do you determine that year over year?

MR. VINCE WARDEN: We go through a very extensive budgeting process every year, and through regular reports to management, at least monthly reports to management, we -- we look at our progress towards retaining those budgets. So, we have strict internal controls that we -- we follow, to make sure that we're achieving our -- our targets.

MR. BOB PETERS: Do you keep track of internal productivity gains?

MR. VINCE WARDEN: Well, productivity gains are built into our -- into our budgeting exercise, yes. So, we generally, on a general basis, we expect productivity gains of approximately 1 percent per year to be realized, and we've been quite successful in realizing that.

MR. BOB PETERS: What does that translate to in dollars?

MR. VINCE WARDEN: Well, if we look at the operating and administrative line, and the cost of operations line, which is $304 million, according to the document, at Tab 21, 1 percent of that number would be in the range of $3 million per year productivity savings.

MR. BOB PETERS: Rather than measure it, you say you build it into your budgets?

MR. VINCE WARDEN: Well, by -- by building it into our budgets, we are in effect, ensuring that by meeting those budgets, we are realizing those productivity gains.

MR. BOB PETERS: Are you telling the Board that -- that you always meet your budgets?

MR. VINCE WARDEN: There are exceptions when we don't meet our budgets, but if -- if we don't, we certainly know the reason why, and there could be a major storm, for example, which would be totally beyond our control, and might cause us to go over budget. But even in that circumstance, where there is a major storm, we work very hard to recoup that elsewhere.

MS. LYN WRAY: If I can just add to that, that although we generally meet our budgets overall, there are sacrifices, if you will, being made by some areas to try to offset unavoidable cost overruns elsewhere.

We rarely get what we ask for in terms of when departments put together their budgets and we -- as is expressed in our materials, we go through a process at a departmental and divisional level as well, where we try to -- to remove extraneous types of needs.

But beneath the surface of the -- the overall forecast are a number of department -- departmental and divisional budgets and it -- it does require a fair amount of juggling to try to meet those targets which already have the 1 percent productivity built in.

MR. BOB PETERS: Mr. Warden or Ms. Wray, under the cost of operations line on the IFF, did Manitoba Hydro have a 1 percent per year efficiency gain in fiscal 2002/03 and 2003/04?

MR. VINCE WARDEN: As a matter of fact, I believe the productivity gains that we had built in to those forecasts were higher than the 1 percent. If I can just take -- I'll just confirm that.

Yes, in response to CAC-II-13, in fact, we do speak to the amount of productivity factors are built into -- into the forecast.

MR. ROBERT MAYER: While we're waiting, when we did the status update hearing, we actually did the issue of the -- of the savings, the synergies you were going to achieve upon the acquisition of Centra Gas.

You gave us a number of staff years, you -- equivalent something or others, we call them staff years, you people call them something else.

And you were going to save -- make some significant synergy savings as a result of reducing those number of staff years as the total combined between Centra and Hydro.

Now I understand that when you acquired Winnipeg Hydro, you also acquired the employees with a guarantee of employment and I'm assuming that results for some of the increase.

But have we lost track of those synergy savings on the staff years that we were supposed to have during -- with the acquisition of Centra, because I do seem to -- it does seem to appear that your number of -- what I will call employees, but number of staff years, seems to be going up over the past few years.

MR. VINCE WARDEN: Well I can tell you we definitely haven't lost track. As a matter of fact, we make regular reports to our -- the Manitoba Hydro Board as to our progress in attaining those synergies and I can give you some fairly rough numbers but the -- the synergies we estimated when we acquired Centra Gas were in the range of $16 million per year. That was the estimate we estimated -- that we -- at that time thought we would achieve.

We've -- to the end of this last fiscal year -- perhaps I'll back up a little bit, at the status update, we had -- we agreed there -- I think we got agreement that the amount of synergies we attained were approximately $13 million and we had $3 million left to achieve at that point in time.

According to the most recent update that we've done, we're down to $1 million and, as a matter of fact, the actual costs in Centra Gas were -- are now lower year over year than they were -- that is in '03/04 they were lower than they were in '02/03 by approximate -- approximately $1 million.

We think we've got another million dollars to find and we'll get that when we do amalgamate the billings systems.

So we're tracking those synergies very closely.

MR. ROBERT MAYER: Thank you. I -- I recognize how that Mr. Harper had a different view as to how much your actual synergy -- synergy savings were, but I'm not sure what the end result --

MR. VINCE WARDEN: Well, yes. The numbers are the numbers and we believe our numbers.

MR. BOB PETERS: Mr. Chairman, in light of the hour, perhaps this is an appropriate time to take the lunch recess and I'll start again after lunch and I'm expecting to complete this afternoon.

MR. DAVID CORMIE: Mr. Chairman, before we break for lunch I have a response to an undertaking we took on this morning with regard to our operations planning criteria. If we could provide now so that the Board may consider it over the noon hour.

THE CHAIRPERSON: Please proceed.

(BRIEF PAUSE)

THE CHAIRPERSON: This will be Manitoba Hydro Exhibit, I think we're at 18?

--- EXHIBIT NO. MH-18: Manitoba Hydro Operations Planning Criteria.

MS. PATTI RAMAGE: Yeah, 18 is my count.

THE CHAIRPERSON: 18 is it? Well thank you very much, Mr. Cormie. We will break now and just to remind everyone, I think we indicated yesterday that we would return today at -- at 1:30. Thank you.

--- Upon recessing at 12:00.
--- Upon resuming at 1:34 p.m.

THE CHAIRPERSON: Okay folks, we might as well get back to it. Mr. Peters if you're not tired out?

MR. BOB PETERS: Thank you for the concern and I'm getting there but I'm hoping that this is the home stretch. And I'm -- I think My Friends opposite are wagering heavily on that so we'll try to .

(BRIEF PAUSE)

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Warden before the lunch recess, we were talking about budgeting and cost efficiencies and you indicated to the Board that you build into your budgets some -- some reduced expenditures of savings is -- is how I think you indicated, is that correct?

MR. VINCE WARDEN: We build into the budgets productivity savings, yes, we do.

MR. BOB PETERS: And you drew the Board's attention to an interrogatory CAC/MSOS MH-II-13 which I had a chance to look at over the lunch break. And in that interrogatory the answer talks about productivity factors included in the various operating budgets and that's what you were referring to before lunch I take it?

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

MR. BOB PETERS: And the productivity factors that are built into the budgets, what I wanted to get from you, sir, was has the productivity factor materialized after the year is over when it's -- when you're able to measure the -- the forecast or the budget against the actual expenditures?

MR. VINCE WARDEN: Yes. And -- and I think alluded to that, we do check -- track that every month and as a matter of fact for 03 -- the year '03, '04 we did come in under budget so we did achieve the productivity factor we were striving for.

MR. BOB PETERS: Can you tell the Board how much under budget or what additional productivity savings you were able to embed?

MR. VINCE WARDEN: Yes, if you just give me a second I should be able to come up with that number.

(BRIEF PAUSE)

MR. VINCE WARDEN: Sorry for the delay Mr. Peters. I wanted to make sure I gave you the electricity operations only and we have both consolidated which would include all of the subsidiaries and electricity alone.

But looking at electricity alone, we came in at $283.4 million which was 20 million -- $20.2 million lower than -- than what our forecast was.

This is still somewhat preliminary and so I would like to verify those numbers but that's what I have at this time.

(BRIEF PAUSE)

MR. VINCE WARDEN: I wouldn't want to leave the impression that all that $20 million was productivity savings. There's a -- a number of factors that entered into that.

We -- I think Mr. Derksen referred earlier to the increase in the pension costs because of the performance of the pension fund in 2002/2003, that actually rebounded in

’03/’04 -- or recovered that is. And so part of that $20 million favourable variance from budget was because of the recovery in the pension performance during the year ’03/’04. So, not totally productivity.

MR. BOB PETERS: Are you going to provide a breakdown between productivity and what was related to the pension, Mr. Warden?

MR. VINCE WARDEN: Yes, I can provide a further breakdown of that. Yes.

MR. BOB PETERS: All right. I appreciate that undertaking.

--- UNDERTAKING NO. 15: Provide a breakdown between productivity and what was related to the pension.

MR. BOB PETERS: While we’re talking generally about cost control procedures, Mr. Warden. You told the Board about how you deal with it internally. Does the corporation engage any external consultants on the evaluations or suggestions for efficiency improvements?

MR. VINCE WARDEN: From time to time we do have consultants come in and look at various aspects of our business. Most recently we had Deloitte and Touche conduct a review of our risk management practices and -- and confirm that we were, in their words, leading edge for Canadian utilities.

But, as far as the overall efficiency of the -- of operating, no. And that would be fairly difficult for somebody to come in and do that without knowing our business and so I wouldn't -- I never contemplated doing that. We -- we operate differently than does Sask Power or -- or BC Hydro, Hydro Quebec. We all have our unique circumstances and to come in and do a comprehensive review, I just don't think would be cost effective for us.

MR. BOB PETERS: You don't recall that having been done then in the past?

MR. VINCE WARDEN: It hasn't been done in the past in -- in my recollection, no.

MR. BOB PETERS: Mr. Warden, that Deloitte and Touche study on risk management, is that different from the one (1) that Mr. Cormie had talked to me about?

MR. VINCE WARDEN: Yes, that is a different -- different review.

MR. BOB PETERS: How -- how recent was that done?

MR. VINCE WARDEN: That was done, I believe, February -- February/March in that time-frame.

MR. BOB PETERS: Of '04?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: Is that a document that you'd be prepared to file with the Board?

MR. VINCE WARDEN: Certainly, I could do that.

MR. BOB PETERS: Thank you for that undertaking.

--- UNDERTAKING NO. 16: Deloitte and Touche Study on Risk Management.

MR. VINCE WARDEN: Mr. Peters, not to interrupt but it -- we have a couple of items being dropped off that we want to give Exhibit numbers to them.

THE CHAIRPERSON: Certainly, Sir. I was responsible for one (1) of those documents and I think one (1) was from Ms. Ramage. Ms. Ramage, as witness, as Mr. Warden indicated before lunch that they were endeavouring to provide an -- a response to an undertaking given in respect of the forecast net loss for fiscal year ending in March 31st of 2004. And narrow the range for us.

So, I suggest we take that as Manitoba Hydro Document Number Exhibit 19.

--- EXHIBIT NO. 19: A Response to an Undertaking Given in Respect of the Forecast

Net Loss for Fiscal Year Ending in March 31st of 2004.

MR. BOB PETERS: And if we're onto it, Sir, I expect that I will be referring with this panel shortly to the other document which is really a worksheet on a comparison of payments to the Province and with your permission, I would suggest we mark that as Exhibit PUB number 9 and I'll refer that to the witnesses at that time and those are the only two (2) that I have, sir.

THE CHAIRPERSON: Thank you.

--- EXHIBIT NO. PUB-19: Worksheet showing comparison of payments to the Province.

(BRIEF PAUSE)

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Warden, now that we've marked Exhibit Manitoba Hydro 19, that contains the -- the -- the -- the narrowed range of the net loss attributable to the electrical side of the operation for the year ending March 31st, 2004.

Is that correct?

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

MR. BOB PETERS: Would I -- would I also be correct in that we're still expecting Manitoba Hydro to find out whether or not it can, in some way, shape or form, speed up a process where a more comprehensive forecast or other document can be provided to provide the actual audited results from March 31st, 2004?

MR. VINCE WARDEN: Well, no, actually I was hoping this would serve that purpose. I -- I don't expect that we'll be able to speed up the process that's provided for in the Act -- the Crown Corporation's Act. So if there's something more that you need other than this range I've provided, I guess I could investigate that further but it wasn't my intention to do that at this time.

MR. BOB PETERS: All right. Then thank you for that and maybe just leave it with us and I'll notify you and the Board and your Counsel on the record if there's anything further.

If you could, Mr. Warden, document number 22 in the book of documents that's been handed out is a PUB Manitoba Hydro First Round Question 21 and your response to it, this was operation, maintenance and administration costs by various business groups within the Corporation as I understand the document.

Have you located that?

