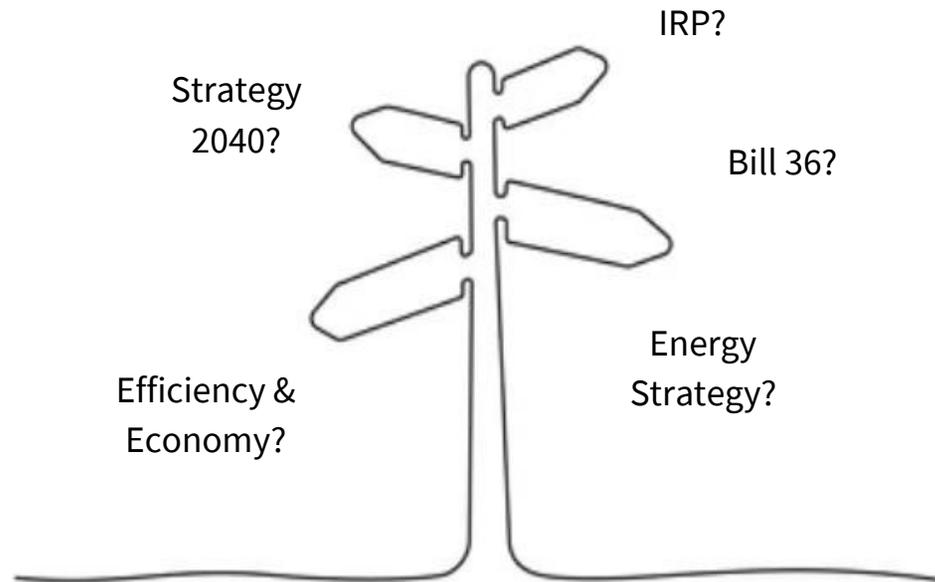


# A MONOPOLY AT THE CROSSROADS AND CAPTIVE CONSUMERS

Opening Submissions of the Consumers Coalition



Manitoba Hydro 2023/24 & 2024/25 General Rate Application

Presented by: Public Interest Law Centre

May 15, 2023

## OUTLINE

- 1) The Consumers Coalition
- 2) A Monopoly at the Crossroads and Captive Consumers
- 3) These are Not Just and Reasonable Rates
- 4) Order 164/16 has not been Honoured
- 5) Preview of Consumers Coalition Recommendations

## PART I: THE CONSUMERS COALITION

- Member Organizations:
  - Consumers' Association of Canada (Manitoba) Inc.
  - Aboriginal Council of Winnipeg
  - Harvest Manitoba
- Represents the interests of residential customers
- Develops its positions through direct engagement with consumers, broad stakeholder consultation and expert advice.<sup>1</sup>
- Looks forward to learning from amazing community presenters on Day 2.



<sup>1</sup> See, for example, public opinion surveys filed as MH/COALITION I-I(c) Attachments I-3.

## **THE INDEPENDENT EXPERTS OF THE COALITION**

While Manitoba Hydro continues to struggle with losses of subject matter experts, the Consumers Coalition is supported by an outstanding team:

- Leading experts on public utility regulation, capital asset management and the financial markets for energy companies
- Extensive experience inside Manitoba Hydro at senior management levels
- Relied upon by independent regulators, businesses, utilities and consumers to develop pragmatic responses to contemporary Canadian challenges

## **HYDRO NEEDS TO UP ITS GAME ON COMMUNITY ENGAGEMENT**

Key message from experts and the Consumers Coalition:

- Manitoba Hydro brings an impoverished approach to engagement on customer priorities (see good practice examples on the record)<sup>2</sup>

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<sup>2</sup> Independent Evidence of Midgard Consulting, Inc. at section 7.2.1. See also the survey by Innovative Research Group filed with the British Columbia Utilities Commission as part of the BC Hydro 2021 Integrated Resource Plan process cited at footnote 68 of the Midgard report.