MR. VINCE WARDEN: Yes, I have.

MR. BOB PETERS: And what this document was asked to provide was a measure of Manitoba Hydro’s actual OM&A costs by business unit and bring into the mix the Winnipeg Hydro additions as well as the additions only attributable to Manitoba Hydro and that’s what is being done here.

Am I correct?

MR. VINCE WARDEN: It is.

MR. BOB PETERS: So when I look at the president and CEO, that business group was at $15.7 million back in the year ending March of 2002 and since then there’s been about $4.2 million of additional costs in that business group, is that correct?

MR. VINCE WARDEN: I’m sorry, Mr. Peters. I -- would you just repeat the last part of that question?

MR. BOB PETERS: Yeah, let me -- let me phrase it this way: When the Board last saw Manitoba Hydro’s operating and administrative costs, those were done and forecast and now those are turned to actual and that’s the column that’s under 2001/02 Manitoba Hydro Actual?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And then in addition to that you’ve since acquired -- since appearing before the Board you’ve acquired Winnipeg Hydro and the costs that you are attributing to Winnipeg Hydro by the same business groups are then shown in the -- under the Winnipeg Hydro 2003/04 column?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And the column that's entitled, "Manitoba Hydro Changes" represents only those additions or reductions in expenditures that are related to Manitoba Hydro's operations exclusive of Winnipeg Hydro additions?

MR. VINCE WARDEN: To -- to move from the 2001/02 actual cost to -- to 2005/06 forecast, yes, that's correct.

MR. BOB PETERS: All right. Just by taking on Winnipeg Hydro, that's added $1.587 million to the president and CEO business unit of the Corporation?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And in addition to those expenditures that are added, Manitoba Hydro also had another $4.248 million dollars attributable to the same Business Unit from 2001 to 2005?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: Can you explain to the Board in general terms what that $4.2 million dollars includes?

(BRIEF PAUSE)

MR. VINCE WARDEN: Mr. Peters, Ms. Ramage has just brought to my attention the fact that there were -- there were some revisions to that response contained in -- in Tab 22. And I believe we would probably -- it would be better if we -- if we updated that document before we -- before we spoke to the numbers.

MR. BOB PETERS: All right. I wasn't going to drill down to too many of them but --

MS. PATTI RAMAGE: We have revised copies available now. As I -- I had spoken to Mr. Peters at the break, the revisions don't affect the totals but it was the numbers themselves.

So, given that we're going to -- to the numbers in the columns perhaps just so that we're working from the correct numbers that the -- the electric cost of operations totals don't change.

But for the purposes of running through this I would suggest we'll pass out the revised answer with the corrected numbers.

(BRIEF PAUSE)

MR. BOB PETERS: With Ms. Ramage's concurrence I suggest we mark this for the record as Exhibit Manitoba Hydro number 20 and recognize that it's a revised response to PUB/MH-I-21 which document is also found in the unrevised form at Tab 22 of the Document Brief that I circulated.

--- EXHIBIT NO. MH-20: Revised response to PUB/MH-I-21.

THE CHAIRPERSON: So marked.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Thank you. Mr. Derksen or Mr. Warden, just looking at Manitoba Hydro, Exhibit 20, which is the revised document, I'm wondering if you can advise the Board as to what led to the $4.793 million dollars increase under the President and CEO function of the Corporation from 2002 through to fiscal 2006.

MR. VINCE WARDEN: Sure. Part of that, of course, would just be the normal inflationary increases that would occur from year to year. In the President's account though, when we go over the budgets at -- at Executive Committee, Mr. Brennan will take the prerogative of taking -- taking into his responsibility area any unallocated amounts.

That is if the Business Units have increases that he considers are over and above what he is prepared to approve and yet the bottom line is still reasonable -- the bottom line increase overall is reasonable, he'll take a contingency amount into his area.

And that’s what happened in that particular case. He’s actually got of -- of that 4.8 million approximately 2 million is the contingency that he kind of holds in reserve for doling out for special events that might -- might occur -- occur over that time period. So that’s --

MR. BOB PETERS: All right. Thank -- thank you for that. I see the bottom line numbers didn’t change so it was just a shuffling of the numbers amongst and between the various business units that’s transpired with the revision?

MR. VINCE WARDEN: That’s right.

MR. BOB PETERS: And if I do look at the bottom line numbers, Manitoba Hydro’s O & A costs, back to fiscal ’02, were 242 million and they’ve increased by 34 million. Have I got that right? Just -- just the Manitoba Hydro ones excluding the Winnipeg Hydro ones.

MR. VINCE WARDEN: That -- that’s correct, yes.

MR. BOB PETERS: That’s roughly a 15 percent increase; would you agree, maybe subject to check?

MR. VINCE WARDEN: Yes, I agree that’s roughly a 15 percent increase.

MR. BOB PETERS: And it --

MR. VINCE WARDEN: I think though you probably -- to do that correctly, we probably should be adding Winnipeg Hydro numbers into the base and then recalculating the increase over -- because part of that increase would be attributable increases on Winnipeg Hydro base as well. So I think the increase will be something less than 15 percent.

MR. BOB PETERS: Okay, fair enough. But if inflation was the -- was the driver, than instead of a roughly 15 percent increase, that should have been closer to an 8 percent increase, should it not?

MR. VINCE WARDEN: Yeah, I agree. And there would -- there would be programs that come up during that period of time.

For example, one (1) of the new initiatives that -- that was introduced into the budgeting process during that period would have been the export marketing area which, under David Cormie, as we discussed this morning.

That area has grown somewhat as the -- the whole function of export marketing has grown over that period of time. So there would have been minimal costs included in '01/'02. Recognizing that is an important initiative for the corporation, we have devoted more resources to that area and so that cost would be included in the '05/'06 forecast.

MR. WILLIE DERKSEN: Well, Mr. Peters, we talked about the increases in pension and benefit costs and they're incorporated into here as well. So ten (10) to $12 million dollars of that increase relates to that -- those pension increases.

THE CHAIRPERSON: Are the pension increases continuing and ongoing?

MR. VINCE WARDEN: No, the 12 million dollars was -- that Mr. Derksen referred to was to recoup some of the experienced losses that we had in -- in ’02/’03 and we’ve recovered in ’03/’04. So those -- about -- of the 12 million dollars, there would be about 6 million dollars left to be recovered. And that would be reflected in the next -- in the next update to the -- to the forecast.

MR. BOB PETERS: With those comments, Mr. Derksen and -- and Mr. Warden, would you agree with me that any productivity gains that may have been realized were then usurped by either new initiatives or some other factor?

MR. VINCE WARDEN: I guess I would prefer to look at performance as opposed to what we might have in our budget. I -- I know for sure, by looking backwards, that our productivity gains have been certainly realized and we do incorporate productivity gains in the forecast going forward. We do add new initiatives and then take from -- from that, subtract any productivity gains.

Have they been usurped by new initiatives? I -- I wouldn’t like to quite express it that way. I -- I think we’re always striving for productivity gains and take great pains to achieve them.

Having said that, there are new initiatives that come along that are of benefit to the corporation as rate payers going forward and we make a business -- a business decision on those initiatives.

But having said all that, there are -- there is, as you pointed out, a net increase over that period of time that would appear on the surface not to include productivity gains but I assure you they are there.

MR. BOB PETERS: Well in terms of capitalized overheads which is an item shown on the second last line, can you explain what that item is, Mr. Derksen or Mr. Warden?

MR. WILLIE DERKSEN: Yes, capitalized overhead is the amount of overhead costs. And overhead includes primarily administrative costs such as executive and finance and also includes facilities' costs and computer costs. And this is the amount of those administrative costs that are allocated to capital activities and therefore are capitalised as part of our capital program.

MR. BOB PETERS: Does that include everything from salaries to rent and the like, Mr. Derksen?

MR. WILLIE DERKSEN: Yes, salaries, rent, depreciation, interest; those sorts of things.

MR. BOB PETERS: Why does Manitoba Hydro capitalize those as opposed to expense some of that?

MR. VINCE WARDEN: The decision as to whether or not to capitalize depends on whether there's a future benefit. So, we're striving to match costs with benefits and recover them from the ratepayers in the -- in the period in which those benefits are -- are derived.

So, capitalization does that. It moves forward costs incurred in one period to future periods to -- to match up with benefits during those periods.

MR. BOB PETERS: Is that exercise gone through for each and every item that is capitalized, Mr. Warden?

MR. VINCE WARDEN: Well, the -- the whole process of capitalization is based on a -- on certain cost drivers.

So, for example, we have activity rates associated with labour that carry a portion of overhead that is depending on the -- on the project being worked on by employees can be charged into future periods based on the rates associated with those activities.

MR. BOB PETERS: Mr. Derksen or Mr. Warden, can you explain to the Board the line item called, 'Operating and Administration Charged to Centra, $53.2 million in '01/'02 up to 56.8 in '05/'06'?

MR. WILLIE DERKSEN: Yes, the company operates in an integrated and the costs that are incurred on behalf of gas operations are charged to Centra gas and that's what that line represents.

MR. BOB PETERS: So, if the Board was to check the -- the statements from Centra Gas Manitoba Inc., this number would be carried across as the operating and administrative costs for that portion of the business?

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

MR. BOB PETERS: All right. What about corporate allocations and adjustments? This is a downward adjustment, Mr. Derksen?

MR. WILLIE DERKSEN: That line includes things like the reclassification of payroll taxes from operating expense. It’s included in our operating budgets of departments and -- and activity rate calculations but then it’s reclassified as a tax expense. So, there’s a credit in that -- in that area to remove it from operating expense to reclassify it as a tax expense.

There’s also an adjustment in there for vehicle lease rates. Vehicle costs are charged to departments on the basis of what we call a lease rate and it includes departmental costs, depreciation interest and repairs and materials, gas, insurance and those sorts of things.

And in that line is re -- what’s removed is the depreciation and interest which is reclassified again as depreciation and interest respectively. And also there would be a double-up component included in operating costs.

The vehicle -- the department that's responsible for maintaining vehicles is included in the operating costs but its charges are also included in the lease rate calculations that are charged to other departments.

Now, further in that line are general re -- unallocated reductions that we've talked about earlier. There are reductions -- unallocated synergy reductions in 2005/06 of about $3 million relating to Winnipeg Hydro and there are some other reductions relating to the new computer system implementations and some general reductions that haven't been allocated to specific departments.

Finally, in that -- in that category, there are some other costs that -- and credits, that are just not allocable to specific departments and therefore they're -- they stand alone are -- and are captioned in -- in that category.

MR. BOB PETERS: Thank you for that, Mr. Derksen, but with -- following your further -- your last answer, it appears that this corporate allocations and adjustments essentially doubled for Manitoba Hydro's operations from fiscal '02 to fiscal '06.

Would that be correct?

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

MR. BOB PETERS: What was the major driver for that or the major drivers, plural?

MR. WILLIE DERKSEN: The major driver for that is the general reductions that have increased quite significantly. In 01/02 there are no general reductions and in the forecast there are approximately, I think $8 million dollars of general reductions that will be -- are expected to be achieved but haven't been allocated to departments.

Other things that are -- that have caused the increase would be in the 2001/02 actual what's included in that fourteen million six hundred and thirty-nine thousand (14,639,000) is a charge of about $3 million dollars related to benefits costs and that debit to that charge will not be in there in 2005/06. So that causes a $3 million dollar increase to it. As well, there's a few other odds and ends like that, that cause increases.

MR. BOB PETERS: When it comes time to -- to assessing the overall impact of these operating and administrative charges, one of the things the Corporation looks at, Mr. Warden, is -- is various benchmarks. Would that be correct?

MR. VINCE WARDEN: We do look at various benchmarks, yes.

MR. BOB PETERS: And one of the benchmarks is operating and administrative costs per customer. And I believe that was referred to in previous evidence from the Panel?

MR. VINCE WARDEN: Yes, that's one of the benchmarks.

MR. BOB PETERS: And at Document 23 in the Book of Materials that has been circulated is a copy of interrogatory CAS/MSOS-MH-II-56, and is it correct to interpret that -- that in the 2002/03 year the OM & A cost per customer from Manitoba Hydro was estimated at six hundred and seven dollars ($607) per customer?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And the following year, in 2004 that amount went down to five eighty-nine (589) per customer?

MR. VINCE WARDEN: Yes. As indicated here those are in constant dollars so, yes, but I agree with that number.

MR. BOB PETERS: And would you agree with me that the -- the major event for the Corporation at that time line was the acquisition of Winnipeg Hydro?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: Would it be fair to say then that the acquisition of Winnipeg Hydro and its lower cost per customer allowed the overall average cost per customer to come down?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: Why did -- why do you believe Winnipeg Hydro was able to operate with a lower operating and administrative cost per customer than can Manitoba Hydro?

MR. VINCE WARDEN: It was primarily because of the density of the population in the City of Winnipeg so the cost to serve in are -- are proportional to the geography of that we -- we -- of the customers we serve.

MR. BOB PETERS: The -- I think it was the Canadian Electricity Association did some bench-marking also on revenues for full-time employee of the company. And just by way of reference, although it's not included in the Book of Documents, Appendix 14 found in Volume 7, had a -- had a study done; the 2002 COPE Executive Summary. Are you familiar, generally, with that, Mr. Warden?

MR. VINCE WARDEN: Yes. I'm generally familiar.

MR. BOB PETERS: Do you -- do you know whether or not Manitoba Hydro participated in that 2002 Summary?

MR. VINCE WARDEN: Yes, we've been a member of COPE for a number of years so we would have participated in that.

MR. BOB PETERS: And as I understand, the document and I thank your counsel for -- for producing it for you, with nine (9) utilities involved in the study, the revenue per full-time equivalent employee worked out to about five hundred and fifty-nine thousand dollars ($559,000) per employee.

MR. VINCE WARDEN: Do you have the reference on that?

MR. BOB PETERS: I think it might be on the Corporate overview on Page 2, if you're leafing through it.

MR. VINCE WARDEN: Okay, yes, I see that.

MR. BOB PETERS: So you'd agree that it was approximately five hundred and sixty thousand dollars ($560,000) of revenue per full-time equivalent employee?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And when Manitoba Hydro was asked in PUB-MH-II-IR-60 to find out what was the total revenue per full-time equivalent employee in Manitoba for the same year, the answer was three hundred and sixty thousand dollars ($360,000).

Will you accept that, subject to check?

MR. VINCE WARDEN: I'll accept that, subject to check, yes.

MR. BOB PETERS: So what I see here is, based on a survey of nine (9) utilities, the Canadian Electricity Association is saying that there should be approximately six

(6) -- five hundred and sixty thousand dollars ($560,000) of revenue per employee, and Manitoba Hydro is about 64 percent of that, at three hundred and sixty thousand dollars ($360,000)?

MR. VINCE WARDEN: And that's good.

MR. BOB PETERS: Okay, explain why that's good.

MR. VINCE WARDEN: Well, that means that we're charging our customers less than the other utilities are.

We're taking less revenue from our customers than the other utilities take per customer. Per -- I'm sorry, per employee.

MR. BOB PETERS: All right. My understanding and I'll have to reflect on this as well -- I thought the -- the measure here was of the revenues of the utilities, how much revenue did the utility bring in for each employee and most utilities were bringing in considerably more revenue than Manitoba Hydro, per employee.

MR. VINCE WARDEN: So if our rate increase is granted, we'll bring in more revenue per employee than we do today. And if revenue -- the Board chooses to give us more, we'll bring in more.

MR. BOB PETERS: I see, so the -- so -- so to you, the -- you're suggesting that means that the other utilities rates are the -- are the reason for that?

MR. VINCE WARDEN: Absolutely, yes.

MR. BOB PETERS: All right, we'll come to that with the other Panel then. Do you think that this average, then, from Cope is -- is not applicable to Manitoba Hydro, shouldn't be used as a measure for Manitoba Hydro?

MR. VINCE WARDEN: There actually are some good measures in COPE and others that we just simply ignore and that would be one (1) we would ignore because it's of no value to us.

MR. BOB PETERS: Is there a more appropriate target by way of a measure of revenue for a full-time employee that should be used, rather than the one (1) that COPE uses?

MR. VINCE WARDEN: No, I -- revenue per employee really is a -- not a especially relevant measure for us.

MR. BOB PETERS: Turning to Document 24 in the Brief of Documents as provided, there's a summary of the EFT positions in Manitoba Hydro and these are the equivalent full-time position analysis.

Is that correct? In Tab 24, it's a -- it's a copy of interrogatory PUB-MH-I-IR-6.

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: When we use EFT as the

acronym, what does it -- what is an equivalent full-time employee for -- for purposes of this calculation? How have you -- how's Manitoba Hydro considered that?

MR. VINCE WARDEN: The definition of an EFT depending on whether we're talking over what time period we're -- we're talking, but for a year, an annualized EFT would be nineteen hundred and sixteen (1,916) hours per year, I believe.

I'll just double check that. Nineteen sixteen (1,916) hours per year, yes, that's correct.

MR. BOB PETERS: So employees who work part time are aggregated until one thousand nine hundred and sixteen (1,916) hours and that's -- then determined to be an equivalent full time employee?

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

MR. BOB PETERS: And in terms of overtime, is overtime counted as one (1) hour equals one (1) hour, or is there a -- a doubling up on the -- on the overtime?

MR. VINCE WARDEN: There would be a -- a doubling up. Sorry, hours -- hours worked. I -- I'm sorry. It's hours worked, so it doesn't really matter what the compensation is per hour.

MR. BOB PETERS: The compensation may be double but the hour is still the same.

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

MR. BOB PETERS: All right. And what I see in here is that it would be fair to say that the EFTs by business unit increase every year presumably from 2002 up to 2005?

MR. VINCE WARDEN: Yes, it appears that every business unit has an increase over that time period. Yes.

MR. BOB PETERS: There was another interrogatory that's not produced here but it had to do with the suggestion that Manitoba Hydro has a one (1) to 2 percent decrease in salary budgets per year.

MR. VINCE WARDEN: I believe that was referring to the -- the productivity that's built into the budgets, yes.

MR. BOB PETERS: Ye -- yes. Recognizing that interrogatory and I have a marginal note here it was PUB Manitoba Hydro First Round 11-C where I saw that.

Can you explain to the Board how your salary budgets can decrease every year but your EFTs actually increase?

(BRIEF PAUSE)

MR. VINCE WARDEN: Well, wh -- I think, just to explain that a little bit more, we would take our salary budgets in 2001/02, for example, as indicated in this -- under this tab, add on the EFT changes that have been justified through the budgeting process, factor in the wage and salary increases that would have occurred over that period of time applicable to that higher number of EFTs. From that number, deduct a productivity increase.

Oh, the -- the re -- the calculation of the productivity increase would be netted against what the cost would otherwise be based on the number of EFTs that have been approved for that particular budget year.

MR. BOB PETERS: All right. So it’s not -- the budget reduction is done after you’ve assumed the position has been added?

MR. VINCE WARDEN: Yes, that’s -- that’s correct.

MR. BOB PETERS: And in light of the fact that the Corporation has had a difficult financial year in 2004, is there a hiring freeze on at Manitoba Hydro?

MR. VINCE WARDEN: Well, any -- any new hires from outside the Corporation require the approval of the president and CEO. So it’s not an absolute freeze.

If we can convince the president that the position is needed and sometimes there are those situations where we absolutely do have to have people, then it would be added.

MR. BOB PETERS: All right. I don't want to go through this --

MR. ROBERT MAYER: About --

MR. BOB PETERS: -- chart in --

MR. ROBERT MAYER: -- did I hear you correctly that every deplacement employee that you would bring in from outside has to be approved by the president and the CEO?

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

MR. ROBERT MAYER: So you've got to hire -- a lineman retires, you've got to replace a lineman, you've got to go to the president and CEO to get --

MR. VINCE WARDEN: Well --

MR. ROBERT MAYER: -- approval?

MR. VINCE WARDEN: -- we would -- that isn't quite the way it works. We -- we'd train the line tradespeople from within organization. So, we have a trainee program that is -- where -- whereby trainees are brought in each and every year. The president would approve a trainee program. So we would be adding, at the input level every year, there would be new trainees coming into the system --

MR. ROBERT MAYER: But then you'd --

MR. VINCE WARDEN: So, when --

MR. ROBERT MAYER: -- have to --

MR. VINCE WARDEN: -- so when a lineman retires, ultimately we have somebody from within that's trained to -- to replace that lineman.

MR. ROBERT MAYER: So, you wouldn't have to go to the president and CEO to bring in the new train -- trainee?

MR. VINCE WARDEN: No, but the trainee typically wouldn't be brought in on a one off basis. We bring in trainees each year and the president is -- is aware of that program, approves that program.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Just two (2) specific line items under the various business groups that I want to discuss with you further, Mr. Warden.

You'd mentioned that under power sales, I think you were saying you were adding -- adding people in the power sales recognizing the export marketing area had grown.

Is that correct?

MR. VINCE WARDEN: Yes, I used that as -- as an example of where growth was justified and where growth is justified and a business case can be made, people will be added in those particular areas.

MR. BOB PETERS: And I see that twenty-four (24) people were added under the power sales and operations line, is that what you're referring to?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And a total of eighty-one (81) people now in the power sales field?

MR. VINCE WARDEN: That's the forecast for '04/'05 yes.

MR. BOB PETERS: And those are people who are involved in export marketing and power sales?

MR. VINCE WARDEN: That's correct.

MR. BOB PETERS: All eighty-one (81) of them?

MR. DAVID CORMIE: No, that's -- not all eighty-one (81). There are -- we have about fifteen (15) people who are involved in the sales and marketing area. In addition to those people, there are the water resource planners, the back office function for billing and energy accounting, our hydraulic engineering and operations department.

And I think that's and -- and we have a technical services section in there. But only a -- a portion of -- of the eighty-one people are -- are directly involved in the marketing.

MR. BOB PETERS: Are all of the employees in your area reflected in that eighty-one (81) number?

MR. DAVID CORMIE: Those eighty-one (81) people report to me, yes.

In 2001/2002, Manitoba Hydro had contracted out a portion of its real time trading function. We brought that function back into Manitoba Hydro since that time and -- and have -- are now fully providing that service to Manitoba Hydro where for a period of time that had been contracted out.

MR. BOB PETERS: Are all twenty-four (24) additional employees under the power sales and operations related to export activities?

MR. DAVID CORMIE: I believe there are some of those numbers in the water resource management group and the hydraulic engineering and operations group.

MR. BOB PETERS: I -- I'm not sure if that answer -- if I understand that -- you're saying that of those twenty-four (24) how many are -- are there as a result of the -- their efforts in the export marketing area?

MR. DAVID CORMIE: I -- I believe the majority is -- are.

MR. BOB PETERS: Just one another line item here and -- under finance and administration, Mr. Warden, it looks like Mr. Wien's group has taken a hit of fourteen (14) under the rates and regulatory affairs group. Can you explain to the Board what's happened there?

MR. VINCE WARDEN: We decided he had too many people. Oh, there was a bit of an internal reorganization whereby rates and regulatory affairs was split between treasury and business analysis and Ms. Wray moved from the rates and regulatory affairs area into treasury and there was a re-allocation of positions between those two (2) areas.

So, there's largely an offset between rates and regulatory affairs and business in -- treasury and business analysis.

MR. BOB PETERS: All right. What I'm hearing then is that the fourteen (14) people who were moved out rates and regulatory affairs and they are found somewhere else on that page as additions?

MR. VINCE WARDEN: That's right.

MR. WILLIE DERKSEN: Mr. Peters, there are a number of adjustments like that, that are included in this column so all of the net changes in divisions in Manitoba Hydro are included in that one column. So any -- any place where reorganization occurs that same situation will happen.

MR. BOB PETERS: Mr. Derksen or Mr. Warden, is the increase of thirty-three (33) EFT's on the information technology service related to new billing systems?

MR. VINCE WARDEN: Yes, the -- the large portion of it would be. There's also a new geographical information system that's being implemented at Manitoba Hydro that has added some people.