## PART 2: A MONOPOLY AT THE CROSSROADS AND VULNERABLE CONSUMERS

“Moving into the implementation of Strategy 2040 ahead of the release and analysis of the Manitoba Energy Policy is like a subsidiary company beginning to implement its own strategy **before** the strategy, strategic initiatives and **plans of the parent** company are released and **sufficiently understood.**”<sup>3</sup>

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<sup>3</sup> Independent report of Darren Rainkie at 19.

## A MONOPOLY AT THE CROSSROADS

Manitoba Hydro's Strategic Future is **Highly Uncertain**.

A Critical Year:

- Manitoba Energy Strategy – Summer 2023?
- Integrated Resource Plan (or a plan to have a plan) – Summer 2023?
- The Fate of Bill 36 – October 3, 2023?

Hydro's Strategic Future may look very different in the months to come with **cascading impacts** upon Strategy 2040 and future rate paths.

## RATES MUST BE DRIVEN BY EVIDENCE NOT SPECULATION

- Manitoba Hydro's energy future remains ambiguous, and the arbitrary financial targets that drive Hydro's rate request are not yet binding
- Manitoba Hydro must master the fundamentals of cost control and budget optimization to effectively facilitate any energy transition
- The next year may provide much-needed clarity
- But today's rates require evidence-based justification which is sorely lacking
- It is important for the PUB to signal that economy and efficiency should not be subordinated to the nascent imaginings and decade long journeys of Strategy 2040

## RESIDENTIAL RATEPAYERS ARE VULNERABLE

- Significantly higher-than-inflation rate increases since 2011<sup>4</sup>
- Residual adverse effects of the pandemic
- Overall Inflationary Pressures (i.e. grocery bills)

*“Over the two-year period during the pandemic, arrears > 90 days for electric customers increased 80%, or approximately \$23 million.”<sup>5</sup>*

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<sup>4</sup> Independent Evidence of Darren Rainkie at 127.

<sup>5</sup> Manitoba Hydro 2023/24 & 2024/25 General Rate Application, Tab 3 (Amended) at 44.

## A SIGNIFICANT IMPACT DURING DIFFICULT TIMES

“The MH rate increase proposals . . . represent a cumulative rate increase of 4.04% or approximately \$74 million on an annualized basis. The net present value (NPV) of these two rate increases to customers in perpetuity is approximately \$1.5 billion, assuming a social discount rate of 5%.

[...]

The NPV of these three rate increases [including the interim increase] to customers in perpetuity is approximately \$2.8 billion...”<sup>6</sup>

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<sup>6</sup> Independent report of Darren Rainkie at 111 (footnote omitted)

**THIS GRA COMPOUNDS THE VULNERABILITY OF  
RESIDENTIAL RATEPAYERS**

Driven by Strategy 2040, Manitoba Hydro's application **compounds the vulnerability of residential ratepayers:**

- Rate increases of 4.8% over the next 12 months over and above the 3.8% increase to residential customers granted in the 2021/22 Interim Rate Application
  - 8.8% cumulative increase since January 1, 2022

## CONSUMERS ARE STRETCHED TO THE LIMIT

A March 2020 survey conducted by Prairie Research Associates asked about the amount of rate increase in the following year that would be reasonable and affordable.

Over half of respondents indicated that rate increases of over 2% within the year would be untenable, with 25% of respondents indicating that 2% is the maximum increase they could manage, 11% of respondents identifying a 1% increase as their limit, and 26% of respondents indicating that no increase would be reasonable or affordable for their household.

69% of respondents supported the idea of measures to make electricity more affordable for low-income households.<sup>7</sup>

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<sup>7</sup> MH/COALITION I-1(c) Attachment 3, page 11.