So, new systems basically is driving that number and transfers from other areas has -- some transfers from other areas has also incurred as well.

MR. BOB PETERS: And Aboriginal relations are -- have grown by twenty-one (21) EFT's, almost doubling the department -- that are doubling the group, to what is that attributed?

MR. VINCE WARDEN: Well similar to the export marketing area, this is a new initiative of Manitoba Hydro to place more emphasis on the aboriginal relations areas.

As a matter of fact, since this was prepared, this document was prepared, there's a new vice-president of Aboriginal Relations, actually referred to as "Corporate Relations", but a new business unit has been formed with that group transferred into it.

MR. BOB PETERS: Do you know, Mr. Warden, when Winnipeg Hydro was acquired, it appears that their employees on generation south as a category, there was eighty-seven (87) of them and can you explain, briefly, what -- what's encompassed by that to the ...

MR. VINCE WARDEN: Well, I believe that would be primarily the people on Winnipeg River system operating the plants at Pointe and Slave, Pointe du Bois and Slave -- Slave Falls, so that would be the -- the bulk of the people there.

MR. ROBERT MAYER: Don't leave that line, Mr. Peters. You've got -- before you acquire Winnipeg Hydro, you've got two hundred and thirty-nine (239) bodies generation north, four hundred and fourteen (414) generation south.

We consider everything north of the 53rd parallel as north, therefore about 70 percent, I guess, of your hydro-electric power is generated north.

How come you got so many generation south people?

MR. VINCE WARDEN: I'll let Mr. Cormie answer that.

MR. DAVID CORMIE: Mr. Mayer, although most of our electricity's generated in the north, they're generated at the three (3) Nelson River generating stations where you have thirty-two (32) units.

Manitoba Hydro has a hundred and thirty-two (132) generating units, so the -- we have may -- way more generating units in southern Manitoba, producing a lot less electricity than we have in the north.

And it's just a matter of scale.

MR. ROBERT MAYER: Following from that, under what possible circumstance could Winnipeg Hydro have had three (3) people in generation north? That is what it says, isn't it?

MR. VINCE WARDEN: Well, I think that what that says is that that's where they ended -- the -- these are people that were acquired from Winnipeg Hydro and they were allocated to these -- these respective areas, so they were allocated to generation north.

MR. ROBERT MAYER: Thank you, that was a little confusing.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Mr. Warden, I understood from one (1) of your previous answers that the -- the cost per customer at Winnipeg Hydro was lower than it is at Manitoba Hydro to which you attributed that to the -- to geography?

MR. VINCE WARDEN: That was my answer, yes.

MR. BOB PETERS: And would you agree that by bringing Winnipeg Hydro on board, then, and to keep those efficiencies that Winnipeg Hydro had, that the cost per customer for Manitoba Hydro's customers now should be reduced from six hundred dollars ($600) to something lower than that?

MR. VINCE WARDEN: And it has, yes.

MR. BOB PETERS: And what is the new number?

MR. VINCE WARDEN: The number we're tracking now is five hundred and eighty-four dollars ($584) per customer.

MR. BOB PETERS: How was that arrived at, generally?

MR. VINCE WARDEN: Well, it's simply taking the -- the new budget amount for operating, maintenance, administration and dividing it by the number -- total number of customers.

(BRIEF PAUSE)

THE CHAIRPERSON: Mr. -- Mr. Warden. Looking at the various departments, are any of these departments there totally capitalized?

THE WITNESS: Yes, the transmission construction. Well, actually no, sorry, I'll have to back up that.

Distribution construction would be the -- the one (1) that would be virtually 100 percent capital. To a lesser extent, transmission construction, line maintenance. There is a line maintenance component of that -- in that group.

But the TND (phonetic) area would have the largest component of -- of capitalization across the corporation.

THE CHAIRPERSON: Thank you.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: If I could turn with you, Mr. Warden, to Tab 25 of the Book of Documents, it contains a number of interrogatory responses dealing with Manitoba Hydro's payments to the Province and that includes PUB Manitoba Hydro First Round 20-A, B, C and D.

Do you have that?

MR. VINCE WARDEN: I do.

MR. BOB PETERS: And this chart just provides information to the Board to demonstrate the expenditures that Manitoba Hydro makes annually since 2002 and forecast to 2006 to the Province of Manitoba?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: This includes all of the ones that you're aware of?

MR. VINCE WARDEN: Ye --

MR. BOB PETERS: All of the expenditures?

MR. VINCE WARDEN: Yes, it does.

MR. BOB PETERS: And has Corporation's capital tax been payable -- when did that first become payable, do you recall? Has it been a long time payment or is it relatively current?

MR. VINCE WARDEN: It's relatively current. I believe it was the mid-90s it would have -- '96, I'm informed, that it was introduced.

MR. BOB PETERS: It's a tax that's calculated on the assets of the Corporation?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And that includes also, on deferred assets it's a tax?

MR. WILLIE DERKSEN: I think that it excludes some component of deferred assets in its calculation.

MR. BOB PETERS: It excludes some but includes most?

MR. VINCE WARDEN: Yes, I believe that would be correct.

MR. BOB PETERS: The water rental fees that are paid to the Province is a rate that is determined solely by the Province?

MR. VINCE WARDEN: Yes, it is.

MR. BOB PETERS: And on PUB Manitoba Hydro First Round 20-D, which is the last piece of paper under Tab 25, there's a schedule that shows how the water rental rate calculation has changed. And the -- the notable change on that schedule is that that rate changed in fiscal 2002 and it is now at three point three four one (3.341) per megawatt hour?

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

MR. BOB PETERS: And that's on domestic as well as exported --

MR. VINCE WARDEN: It is.

MR. BOB PETERS: -- production?

MR. VINCE WARDEN: It is.

(BRIEF PAUSE)

MR. BOB PETERS: If I read that interrogatory Part D correctly then, Mr. Warden, with the increase in rates the water rental actual payment went up from $50 million dollars to approximately $107 million dollars that year?

MR. VINCE WARDEN: Yes. There -- there's a fair bit of background to that rate. I'm not sure whether you want me to get into that or not. The water rental rate was frozen by the Province for a number of years in exchange for which the Manitoba Hydro made payments on the Province's behalf for certain mitigation works in northern Manitoba.

So there is a reason why it jumped as suddenly as it did. That freeze ended at March 31st, 2001.

MR. BOB PETERS: Thank you for that. On the debt guarantee fee -- this is the -- the payment of the Province because the Province, in fact, guarantees the debt of Manitoba Hydro?

MR. VINCE WARDEN: That's right.

MR. BOB PETERS: And we see also on Part D of the Information Request found at Tab 25 that the debt guarantee fee has also changed over time?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: And it presently stands at decimel nine five (.95) of a percentage point on every dollar of debt of the Corporation?

MR. VINCE WARDEN: That's correct, there's an exception for Manitoba Hydro mitigation bonds but essentially all of the debt of Manitoba Hydro, yes.

MR. BOB PETERS: From that last answer, is there a reduced rate on the mitigation bonds or is it -- is it zero (0)?

MR. VINCE WARDEN: It's zero (0).

MR. BOB PETERS: On the sinking fund administration fee, can you briefly explain what that charge is for?

MR. VINCE WARDEN: Well, the Province manages the sinking fund on behalf of -- of Manitoba Hydro, manages the investments in that fund and that -- for that they charge a fee of .075 percent.

MR. BOB PETERS: You've included in this response on -- Part A, the special payment to the Province, Mr. Warden. And that came about by way of legislation back in approximately 2002 and 2003?

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

MR. BOB PETERS: Am I correct that the amount was initially forecast to be larger than the $204 million shown on this schedule?

MR. VINCE WARDEN: Yes, it was originally forecast to be $288 million. It was dependent on earnings on each of the years, ’02/’03 and ’03/’04.

MR. BOB PETERS: So, in the ’03/’04 year, the -- the payment to the Province under this category was reduced because of the -- the lower net income of the Corporation?

MR. VINCE WARDEN: That’s right.

MR. ROBERT MAYER: Lower net income is an interesting concept. I thought we had a negative net income?

MR. VINCE WARDEN: We -- we did. Yes. Actually, what -- what is shown on this schedule, the payment -- it -- that’s when the cash payment was made but it was actually applicable to the earnings of ’02/’03.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: And likewise that -- that’s shown under Column ’02/’03, was attributable to the prior year?

MR. VINCE WARDEN: No. It was the -- the 204 million. It was actually 203.5 million was all attributable to the fiscal year ’02/’03.

MR. ROBERT MAYERS: And that number represented, as I understand it, a certain percentage of net export. I thought it was net export revenue, not net revenue.

MR. VINCE WARDEN: It was net revenue.

CONTINUED BY MR. BOB PETERS:

MR. BOB PETERS: Do you recall, Mr. Warden, was it 75 percent of -- up to a maximum of 75 percent?

MR. VINCE WARDEN: It was a maximum of 75 percent of net income, yes.

MR. BOB PETERS: Mr. Warden, on PUB-MH-I-IR-20(b), which is the second page found under Tab 25, the Corporation has shown that the -- the payments to the Province are in and around the 15 percent of gross revenue per year. But for that -- the one (1) year in which the special payment was made.

Is that correct?

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

MR. BOB PETERS: And for planning purposes, does Manitoba Hydro incorporate roughly that same percentage in their IFF's going forward each and every year? Or do you have any contingency built in for further payments to the Province?

MR. VINCE WARDEN: We have no contingency built in for any further payments. It's not really based on a percent of gross revenue though. We forecast -- forecast each of the payments to the Province individually.

So water rentals, for example, would be based on our -- our expectation of generation in that year.

MR. BOB PETERS: And from -- from the information in the filing, Manitoba is not alone in terms of payments to the shareholder or the government in the Province in which the utility is located because you provided evidence that BC Hydro and Hydro Quebec, likewise, make those payments to the Province -- to their provinces?

MR. VINCE WARDEN: Yes, and certainly BC Hydro, Manitoba Hydro, Hydro Quebec, we're not alone in that. Other provinces do the same thing. SaskPower, Nova Scotia, New Brunswick. It's -- it's fairly typical across Canada for utilities to make payments to -- to the Province.

MR. BOB PETERS: When the -- just for the purposes of the record, PUB Exhibit 9 was a document circulated today as a worksheet that we've marked that has comparison information between Manitoba Hydro, BC Hydro and Hydro Quebec; and I appreciate, Mr. Warden, you and your colleagues haven't had an opportunity to study it in any depth.

But if you assume the numbers are calculated correctly from the information provided in the filing, including PUB-MH-II-IR-51 and also some information found at CCEP-MH-I-IR-3(b), Manitoba Hydro is compared to the other provinces based on total payments as a percentage of total revenue.

Have you charted Manitoba Hydro's payments to the Province on that basis against other utilities?

MS. LYN WRAY: Mr. Peters, we did so, to answer this interrogatory and I suppose as a matter of general practice we try to keep tabs on what's happening in other provinces.

But there's one (1) number that we could add to the table for Hydro Quebec to make it more comparable to the other two (2).

At the time, I think we answered some of the interrogatories. We didn't have the 2003 numbers for their payments and that first number, total payments, over total revenue for 2003, would be 15.42 percent.

So, if you're comparing apples to apples, I suppose you would be looking at the 2001/2002 and 2003 numbers for Hydro Quebec.

MR. BOB PETERS: Can you complete the table then, Ms. Wray, in terms of total payments divided by total assets for 2003 for Hydro Quebec or did you not do that?

MS. LYN WRAY: Yes, it's 3.09 percent. And then for total payments over net income for Hydro Quebec 2003, it would be 91.25 percent.

And total payments in dollar terms for Hydro Quebec 2003, one seven six two (1,762).

Some of that information was provided in I think PUB-II-IR-51 but it -- not the payments part.

MR. BOB PETERS: Yes, thank you for that update, Ms. Wray.

Looking at it as you have then, Ms. Wray, is there is any position of the Corporation as to whether Manitoba Hydro is in line, out of line, about the same as others?

Or what's the conclusion the utility reaches?

MS. LYN WRAY: Well, certainly looking at these numbers and our projections for 2004, 2005 and 2006, we're very much in line with BC Hydro and Hydro Quebec in being around that 15 percent mark -- fifteen (15) -- actually, we are a little bit less than BC Hydro and Hydro Quebec.

So the one (1) different year was 2002/3 in which there was the special payment which amounted to about half of the extraordinary $400 million plus net export revenue that we earned in that year.

MR. BOB PETERS: Ms. Wray, the -- the payments to BC Hydro and Hydro -- I'm sorry, the payments made by BC Hydro and Hydro Quebec to their Provincial Governments, those include express government dividends.

Is that correct?

MS. LYN WRAY: Yes, in both cases.

MR. BOB PETERS: And in -- in light of that, does Manitoba Hydro have a position as to whether or not discrete and identified government dividends is -- is supported or not supported by the utility rather than, or in substitution to other levies?

MR. VINCE WARDEN: I think it's important from Manitoba Hydro's perspective that payments to government are reasonably predictable.

We don't like to be surprised because, obviously, it distorts the planning processes at Manitoba Hydro and -- would -- would prefer that we know in advance so we can plan for it over the long term and -- and build that into our -- into our rates.

MR. BOB PETERS: And -- and that's, in fact, what you do then, with the way they presently calculate the payments to the government, Mr. Warden?

MR. VINCE WARDEN: Yes, with one (1) exception that we've -- we've talked about before. Of course the -- the one (1) special -- in fact, we've labelled it a special payment, because we don't expect it to recur.

While we're on some of the expenditures, Mr. Warden, the materials appear to show that Manitoba Hydro has a number of affiliated or related companies.

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

MR. BOB PETERS: Can you tell this Board generally why Manitoba Hydro would take equity positions or have interests in -- buy interests in affiliated companies?

(BRIEF PAUSE)

MR. VINCE WARDEN: Well, there are a number of reason -- reasons, and it depends on the company what those reasons might be.

For example, the utility -- the meter reading company we refer to as "Manitoba Hydro Utility Services" was set up initially as a joint venture with Centra Gas before Centra Gas was acquired by Manitoba Hydro.

It was viewed, at that time, to be an efficient way of -- of providing that service back to the utilities and is proven to be -- very much to be the case.

So, that utility was set up for purposes of -- primarily for purposes of reading meters. And we have chosen to leave it as a separate subsidiary even after the acquisition of Centra Gas because it -- it is providing that service back to the utility in a very efficient manner.

Manitoba Hydro International is a subsidiary that was established a number of years ago to provide services to other utilities around the world and has also been quite successful.

And we do that, not so much for generating revenue, although it does produce a -- a modest amount of revenue, but it’s more to expose employees to experiences in other jurisdictions and to provide expertise to developing countries.

MR. BOB PETERS: Just -- if I can interrupt you. At Tab 25 of the -- I'm sorry, at Tab 26 of the book of documents that's been prepared, there's a copy of response PUB-MH-II-IR-44(a), and this is where you list, Mr. Warden, the various related companies in which you have either a partial or a wholly-owned interest.

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

MR. BOB PETERS: And can you tell this Board, how Manitoba Hydro provides service to these companies and -- and how does it charge them?

MR. VINCE WARDEN: Well, each of the subsidiaries, for the most part, has employees that are seconded from Manitoba Hydro. So there would be employees that are dedicated to each of the subsidiaries primarily on a secondment basis. And any -- any services that are provided to those subs are -- are costed out based on the -- on the services that are provided.

So the employees would -- the wages and salaries of those employees that are seconded there would be borne by -- by the -- or supported by the revenues generated within those subsidiaries. So the expenses are charged directly to the subsidiaries.

MR. BOB PETERS: If I can interrupt you

there, Mr. Warden, this method of allocation of the costs to the subsidiaries is done the same for these subsidiaries as Manitoba Hydro does it to Centra Gas Manitoba Inc.?

MR. VINCE WARDEN: There are -- there are some differences. For example, in -- in Manitoba Hydro Utility Services, there -- the -- the employees there are for the most part dedicated and hired by that subsidiary and therefore there's no allocation from -- from Manitoba Hydro back. So they're not integrated, they're stand-alone.

The -- the reason that we allocate costs the way we do to -- to Centra Gas is because the operations are totally integrated. But for those stand-alone subsidiaries, they -- they're -- that isn't the case and therefore the costs are incurred and self-contained within the -- within the subs.

MR. BOB PETERS: Well, if an employee of Manitoba Hydro does one (1) hour of work for one (1) of these affiliated companies, is that one (1) hour labour charge, plus overheads, allocated back to the affiliate?

MR. VINCE WARDEN: That isn't typically how work is done for the subsidiaries. Normally, the employees would be dedicated for an extended period of time and their -- and their wages and salaries would be transferred over to that subsidiary. So, there isn't a transfer back and forth of services as there is between Manitoba Hydro and Centra

Gas.

MR. BOB PETERS: Does Manitoba Hydro inject equity on an annual basis into any of these companies?

MR. VINCE WARDEN: Depending on the circumstances. But for the most part, no. They're -- they're stand-alone and -- and don't require infuse -- infusions of equity.

MR. BOB PETERS: What would be an example of where Manitoba Hydro determines it's going to inject equity into these affiliated companies?

MR. VINCE WARDEN: Well, of all the subsidiaries we have, probably Meridian Power is the one (1) that's been struggling the most.

And there have been advances to Meridian to keep it solvent and it's -- there's a point at which we're going to -- we would probably decide that we will not do that any longer. Or, hopefully, more positively, that is, it will start to generate sufficient revenues to carry it's costs.

MR. BOB PETERS: Do you inject it into that company, Meridian Power, as by way of debt or is by way of equity?

MR. VINCE WARDEN: There has been both. There's -- there have been advances -- working fund advances to Meridian as well as start up equity.

MR. BOB PETERS: And when it comes time for accounting for -- for these affiliated companies, Mr. Warden, Manitoba Hydro is using money it receives from ratepayers within Manitoba to pay money over to these affiliated companies?

MR. VINCE WARDEN: Well, that's true except that the amounts we're tal -- talking are relatively small and on an overall basis, the -- the subsidiaries were profitable or are profitable. Last year, for example, they netted about three hundred and seventy-five thousand dollars ($375,000) on a consolidated basis which was to the benefit of ratepayers and Manitoba Hydro.

MR. BOB PETERS: What happens in the years where the consolidated efforts of all of these affiliated companies is on the negative side of the -- of the line?

MR. VINCE WARDEN: Well, like I say, it's relatively small and it could go either way but for the most part, there's a -- there's a benefit -- there has been a benefit in recent years.

And, again, if I look at a company like Manitoba Hydro Utility Services we're only looking at the revenue expense generated by that company.

If we were to provide those meter reading services within Manitoba Hydro, the costs would be higher than they are within the subsidiary and therefore, there's a benefit there that's -- that's not measured in the three hundred and seventy-five thousand dollar ($375,000) number that I provided to you previously.

MS. LYN WRAY: Mr. Peters, I believe in their IFF taking all of the subsidiaries over that period, they're positive by a small amount in every year.

MR. BOB PETERS: I apol --

MS. LYN WRAY: In terms of net income.

MR. BOB PETERS: -- I apolgize, Ms. Wray, I was -- I distracted myself.

MS. LYN WRAY: Sorry, I was just saying that in terms of our upcoming IFF-03 net income overall for all of the subsidiaries is positive by a small amount in every year -- projected to be positive.

MR. BOB PETERS: Right. That's built into IFF 03-1 that's before the Board now?

MS. LYN WRAY: Yes, that's right, including the two (2) test years.

MR. ROBERT MAYER: Mr. Warden, while we're waiting, I'm looking at this Tab 26. I'm showing -- I'm seeing 12345 Delaware Inc. and on the first page it says it holds US equity interests. On the next page it says:

"Manitoba Hydro does not provide services to 12345 Delaware. An advance was made by Manitoba Hydro to 12345 in January for nine (9)..."

I'm assuming that's nineteen thousand nine hundred and ninety-nine dollars ($19,999).

"12345 Delaware does not have any employees and does not occupy any premises."

You've got twenty-nine (29) -- thirty two (32) is -- I'm assuming that's thousand dollars or twenty-six thousand dollars ($26,000) owed to Manitoba Hydro from that company.

I'm having trouble following this. If it was set up to hold US equity interest, what US equity interest does it hold and what did it use the nineteen thousand nine hundred and ninety-nine dollars ($19,999) for?

I realize it's small potatoes but that really is hard to understand.

MR. VINCE WARDEN: Well, 12345 Delaware was set up as a shell company to -- to -- for -- mainly for tax purposes should we do business in -- in the US. We actually -- and -- and most of those costs are just the costs of setting up the company, legal fees asso -- associated with setting up the company, however, we also bought some shares in Xcel Energy and just so we can keep track of what's going on in that company.

MR. ROBERT MAYER: The other one, Meridian Power Inc., distribution in Canada of Written Pole Motors?

MR. VINCE WARDEN: Written Pole Motor is -- is a trademark associated with a special type of motor that is being marketed by Meridian power and has a lot of potential to reduce costs in those areas that are not served with three (3) phase power.

So, this mo -- motor can operate on single phase power, has a lot of application in areas like where there's remote locations that doesn't have three (3) phase for irrigation, for example.

They've had some problems in the past because of their supplier in the US has had some financial difficulties which are -- we understand, are now resolved and the supply problem should be resolved. And this company, we're expecting will move into profitability.

MR. ROBERT MAYER: Is that spelled correctly? Written?

MR. VINCE WARDEN: Written? Yes. W-R-I-T-T-E-N, Written Pole Motor. Yes.

CONTINUED BY BOB PETERS:

MR. BOB PETERS: Just so that Mr. Cormie and Mr. Surminski can think these discussions about the IFF's don't -- don't involve them. I want to bring them back on the last point.

I was looking over the break at the extra-provincial revenues. And I'd like you to turn back, if you would, to -- to Tab 21 of the book of documents.

Tab 21 was a comparison, gentlemen, of the IFF-02-1 to IFF-03-1, if you've been following, which I'm sure you have.

And if you could -- if you could come down to the extra-provincial review which is in approximately the middle of the page. I understand that the extra-provincial revenue reduction under the year 2004, relates to the -- to the drought we've been through. And that's what you would subscribe -- ascribe that to as well. Is that correct?

MR. DAVID CORMIE: Yes, that's correct.

MR. BOB PETERS: And then moving on, Mr. Cormie, I understood that when you prepare the IFF's, such as for 2005, that year you would be using -- I think it was median flows, if I understood before. Because it's the -- the second year out, you'd be using a median flow analysis for that year?

MR. DAVID CORMIE: Yes, that's correct.

MR. BOB PETERS: And, there's no drought assumption then in that year because the median flow takes into account all of the possible eighty-six (86) years of water flows that could possibly be encountered again, if history repeats itself.

MR. DAVID CORMIE: That -- that is correct. Under median flows we expect to have more -- greater surplus then we would have under the weighted average conditions. So there will be an affect on extra-provincial revenue.

MR. BOB PETERS: Generally, coming off of a drought year, to a median flow year, would be -- should produce pretty good news, correct?

MR. DAVID CORMIE: There -- there may be some minor carry-over effects not associated with in-flows, but associated with storage effects. And I believe in the median flow year, in -- in the second year of IFF-03 we were -- we were capturing some of those.

MR. BOB PETERS: Is that to what you attribute the 40 million dollar reduction in forecast of extra-provincial revenues in 2005?

(BRIEF PAUSE)

MR. DAVID CORMIE: There are various factors that contribute to the variation; the difference that you pointed out having to do with median flows versus weighted average flows.

There's also the issue that we update our export market price forecasts as well. That will have an affect.

And the third factor is there will be changes due to the change in the Manitoba load forecast that will have an affect.

The net of those three (3) will be the reduction shown.

MS. LYN WRAY: I would add to that also, in -- the lower US exchange rate for the portion that's not hedged.

MR. BOB PETERS: And those are the factors then for the 2005 years on the forecasts?