## A COUNTER-INTUITIVE APPLICATION

Manitoba Hydro seeks to impose 4.8% in rate increases on residential customers over the next year despite:

- Record-setting Export Revenues in 2022/23 of almost \$1.3B
- A record-setting year in 2022/23 with \$750M in net income
- Projected net income in 2023/24 without the rate increase of \$445 M
- Annual \$180M reduction in water rental and debt guarantee fees
- Endemic backsliding on expenditure control and longstanding inertia on capital asset management

## PART 3: THESE ARE NOT JUST AND REASONABLE RATES

Manitoba Hydro has the **onus** to establish its proposed rates are just and reasonable.

The PUB's statutory mandate requires it to:

- ensure that MH's forecasts are reasonably reliable,
- determine that actual and projected costs incurred are necessary and prudent,
- assess the reasonable revenue needs of the Corporation in the context of the overall general health of MH,
- estimate an appropriate allocation of costs between classes, and
- setting just and reasonable rates in accordance with statutory objectives.<sup>8</sup>

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<sup>8</sup> PUB Order 5/12 at 27. See also *The Crown Corporations Governance and Accountability Act*, CCSM c C336 at s 25 as it read on November 2, 2022; *The Manitoba Hydro Act*, CCSM c H190 at ss 39(1), 39(2.1) as is read on November 2, 2022; *The Public Utilities Board Act*, CCSM c P280 at ss 77, 82 as it read on November 2, 2022. See also *The Manitoba Hydro Amendment and Public Utilities Board Amendment Act*, SM 2022 c 42 at s 65.

## **PROJECTED COSTS ARE NOT PRUDENT AND NECESSARY**

\$2.3 Billion increase in BOC/O&A between 22/23 and 35/36 between MH 16 and MH 22<sup>9</sup>

The Projected O&A & BOC Increases of \$1.5 Billion & \$0.8 Billion are Not Consistent With or Responsive To PUB Findings and Regulatory Signalling from Orders 59/18, 69/19 and 9/22<sup>10</sup>

54% of the \$16.5 billion 20-year capital expenditure forecast is comprised of “placeholder budgets”, unsupported by business plans or sound justification.<sup>11</sup>

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<sup>9</sup> Independent report of Darren Rainkie at 24.

<sup>10</sup> *Ibid* at 74.

<sup>11</sup> *Ibid* at 101. See also the rebuttal evidence of Manitoba Hydro at 22.

## **O&A SIGNIFICANTLY OUTPACING INFLATION**

Costs in 2022/23 are \$85 million or 16.9% higher than prior PUB direction from Order 69/19<sup>12</sup>

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<sup>12</sup> Independent report of Darren Rainkie at 119

## A “SHARED HEALTH” APPROACH TO NON-OPERATIONAL MANAGEMENT BUREAUCRACY

- The largest increase in business unit O&A costs over the last five years, is found in the Governance & Services business units (\$72 million).
- The average increase in these business unit costs is in the order of 10% per year, compared to the average increase in the operational business units which is in the order of 2% per year.<sup>13</sup>
- Some increases such as a 110% (FTE) increase in the President & CEO business unit appear to have minimal support for the change.<sup>14</sup>

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<sup>13</sup> Independent report of Darren Rainkie at 69-70.

<sup>14</sup> Independent report of Dustin Madsen at 82.

## **ALARMING GROWTH IN THE COSTS OF CONSULTANTS AND ECHOES OF PROJECT NOVA**

- MH was forced to concede that it does not have yet have a Digital & Technology strategic plan that is reviewed and approved by the MHEB.<sup>15</sup>
- Driven by Strategy 2040, the forecast increases in consulting costs are alarming with a compound annual growth rate of 48.60% from 2021/22 to 2024/25 as compared to the historical rate of 4% from 2012/13 to 2021/22.<sup>16</sup>
- MH was unable to provide the business case for SAP or provide any information with respect to alternatives being evaluated, risks and NPV of the alternatives.<sup>17</sup>
- Manitoba Hydro's proposed transition to SAP S4/HANA and the related costs (\$150 million+) is highly preliminary and not supported by evidence.<sup>18</sup>

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<sup>15</sup> Independent report of Darren Rainkie at 102.