MR. DAVID CORMIE: Those are the majority of the factors, yes.

MR. BOB PETERS: And when I look forward, and I don't want to go line -- or year by year, but as I look to 2006 through '07, '08, '09, 2010, I see that what you were forecasting a year ago is now down throughout all of that period of time. Do you agree?

MR. DAVID CORMIE: Yes, that is correct. But if you look back up to the change on general consumer revenue, you can also see that is up. That's an off-set due to the increase in domestic sales. And that probably explains the majority of that variation.

MR. BOB PETERS: Not totally off-set, but partially off-set you --

MR. DAVID CORMIE: That's correct.

MR. BOB PETERS: All right. So, instead of having it available for export you're selling it to your domestic customers, is what you're telling the Board?

MR. DAVID CORMIE: Yes, and -- and generally we receive a greater rate of return by selling it into the export market than if we were to sell a megawatt hour to our domestic load.

MR. BOB PETERS: Has there been a revision to the forecasted cost -- I'm sorry, the forecasted price to be received on the export market that's been downward that would also contribute to some of this revenue reduction?

MR. DAVID CORMIE: On an annual basis, we update our forward price view and that would be reflected in that change as well.

MR. BOB PETERS: Is that adjustment you're talking about in these years upward or downwards in terms of additional revenues?

(BRIEF PAUSE)

MR. HAROLD SURMINSKI: Generally our export price forecast have been increasing over time, so I'd have to check, but I would assume that -- that our forecast had increased from the '02 to the '03 IFF.

So, it's other factors that are causing the -- the dec -- overall decrease.

MR. BOB PETERS: All right. Can you be more specific then. If we rule out your group, Mr. Surminski that you've been forecasting higher export prices what would be the factors then that would, in addition to the additional domestic consumption, be the reasons for the decline in the export revenue projections?

MR. VINCE WARDEN: The -- the exchange rate as -- as Ms. Wray pointed out, would also contribute to that reduction. So, a stronger Canadian dollar will translate into lower extra-provincial revenues.

MR. BOB PETERS: Mr. Chairman, in light of the hour, this might be an opportune time for a short afternoon recess and on our return, I would like to just finish the last area I have for this witness Panel on the area of their balance sheet and that should probably take the balance of the afternoon, but I'll...

THE CHAIRPERSON: Will ten (10) minutes do you?

MR. BOB PETERS: It's fine by me.

THE CHAIRPERSON: Okay, ten (10) minutes.

--- Upon recessing at 3:02 p.m.
--- Upon resuming at 3:18 p.m.

THE CHAIRPERSON: Okay, we're back to it Mr. Peters and we have your undertaking that you will be done at

four (4), correct?
MR. BOB PETERS: Well --
THE CHAIRPERSON: And the intervenor -- and the intervenors could look forward to a good launch on Monday morning.
MR. BOB PETERS: All right. I'll -- I'll embark on getting there quickly. I should note that Manitoba Hydro has filed and with my colleague's permission I'll ask that the Board as Manitoba Hydro Exhibit 21, Manitoba Hydro's Undertaking number 14 which deals with import and export of power, Approval Authority for Transactions and related agreement.
THE CHAIRPERSON: So noted.
MR. BOB PETERS: I have it as number 21 and My Colleague and I are all ready fighting so I -- I think we can sort that out when it's not -- when I'm not on the clock.

--- EXHIBIT NO. MH-21: Manitoba Hydro's Undertaking No. 14.

CONTINUED BY MR. BOB PETERS:
MR. BOB PETERS: Ms. -- Ms. Wray -- Ms. Wray, before the break, Mr. Warden was saying that the foreign exchange rate does play a role in the diminishing returns of extra-provincial revenue that I draw -- I drew to the attention of the witnesses before the break. You agree

with that?

MS. LYN WRAY: Yes.

MR. BOB PETERS: And I recall in one of the sensitivity analysis that was run by you that -- that's found in Tab 15 of the materials, that you ran a sensitivity on page -- let me give the proper citation, it's Tab 15 of the Book of Documents that I handed out -- it's Manitoba Hydro -- sorry, it's MIPUG/MH-I-3-B and page 17 of 19 shows the Canadian dollar going up five (5) cents US as an indication as to what would happen on the forecast if the Canadian dollar strengthened, correct?

MS. LYN WRAY: Yes.

MR. BOB PETERS: And what would happen -- can -- can you tell the Board at least generally what would happen if the Canadian dollar was to skyrocket upwards and -- and got up into the -- the region of maybe ninety (90) cents US?

MS. LYN WRAY: Just first before answering that, to go back to the linkage to the decline in export revenues attributable to foreign exchange. We should add to that, that there would be a decline in finance expense as well, attributable to foreign exchange and therefore the impact on the bottom line to a fair degree, would be hedged over a period of time.

Now, as to your question as to what would happen if we had a very large increase in -- in -- I think you said the -- the Canadian dollar, was it?

MR. BOB PETERS: Well I was --

MS. LYN WRAY: You can make it, yeah --

MR. BOB PETERS: Canadian dollar strengthened --

MS. LYN WRAY: Yes.

MR. BOB PETERS: -- against the American dollar.

MS. LYN WRAY: The -- the financial sensitivity that you alluded to looked at a situation in which the Canadian dollar might go up five (5) cents US and what that would do in IFF-03 would be by 2014 would increase our debt ratio by 1 percent.

And the reason for the fairly small impact would -- is that as well as having US revenues coming in, we also have US debt.

And over a period of time, those two (2) are to a fair degree, hedged. Having said that, if there was a very certain -- very sudden turn-around in the US dollar, then we would see impacts for a particular year that -- that would not have been anticipated and -- and then we would probably deal with that as we did this year by a strategy such as purchasing half of the shortfall on a monthly averaging basis and -- and placing forward contracts for the balance, something like that, that would even out the -- the effect of the -- of that foreign exchange exposure which would, in that event, affect our net income statement, either up or down.

MR. BOB PETERS: Well, it would -- would it not affect it negatively, Ms. Wray, if -- if it got --

MS. LYN WRAY: Well, if we -- yeah --

MR. BOB PETERS: -- strong?

MS. LYN WRAY: Yes, if we were in a -- if we were in a long position, then -- which means if we've got more US export revenues coming in than -- than US expenses going out, then that would affect us negatively if the US dollar came down.

Conversely, if we were in a short position, as we were last year where our out -- US dollar outflows are greater than our US finance expense, then that would be beneficial, as the US rate came down.

MR. BOB PETERS: All right, thank you, Ms. Wray. With yourself and Mr. Warden and Mr. Derksen, I'd just like to turn to the balance sheet which is found at Document 27 of the Book of Documents that's been provided, and this copy was taken from the annual report; page 78 I think is the reference.

But I take it it's one that you've seen before and many times, perhaps?

In turning to the assets in service, the assets in service have been valued at $9.99 billion dollars. How was that number determined?

MR. VINCE WARDEN: Well, it's the 9 million oh seventy-two (72) of the previous year to which any plant in-service coming in during the year is added and any retirements are subtracted.

MR. BOB PETERS: Based on its cost, Mr. Warden?

MR. VINCE WARDEN: Based on its cost, yes.

MR. BOB PETERS: And then the depreciation that's been subtracted includes the revised depreciation that Mr. Derksen told me about as a result of the new study?

MR. VINCE WARDEN: That would reflect the new rates, yes.

MR. BOB PETERS: All right. So, net we're looking at $6.9 billion dollars of assets in service?

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

MR. BOB PETERS: In terms of -- of -- Mr. Warden and Mr. Derksen, I understand that the information technology costs can be capitalized and included in those assets in service, under certain circumstances.

Have I got that right?

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

MR. BOB PETERS: And as I understood, one of the interrogatories, Mr. Derksen, if you have IT costs than are more than two hundred (200) days on a project, two hundred (200) person days on a project, then you would capitalize it?

MR. WILLIE DERKSEN: That would be for system development costs, yes. That’s the criteria that we use for internal components.

MR. BOB PETERS: And how was that determined that two hundred (200) person days is the point at which IT costs then get capitalized?

MR. WILLIE DERKSEN: It -- well, it’s a company policy. It’s -- it’s an assessment to say projects that are under that -- that materiality level, it’s appropriate to charge them to expense and projects that are over that, it’s substantial enough that they should be capitalized.

It’s -- it’s really an assessment of -- of a materiality guideline.

MR. BOB PETERS: You don’t assess it on individual projects, you just apply it as a blanket policy?

MR. WILLIE DERKSEN: Yes, that’s correct. Presumbly -- in fact, all of our software application activities would qualify as assets by the nature of the period to which they are expected to be in service. So they will provide service and value to -- in future periods, as well as the current period.

MR. BOB PETERS: But you don’t determine the future benefit of that two hundred (200) person days worth of IT work before deciding whether or not to capitalize it?

MR. WILLIE DERKSEN: No, sir, we don’t. The thing is, if we took all of our IT projects and we said -- and we looked at each one of them, every single improvement would have future benefit and so you’d end up -- you could end up capitalizing the vast majority of your IT application support people’s costs.

Consistent with most companies and utilities, there’s a guideline -- a materiality guideline, that’s used to ascertain whether it warrants capitalization or whether -- whether it should be expensed.

MR. BOB PETERS: Thank you, Mr. Derksen and turning to construction at progress, Mr. Derksen, of $356 million dollars.

Does that include expenditures on Wuskwatim?

MR. VINCE WARDEN: To the extent there are any expenditures on Wuskwatim, they wouldn’t be -- be included in that number, how -- however, they would be minimal at this point in time.

MR. BOB PETERS: Also included in that would be if any projects that you have on the go, Mr. Warden or Mr. Derksen, they’d be financed and you would also include in there the weighted average cost of your capital?

MR. WILLIE DERKSEN: That's right.

MR. BOB PETERS: And that weighted average cost of capital, Mr. Derksen, would include both a debt component and an equity component?

MR. VINCE WARDEN: No, for pur -- purposes of capitalization, it's the -- the cost of debt only.

(BRIEF PAUSE)

MR. BOB PETERS: But while it includes the debt portion only then, Mr. Warden, the entire finance expense is capitalized while the project is still under construction?

MR. VINCE WARDEN: It is, yes.

MR. BOB PETERS: And is that cost of capital which is based only on the debt cost based on your actual or on your forecast, cost of debt.

MR. VINCE WARDEN: Actual.

MR. BOB PETERS: Mr. Warden, would another option to the Corporation be to, rather than capitalize the finance expense, expense it in the year in which it was incurred?

MR. VINCE WARDEN: No. No, that wouldn't be good accounting to do that.

MR. BOB PETERS: Why is that not good accounting?

MR. VINCE WARDEN: Well, because it, as mentioned earlier, one of the primary objectives of accounting is to match revenues and expenditures so the ratepayer should only pay the cost associated with the benefits they derive and to -- to charge those ratepayers with financing costs that pertain to future periods would be inequitable.

MR. BOB PETERS: But once a project comes in service then those capitalized costs including the capitalized financing costs are then depreciated and started charging through in the rates?

MR. VINCE WARDEN: That's right.

MR. BOB PETERS: Do you believe, Mr. Warden, that the embedded and capitalized financing costs add value to the assets?

MR. VINCE WARDEN: Yes, it's -- it's a part of the cost of -- just as much a part of that cost as our materials and labour and expense; all of the other costs.

MR. BOB PETERS: You're not of the view that that would overstate them on the balance sheet?

MR. VINCE WARDEN: Not at all, no.

MR. BOB PETERS: When I come to the pension assets on the balance sheet, there appears to be some indication that there’s a deficit under Manitoba Hydro in their pension assets.

Mr. Derksen or Mr. Warden, is that correct?

MR. VINCE WARDEN: That’s correct. For the fiscal year ended ’02/’03, there was a deficit. There was a surplus in ’01/’02 and we’re back into a surplus position again in ’03/’04.

MR. BOB PETERS: And the deficit the -- the surplus you’re talking about now is in the -- is in the financial statements for the year ending 2004?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: All right. Which we haven’t seen yet?

MR. VINCE WARDEN: That’s correct.

MR. BOB PETERS: Okay. And the deficit that existed in 2003, Mr. Warden, was approximately 22 million?

MR. VINCE WARDEN: Yes, I believe so. Yes, the difference between the 457 million that’s indicated in the assets versus the pension obligation of four seventy-nine (479), that -- that’s -- you’re correct in your calculation.

MR. BOB PETERS: And I also noted that there was a positive position on the Centra pension asset side of the ledger. Are you aware of that?

MR. VINCE WARDEN: No, no. There’s not a -- I’m not sure what you’re referencing there, but there’s not a positive balance on the Centra side. The Centra plans are actually in deficit.

MR. BOB PETERS: That's a separate deficit as opposed to the Manitoba Hydro? They're not combined?

MR. VINCE WARDEN: It is -- it's a separate deficit, yes.

MR. BOB PETERS: What is Manitoba Hydro's plan to fund this $22 million dollar deficit?

MR. VINCE WARDEN: They're being funded -- they'll be fully funded within the next five (5) years.

MR. BOB PETERS: Can you tell the Board what is the status of the Winnipeg Hydro Pension Plan relative to the Manitoba Hydro Pension Plan?

MR. VINCE WARDEN: The Winnipeg Hydro Pension Plan is basically in a surplus position. However, there are small -- there is a small contribution being made by Manitoba Hydro. I believe the amount last year was about two hundred thousand dollars ($200,000), subject to check. I can check that number, but it's in that range.

MR. BOB PETERS: Was that a deficit that existed at the time of acquisition?

MR. VINCE WARDEN: No. Like other -- many other pension funds, the City of Winnipeg Plan also experienced some losses on investments and therefore the surplus that was there at the time of acquisition, was reduced.

MR. BOB PETERS: Will Manitoba Hydro be amalgamating the pension plans?

MR. VINCE WARDEN: Of --

MR. BOB PETERS: Centra, Winnipeg Hydro and Manitoba Hydro?

MR. VINCE WARDEN: Well, no. Part of the asset purchase agreement was that the employees of Winnipeg Hydro -- the former employees of Winnipeg Hydro, would remain part of the civic plan because it's a superior plan to Manitoba Hydro's and we'll continue to contribute to that plan.

The -- the only way they could be -- ever be merged is -- would be if Manitoba Hydro's plan was brought up to the benefits provided in the -- in the civic plan. But we don't foresee that happening in the near future.

MR. BOB PETERS: Would it be correct then, that any new employees that are hired, whether they work in the old Winnipeg Hydro surface -- service territory or not, are added onto the Manitoba Hydro Pension Plan?

MR. VINCE WARDEN: Yes. That's what we're doing. The bargaining unit that represents the former Winnipeg Hydro employees doesn't agree with that and there's a grievance filed for that reason.

MR. BOB PETERS: On the deferred debt costs, listed on the balance sheet, I understand that approximately $513 million of deferred foreign exchange is included in that $571 million of deferred debt cost.

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

MR. BOB PETERS: Can you explain to the Board how deferred foreign exchange arises on your balance sheet?

MR. VINCE WARDEN: Well, it’s simply a translation of US debt at the exchange rate prevailing at balance sheet date. So, we would take all of the outstanding US debt at March 31, 2003, for example, translate it at the exchange rate at that date, and the gain or -- or loss is recorded in deferred foreign exchange.

All those amounts are -- are hedged with the firm export revenues and that will be reduced in two (2) ways. Either by an improvement in the exchange rate, or by the recording of revenues in the year in which those debt -- those debt -- respective debt issues mature.

MR. BOB PETERS: What exchange rate for -- for US debt do you record on your balance sheet?

MR. VINCE WARDEN: The exchange rate for US debt is recorded at the exchange rate as at March 31st, 2000 -- of the respective year.

MR. BOB PETERS: I’m not sure that --

MR. VINCE WARDEN: Well, whatever the exchange is at March 31st we’ll record it at that existing rate.

MR. BOB PETERS: Okay. And then what was that day -- what was that rate on March 31st if you know, Mr. Warden?

MR. VINCE WARDEN: Of 2003 or 2004?

MR. BOB PETERS: Well, since I haven't seen 2004, I'll stick with 2003.

MR. VINCE WARDEN: If I can just take one (1) minute I'll give you both rates.

(BRIEF PAUSE)

MS. PATTI RAMAGE: Mr. Chair, while Mr. Warden is looking that up, Mr. Cormie has provided me with an answer to another one (1) of the undertakings given during his testimony. So with your permission I thought we'd have that distributed while -- to use the time.

THE CHAIRPERSON: Please.

MR. VINCE WARDEN: And I can give you those rates now if you like. At March 31st of 2003, $1.00 US was equal to $1.47, one forty-seven (147) Canadian. March 31st of 2004, that rate was 1.31 Canadian. So it moved from one forty-seven (147) to one thirty-one (131) over that period of time.

MR. BOB PETERS: Is it the change from the one forty-seven (147) to the one thirty-one (131) that created the -- the deferred charge of $513 million?

MR. VINCE WARDEN: Well, no it's taking all of the debt at March 31st of 2003, all the US debt translating it at one thirty-one (131) and the five hundred and thirteen (513) number is what -- is derived there from -- from compared to the number in the previous year.

MR. BOB PETERS: Does that indicate to the Board then that the -- the debt that you had, the -- the face value of the debt was -- was more favourable?

MR. VINCE WARDEN: Well, the stronger Canadian dollar meant that there was of a deferred amount to -- to record on the balance sheet. It's -- because we're fully hedged though on our debt principal, it really for Manitoba Hydro's perspective we're pretty much indifferent to the exchange rate.

MR. BOB PETERS: And the fully hedged again is -- is simply on the physical side that you're going to have US receipts and US debt and you offset one (1) to the other?

MR. VINCE WARDEN: We match the two (2), yes, that's right.

MR. BOB PETERS: What percentage of Manitoba Hydro's debt is denominated in US currency?

MR. VINCE WARDEN: I believe it's around 60 percent. I’ll double check that number but it’s in that order of magnitude.

MR. BOB PETERS: In turning to the goodwill portion of the -- of the balance sheet, I understand this goodwill comes 46 million from Winnipeg Hydro and 62 million from Centra Gas Manitoba Inc. Have I got that right?

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

MR. BOB PETERS: And, Mr. Derksen, this goodwill is defined by Manitoba Hydro as the difference between the purchase price and the value of the assets that you acquired?

MR. VINCE WARDEN: That’s right.

MR. BOB PETERS: And I understand that from accounting perspectives, there is an impairment test that is -- that is done to test whether the goodwill survives and that impairment tests has been done on Centra?

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

MR. BOB PETERS: And what was the result of that, Mr. Derksen?

MR. WILLIE DERKSEN: The result was that there’s no impairment to the goodwill of Centra.

MR. BOB PETERS: And has an impairment test done -- been yet done on the Winnipeg Hydro goodwill?

MR. WILLIE DERKSEN: Yes, it has.

MR. BOB PETERS: And when was that done?

MR. WILLIE DERKSEN: There was one (1) done for March 31st of 2004.

MR. BOB PETERS: Are you prepared to file that with the Board?

MR. VINCE WARDEN: There's really nothing to file. The auditors at -- as part of their process year-end audit confirm to the audit committee that there's no impairment so there's no real document prepared in that regard.

MR. BOB PETERS: Is there a note in the financial statements?

MR. VINCE WARDEN: There's a note in the minutes to the audit committee. But there's no specific reference to that in the -- in the financial statements. If there was an impairment there would be a note.

MR. BOB PETERS: Just on that note, Mr. Warden and Mr. Derksen, it -- it appeared that there was about $73 million dollars of revenue that could be expected from Winnipeg Hydro as a result of the acquisition.

Does that number sound about right?

MR. VINCE WARDEN: It's more --

MR. BOB PETERS: This would be --

MR. VINCE WARDEN: No --

MR. BOB PETERS: -- over the balance of the seven (7) months left in the --

MR. VINCE WARDEN: Oh, yes.

MR. BOB PETERS: -- the year?

MR. VINCE WARDEN: I agree, yes.

MR. BOB PETERS: And there was still 41 million of prorated expenses, likewise, that would be incurred as a result of that acquisition?

MR. VINCE WARDEN: Do you -- do you have a reference on that?

MR. BOB PETERS: I'll just check and see if it's in the financial statements. Note 2 on page 84 of the consolidated financial statements for 2003.

(BRIEF PAUSE)

MR. VINCE WARDEN: Yes, I see that.

MR. BOB PETERS: And then does it follow that of the surplus of 32 million would be reduced by the $27 million loss to Manitoba Hydro by the wholesale revenue loss?

So that over that seven (7) month period there would be about a $5 million surplus to Manitoba Hydro as a result of the acquisition?

(BRIEF PAUSE)

MR. BOB PETERS: Maybe, Mr. Warden, I can -- I can assist in this fashion. If we start with 73 million appreciating, we're dealing with a seven (7) month period here. $73 million of -- of revenue.

Subtract from that the $41 million of expenses and have about a $32 million surplus. But that $32 million surplus would be reduced by 27 million because of the loss of wholesale revenue that Manitoba Hydro would receive netting out at $5 million of surplus over a seven (7) month period.

Do you agree with that analysis to get to the $5 million surplus?

MR. VINCE WARDEN: Well, I agree that's what you said the first time and yes, I -- that's what it works out to --

MR. BOB PETERS: Well, I --

MR. VINCE WARDEN: -- yes.

MR. BOB PETERS: I was trying to be helpful on it and if that was annualized over twelve (12) months you would be at about $8.6 million of surplus on an annual basis or incremental benefit to Manitoba Hydro?

(BRIEF PAUSE)

MR. VINCE WARDEN: Mr. Peters, actually, in reviewing these numbers I'm -- what I'm a little perplexed about is the -- is the forty-one (41) that looks on the high side. I'm sure it must be right, it's in our financial statements. I'm just having -- trying to reconstruct in my mind where that came from.

I think our estimate of expenses for the year for -- for Winnipeg Hydro were more like thirty-two (32), 33 million.

(BRIEF PAUSE)

MR. BOB PETERS: Well, that --

MR. VINCE WARDEN: If you'd just give me one (1) -- one (1) minute.

MR. BOB PETERS: Sure. Sorry. Sure.

(BRIEF PAUSE)

MR. VINCE WARDEN: Sorry for that delay. Would you like to carry on, Mr. Peters?

MR. BOB PETERS: Is the $41 million of expenses accurate?

MR. VINCE WARDEN: Well, I'm sure it's accurate. The number I was referring to earlier was operating and administrative expenses and you add on interest, depreciation, forty-one (41), yes --

MR. BOB PETERS: Okay.

MR. VINCE WARDEN: -- would be accurate.

MR. BOB PETERS: All right. So on an annualized basis, there would be about $8.6 million of incremental benefit to Manitoba Hydro?

MR. VINCE WARDEN: Well, I'm ha -- using those nu -- the numbers that we have here I do agree with your calculation, yes.

MR. BOB PETERS: All right. Let me give you a chance that once we're finished this area of questioning if you go back and reflect on it and want to file something further, please do. And I don't want to limit the information you provide to the Board.

But, if it was $8.6 million on an annualized basis, we've already heard that the payments start off at $25 million a year, decline to 20 million a year and then 16 million a year in perpetuity. Correct?

MR. VINCE WARDEN: Yes, and I -- I realize that's where you're -- we're going with this and the $73 million would probably not be proportional. The -- the revenue for the full year, depending on the year -- or the month of revenue.

So, I think what it would be -- what we've stated in the past is essentially the acquisition of

Winnipeg Hydro is bottom-line neutral. It might be worthwhile for us to put together a bit of a reconciliation of that so we can demonstrate that that in fact is the case.

MR. BOB PETERS: So you'll take away this and -- and provide the reconciliation and maybe what the annualized incremental benefit is to Manitoba Hydro?

MR. VINCE WARDEN: Yes, I would prefer to do that.

--- UNDERTAKING NO. 17: Provide the Reconciliation and Maybe what the Annualized Incremental Benefit is to Manitoba Hydro.