<sup>16</sup> Independent report of Dustin Madsen at 84.

<sup>17</sup> Independent report of Darren Rainkie at 102.

<sup>18</sup> Independent report of Dustin Madsen at 86-87.

## **IMMATURE ASSET MANAGEMENT PLANNING LEADS TO HIGHER LIFECYCLE COSTS**

“[e]ffective control and governance of assets by organizations is essential to realize value through managing risk and opportunity, in order to achieve the desired balance of cost, risk and performance”<sup>19</sup>

“...paces and prioritizes investments,... ongoing monitoring of performance against targets, and customer engagement to ensure utility plans are informed by customer expectations.”<sup>20</sup>

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<sup>19</sup> Independent report of Midgard Consulting Inc. at 31 citing ISO 55000.

<sup>20</sup> *Ibid* at 44 citing the Ontario Energy Board Handbook for Utility Rate Applications.

## MANITOBA HYDRO IS A LONGSTANDING LAGGARD IN CAPITAL ASSET MANAGEMENT

- MH’s investment decision-making, long-term spending targets, and asset intervention planning is impaired and non-optimized, which leads to higher average lifecycle costs.
- MH is lagging in the foundational GFMAM Groups.
- Data deficiencies lead to “garbage-in/garbage-out” problems with MH’s asset management decision-making.
- MH’s **risk and review activities are consequently so impaired as to be effectively non-existent**.
- The implication is that the group that lobbies most effectively for its cause will be allocated the biggest envelope.<sup>21</sup>

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<sup>21</sup> For references on this slide, see generally the independent report of Midgard Consulting Inc. at 35, 64, 42-43, 57, 62. See also PUB Order 116/08 at 101; PUB Order 5/12 at 105; PUB Order 73/15 at 68; PUB Order 59/16 at 31; PUB Order 59/18 at 111-112.

## CARE SHOULD BE TAKEN IN TERMS OF HYDRO CLAIMS

“MH’s system performance is markedly different than originally claimed. Specifically, MH’s system performance is actually stable and materially better than its Canadian utility peers, as shown in Figure 4 and confirmed by MH...”<sup>22</sup>

“MH ratepayers experience approximately 1/3rd the average interruption duration when compared to ratepayers of MH’s Canadian peers. Similarly (and only slightly less dramatically), MH’s 11-year average SAIFI is 56% of its Canadian peers, which means that the frequency of outages experienced by MH ratepayers is just over half the frequency of outages experienced by ratepayers of its Canadian peers. Simply put, MH’s system performance is markedly superior to that of its Canadian peers.”<sup>23</sup>

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<sup>22</sup> Independent Report of Midgard Consulting Inc. at 20.

<sup>23</sup> *Ibid* at 21.

## STRATEGY 2040 PRIORITIZED OVER OPERATIONAL INVESTMENTS

“In the first 10 years of CEP22, BOC expenditures related to Strategy 2040 initiatives appear to be prioritized over sustaining capital expenditures, despite MH’s concerns with respect to aging infrastructure. MH has not yet developed the business cases that are necessary to support these initiatives for either business purposes or rate-setting purposes.”<sup>24</sup>

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<sup>24</sup> Independent report of Darren Rainkie at 74.

**THE PUB IS NOT BOUND BY THE ARBITRARY FINANCIAL  
TARGETS IN BILL 36**

“debt-to-equity is a questionable metric for a vertically integrated monopoly Crown utility with a debt guarantee from the provincial government. The equity level target does not have the prominence suggested by Manitoba Hydro given the context in which the Utility operates...”<sup>25</sup>

Bill 36 financial targets:

- Do not come into effect for rate setting purposes until April 1, 2025
- Out of step with PUB findings in Order 59/18
- Recognized as arbitrary by independent experts from Morrison Park Advisors<sup>26</sup> and Mr. Patrick Bowman<sup>27</sup>

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<sup>25</sup> PUB Order 59/18 at 63.