MR. BOB PETERS: All right and then -- just in general terms then, and not holding you to any particular numbers at this time, where is the goodwill from the Winnipeg Hydro acquisition. If the numbers of the incremental benefit are in the area of -- and I'm proposing $8.6 million, and your payments are starting off at 25 million.

How -- how do we find goodwill in -- in that transaction?

MR. VINCE WARDEN: Well, according to your definition earlier, which I'd agree with, is -- is the correct one (1) for goodwill.

That is, the -- the purchase price, over and above the value of the assets, is represented by goodwill. Then the goodwill is something that would represent future earning potential of Winnipeg Hydro. And that's what the auditor does when they look at whether or not there is an impairment to -- to confirm that that earning potential is there.

MR. BOB PETERS: Can you confirm that the discount rate used by Manitoba Hydro to assess the purchase price of Winnipeg Hydro was 7.45 percent?

MR. VINCE WARDEN: It was actually -- 7.45. I'll agree with that.

MR. BOB PETERS: All right and was this discount rate the same as the discount rate used on other capital projects?

MR. VINCE WARDEN: It reflected our costs of capital at the time of the acquisition and it would be consistent with how we valued other capital projects at that time.

MR. BOB PETERS: Did it -- did it include both a -- a debt and an equity component?

MR. VINCE WARDEN: No, it would have been debt only, the cost of debt only.

MR. BOB PETERS: Based on actual or based on forecast?

MR. VINCE WARDEN: It would be based on actual at that -- at that point in time.

MR. BOB PETERS: In the Winnipeg Hydro acquisition, there were to be some revenue enhancements as a result of that transaction, correct?

MR. VINCE WARDEN: Revenue enhancements, in terms of? Could you maybe elaborate on what you mean by that?

MR. BOB PETERS: It's my understanding from the materials provided that as a result of purchasing the Winnipeg Hydro assets, Manitoba Hydro thought it would have an opportunity to increase electricity sales over and above what Winnipeg Hydro was actually --

MR. VINCE WARDEN: Oh, I see. Yes. Yes. The -- through the optimization of Winnipeg Hydro generating facilities on the Winnipeg River, we did include some additional revenue for that purpose, yes. And that's what we meant by revenue enhancements.

MR. BOB PETERS: And, I think that one (1) of the three (3) areas of revenue enhancements, but I think we heard today that there's been no decision to enhance the Pointe du Bois or the Slave Falls facilities at this point in time.

Is that also correct?

MR. VINCE WARDEN: That's correct.

MR. BOB PETERS: So at this point in time, there is no revenue enhancement planned as a result of your acquisition of Winnipeg Hydro.

MR. VINCE WARDEN: Well, there -- there's still enhancements in the way we operate those facilities so, rather than operating independently from Winnipeg Hydro, there are benefits derived from it -- from them being operated as part of the integrated generation system.

MR. BOB PETERS: When you say -- but weren't they by and large being integrated before recognizing Winnipeg Hydro was the operator?

MR. VINCE WARDEN: They were, but there were cases where they would be taken down for maintenance, not co-ordinated with Manitoba Hydro. So Manitoba Hydro would have to do work-arounds, because of Winnipeg Hydro's maintenance schedules, those kind of operational difficulties that no longer exist.

MR. BOB PETERS: Do you know what that would quantify to on an annual basis, Mr. Warden, in terms of those operating efficiency enhancements?

MR. VINCE WARDEN: I'll look at -- towards Mr. Cormie, Mr. Surminski. They might have more information in that but I'm sure that's part of our documentation.

I don't have that at my fingertips, so.

MS. LYN WRAY: Mr. Peters, I believe we did all that work as part of the Winnipeg Hydro acquisition project and we didn't file information on that at this hearing because of the -- the provisions that the government issued, that it was not to be reviewed by the PUB.

MR. BOB PETERS: Are you able -- just so that we're clear, if there's a suggestion that there's going to be revenue enhancements as a result of operating efficiencies, I just wondered if you could provide that number to this Board, or is it your position that that's not to be provided to this Board?

MS. LYN WRAY: I can't comment on the legal matters, but I -- just to say that we did look at all of that in the context of the Winnipeg Hydro acquisition.

A purchase price was agreed upon and what we've provided you, and I don't have the reference in front of me, but there's been several interrogatories where we showed the net impact on the IFF of all the efficiencies that we could foresee and synergies, the impacts of the purchase price to Winnipeg Hydro.

And our conclusion as laid out in the responses to the interrogatories was that the impact would be bottom-line neutral. There would be a small impact on the debt ratio by -- by the end of the IFF period and -- and similarly a very small impact on the interest coverage ratio.

But in terms of net income, it might be up a little year, down -- one (1) year and down a little the next year, but by and large, over the forecast period, it was -- it netted out.

And that would have comprised our quantification of the operating efficiencies that you're referring to.

MR. BOB PETERS: All right, just so we don't dwell too long here, Ms. Wray, there was an interrogatory, CAC/MSOS-MH-I-IR-6(A) which contained a schedule attached to it that you may be referring to, and in fairness, you should have a chance to review that and see if you have any further comments in respect of the last answer you gave.

MS. LYN WRAY: What was that number again, Mr. Peters?

MR. BOB PETERS: CAC/MSOS-MH-I-IR6(A). And I'm looking on Page 2 of two (2) at the table.

(BRIEF PAUSE)

MS. LYN WRAY: Yeah, the -- the interrogatory I was thinking of was one (1) to do with the IFF. This is one (1) that Mr. Derksen could speak to.

(BRIEF PAUSE)

MR. WILLIE DERKSEN: I wonder if you could just repeat the question for me, Mr. Peters?

MR. BOB PETERS: Well, what I -- what I wanted to -- to find out was that the revenue enhancements that were going to hopefully be achieved as a result of the Winnipeg Hydro acquisition, I thought were confined to three (3) areas, one (1) of which was the additional output from two (2) plants.

I thought there was excess fibre optic capacity which you could rent out and the other was electricity sales.

Are you familiar with those?

MR. WILLIE DERKSEN: Yes, that's -- I'm familiar with those and those are the three (3) areas that we did talk to.

MR. BOB PETERS: Are those three (3) areas in total, a $2 million enhancement?

MR. WILLIE DERKSEN: That was our projection, yes.

MR. BOB PETERS: All right. And is that projection still being made, recognizing that Pointe du Bois and Slave Lakes may not be up -- or Slave Falls will not be upgraded?

MR. WILLIE DERKSEN: I -- I believe the amount included in this response related to matters that Mr. Warden talked about and I believe we are achieving those enhancements already. It wasn't -- they weren't due to an overhaul or to a refurbishment of that facility.

MR. BOB PETERS: All right, fair enough. In terms of Power Smart savings, Mr. Derksen, is Manitoba Hydro supposed to deliver a dollar amount of DSM savings to Winnipeg -- City of Winnipeg?

MR. WILLIE DERKSEN: Yes.

MR. BOB PETERS: What amount is that, Mr. Warden? Is that eight hundred thousand (800,000) a year?

MR. VINCE WARDEN: Eight hundred thousand (800,000) per year is right, yes.

MR. BOB PETERS: And that's the savings that Winnipeg is supposed to receive annually?

MR. VINCE WARDEN: Yes, over a ten (10) year period.

MR. BOB PETERS: And the costs to achieve that are paid for by whom?

MR. VINCE WARDEN: By Manitoba Hydro.

MR. BOB PETERS: Mr. Derksen, there's an unallocated reserve attached to this transaction noted in one (1) of the interrogatories, I think the one (1) that I had referenced to Ms. Wray of about 2.985 million. Can you explain what that's for?

MR. WILLIE DERKSEN: Yes, at the point or just subsequent to the acquisition, there were detailed assessments made of what synergy savings could be accomplished immediately. Those totalled approximately $3 million dollars and our target and our expectation is that by 2005 and '06 we will achieve a total of $6 million dollars of operating cost reductions.

The $3 million dollars is included in our budgets and is included in the forecasts in this IFF. But the specific areas where that's to be achieved has not yet been planned or assessed.

MR. BOB PETERS: Would you agree, Mr. Derksen, that the good will then is in some way tied to the synergy that you hope to achieve?

MR. VINCE WARDEN: The -- the -- there really isn't a direct linkage there to the synergies. It's more so based on the -- the revenue potential of Winnipeg Hydro as an entity compared to the costs that we -- the amount we paid for Winnipeg Hydro.

MR. BOB PETERS: Can you indicate, Mr. Warden, how Manitoba Hydro will know when it's achieved the -- the synergies that it -- it expects to?

MR. VINCE WARDEN: Well, as Mr. Derksen indicated, we've actually pulled those amounts out of the budgets of Manitoba Hydro. So, they're being driven -- driven through the budgeting process.

MR. BOB PETERS: They're not tracked discreetly by department or a profit centre or a business centre, they're done just through the budgeting process?

MR. VINCE WARDEN: To the extent possible. To the extent that they're allocate -- we're able to allocate them directly to a -- a business unit division, a department, we do that. But to the extent we're not able to do that, they're taken out at the corporate level.

MR. BOB PETERS: All right. Also noted is that as part of this purchase, Manitoba Hydro issued $186 million dollars of debt in the form of Hydro Bonds to the City. Is that correct?

(BRIEF PAUSE)

MR. VINCE WARDEN: I'm not sure where you're getting your reference to Hydro Bonds, Mr Peters. Maybe you can point us in that direction.

MR. BOB PETERS: On page 89 of the financial statements for 2003, there was referenced -- there was a reference to hy -- to bonds being issued to the City of Winnipeg. Perhaps my reference to them as Hydro Bonds may have been inappropriate but --

MR. VINCE WARDEN: Yes, they're -- they're Manitoba Hydro Board Bonds, but they're -- don't come under the heading of what we call Hydro Bonds.

MR. BOB PETERS: And these bonds were to pay off long term debt that -- that the City -- that Winnipeg Hydro had?

MR. VINCE WARDEN: Yes.

MR. BOB PETERS: It -- it appears that the interest rate of these bonds range from 5.9 to 11.7 percent, Mr. Warden. Is that correct?

MR. VINCE WARDEN: Those were the rates on the bonds existing -- the existing debt of Winnipeg Hydro, yes.

MR. BOB PETERS: Okay. Well -- why would you not issue bonds at a lower interest rate and reduce the debt level from what Winnipeg Hydro was carrying?

MS. PATTI RAMAGE: Mr. Peters, I think now we're crossing -- it's a fine line we're walking here I know, but we're -- we're crossing over to acquisition reasons for the purchase price paid versus the impact on rates going forward.

MR. BOB PETERS: In terms of the impact on rates going forward with this -- the additional debt cost would be cost paid for by the consumers of Manitoba Hydro going forward; would they not, Mr. Warden?

MR. VINCE WARDEN: Any costs over and above the revenues we derived from the acquisition would be borne by the ratepayers of Manitoba, that's correct. I think though we've stated that it's bottom line neutral to Manitoba Hydro and its ratepayers and that was the basis under which the purchase agreement was consummated with the City.

MR. BOB PETERS: Mr. Chairman, in light of the hour and the admonition I had received, I think I'll stop at this point.

I do want to thank Mr. Cormie, Mr. Surminski, Ms. Wray, Mr. Warden and Mr. Derksen to -- for answering the questions that they have. And I'll use the time between now and when we next meet to see if I have anymore questions and then if I do I'll beg my friends opposite for an opportunity. But if not, I thank them at this time for their co-operation. I do appreciate it greatly.

THE CHAIRPERSON: Thank you, Mr. Peters. Thank you for Responders from Manitoba Hydro. Ms. Ramage, I -- I guess we have another exhibit here? Exhibit 22?

MS. PATTI RAMAGE: That's right and I'll agree with My Friend, Mr. Peters that we were -- we're 21 now 22 here.

THE CHAIRPERSON: Well, thank you to everyone and we will see you again next Monday at nine o’clock. Take care.

--- Upon Adjourning at 4:05 p.m.

Certified Correct,

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Carol Wilkinson, Ms.