<sup>26</sup> See the independent report of Morrison Park Advisors at 27.

<sup>27</sup> See the independent report of Mr. Bowman at 21.

**HYDRO'S ASSERTIONS REGARDING ITS HEALTH ARE  
UNDERMINED BY ITS ACTIONS**

1. If MH is concerned about its financial outlook, interest rate risk and levels of cash flow, then why has it changed its past policy in terms of cost control and increased its O&A and BOC spending plans by \$2.3 billion in the next 14 years;
2. If MH is concerned about elevated levels of risk, then why didn't it make a decision to expedite the implementation of its ERM Program;
3. If MH is concerned about elevated levels of risk, then why didn't it make a decision to keep the more advanced Uncertainty Analysis that was prepared and presented at prior PUB hearings current;

**HYDRO'S ASSERTIONS REGARDING ITS HEALTH ARE  
UNDERMINED BY ITS ACTIONS (CONT'D)**

4. If MH is concerned about Ageing Asset risk, then why didn't it decide to expedite the implementation of its asset management framework and associated process improvements, instead of a continuing multi-year journey; and
5. If MH is concerned about Technology Risk, then why doesn't it have a MHEB approved IT Strategy, and why is it seemingly in the initial stages of pre-planning for cloud computing arrangements, without associated business cases.<sup>28</sup>

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<sup>28</sup> Independent report of Darren Rainkie at 37.

## **PART 4 – THE SPIRIT OF ORDER 164/16 HAS NOT BEEN HONOURED**

Order 164/16 directed a number of significant foundational changes in COS philosophy (including moving consideration of issues such as uniform rates and marginal costs to serve to the rate making analysis). What Order 164/16 did not find is that these issues were to be ignored.

Manitoba Hydro appears indifferent to the holistic intent of Order 164/16 in terms of Cost of Service and Rate Design which moves all ratemaking objectives to the Rate Design phase as part of a GRA, whereby consideration is given to costs and factors other than the purely mechanistic output of the PCOSS.<sup>29</sup>

Hydro's application explained that it applied 5 rate design principles, 4 of which merely called for RCCs to be moved into the ZOR. This does not constitute a separate, contextual analysis of proposed rates.

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<sup>29</sup> Independent report of Kelly Derksen at 46, 51.

## **COSS OUTCOMES HAVE BEEN SKEWED BY EXTRAORDINARY EVENTS**

The outcome of the Cost of Service Study have been skewed by a record year in the export markets, completion of major capital projects and drastic industrial load reductions

Manitoba Hydro is proposing to differentiate rates based on PCOSS24 that incorporates the largest Net Export Revenue (NER) in the Corporation's history. PCOSS24 reflects NER of \$1.1 billion.<sup>30</sup>

The residential customer class becomes the catch basin for all of the unintended consequences of a mechanistic COSS in an anomalous year

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<sup>30</sup> Independent report of Kelly Derksen at 25.

## CONSUMERS COALITION RECOMMENDATIONS

The Consumers Coalition is actively considering the evidentiary record including the wide range of outcomes that have been proposed. These include but are not limited to:

- Whether the 3.6% interim rate increase should be confirmed or reduced
- Whether any rate increases are justified in 2023/24 and 2024/25, and if so,
  - One increase or two?
  - 0.5%, 1.3%, 1.5% or other?
- Cost control measures necessary to complement rate changes

## **CORE PRINCIPLES UNDERLYING THE CONSUMER COALITION RECOMMENDATIONS**

The Consumers Coalition will seek evidence-based solutions that:

- Prioritize economy and efficiency
- Are consistent with the existing statutory regime
- Honour the Spirit and Intent of PUB decisions 59/18 and 164/16
- Are alive to the reality that the Strategic Outlook for Manitoba Hydro is likely to be materially altered over the next year
- Respond to the realities and concerns of captive residential ratepayers

**THANK YOU**

