



THOMPSON DORFMAN SWEATMAN LLP

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May 25, 2017

Mr. Kurt Simonsen  
Associate Secretary  
Public Utilities Board  
Room 400, 330 Portage Avenue  
Winnipeg, MB R3C 0C4

Dear Sir:

Re: Process Recommendations to Manitoba Hydro's  
Request for a 7.9% interim rate increase  
Effective August 1, 2017  
Our Matter No. 0147961 AFH

On May 12, 2017, Manitoba Hydro ("Hydro") filed with the Public Utilities Board of Manitoba ("PUB") its 2017/18 & 2018/19 General Rate Application ("GRA") requesting approval of interim electricity rates to be effective August 1, 2017. As requested by the PUB in its letter dated May 17, 2017 this submission provides the Manitoba Industrial Power Users Group's ("MIPUG's") view as to whether the PUB should consider a request for an interim rate process and, if so, what the process should be.

In short, it is the view of MIPUG that Hydro should not benefit from interim rate revenues and should not be permitted to record new rate revenue until the completion of a full GRA process. Consequently, there is no need for the Board to convene a process to review Hydro's filing on an expedited interim basis. Vetting the rate request under a full GRA process is appropriate in that Hydro's GRA rate request is based on a fundamentally changed attitude and philosophy for the utility's finances. Any attempt at a simplified review (as would be appropriate for interim rates) given this change in approach to rate setting would be very challenging. Further it is clear that the delay in timing of the request for rate changes, which was required by December 1, 2016 as per PUB Order 59/16, is of Hydro's own making and there are no significant urgent circumstances underlying the need for an expedited interim rate increase. MIPUG therefore requests that the PUB find that an interim rate increase of 7.9% be denied for these reasons, as detailed further in this submission.

Despite justifiable support to outright deny an interim rate increase, MIPUG recognizes that in the last interim rate Order No. 59/16 the PUB sought to balance the fact that Hydro's interim rate request lacked merit, with the need of customers for some level of predictable and routine rate



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transitions. In the circumstances of today's proposal, MIPUG submits that the Board is in a similar position, needing to balance the failure of Hydro to merit any interim revenues with the interests of customers for measured rate transitions. The two perspectives can be balanced by way of ordering an inflationary increase today (such as 1.6% as the recent Manitoba CPI ) with the revenues being entirely targeted to the Bipole III deferral account. This approach ensures that the rate increase revenues are deferred and remain as a future benefit to ratepayers and not simply a component of Hydro's current revenues.

MIPUG is of the view that the efforts, time and expense of the parties are better spent in focusing on an efficient and prompt determination of schedule and process for the upcoming GRA. Adding an interim rate process to a GRA schedule, even a written process, will delay the full review process and result in duplicative, unnecessary work. It is also not clear how a limited process could be convened to review interim rates, which is not in effect a review of everything that goes into final rates. Controlling hearing expenses is a concern for all parties whether or not they are eligible to receive a cost award.

If the PUB finds value in a process for determining further interim rates other than ordering an inflationary increase entirely targeted to the Bipole III deferral account, MIPUG recommends that it be a written process, focused on what has changed in Hydro's Financial Forecast since the PUB last rejected Hydro's request for added interim revenues in Order 59/16 (based on IFF15).

Detailed comments in support of MIPUG's view on the Interim Rate Increase Request

In its December 18, 2015 submission regarding Hydro's previous interim rate increase request, MIPUG noted that:

Interim rate increases are taken very seriously by MIPUG members, as often these increases are finalized without the same level of scrutiny after the fact as final rate increases given on a prospective basis and considered as "no additional impact on ratepayers" when these revenues are already being collected at the time of the following General Rate Application.

MIPUG also noted that "Awarding interim rates, which are subject to final review and adjustment, results in uncertainty in financial planning for MIPUG members." By August 1, 2017, MIPUG members will have been exposed to interim rates for one year and under Hydro's proposals would face an added interim rate increase for a significant additional period. The interim rates would comprise over 11% of the bill paid by customers. On its face, this is a serious concern and a basis for rejection of Hydro's request.

The PUB, at page 4 of interim rate Order No. 59/16, made it known to Manitoba Hydro that interim rates should only be used for "unforeseen or emergency situations". There is no credible basis to argue that Hydro has or will be in an unforeseen or emergent situation from April 2016 through well into 2018 when a final GRA Order may be issued. MIPUG also notes that Manitoba Hydro has not complied with the following directive of the PUB at page 4 of that same Order:

By this Order, the Board accordingly directs Manitoba Hydro to file a General Rate Application for the 2016/17 and 2017/18 years by no later than December 1, 2016. A December 2016 filing would allow for the adjustment of consumer rates for August 1, 2017. Should Manitoba Hydro



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wish an earlier date for rate adjustments they need to file their Application earlier and allow approximately six months for the for the Board's review of a General Rate Application.

Granting an interim remedy in the face of non-compliance would send a message to Manitoba Hydro that it can ignore PUB directives without consequence.

In support of the above, and without any implied assertion that MIPUG has weighed Hydro's application in full, MIPUG notes the following facts:

1. Hydro's Financial Position: Hydro's financial position for 2017/18, when the interim rates would apply, is materially improved compared to the previous two Integrated Financial Forecasts (IFF14 and IFF15) even with no 2017/18 interim rate increase. In particular note the following:
  - a. In IFF14, Hydro projected that it would require 12.32% in rate increases by 2017/18 over the 2014/15 level, with all of this rate revenue being included in Hydro's revenues for the year (i.e., not deferred) to reach a 2017/18 net income of \$64 million. This was comprised of 3.95% increases in each of 2015/16, 2016/17 and 2017/18. In the hearing reviewing that IFF (the 2014/15 GRA) the Board only awarded 1.8% in new revenues to Hydro (plus 2.15% to the Bipole III deferral account). Clearly, the path towards \$64 million in 2017/18 net income was not compelling to the Board.
  - b. By IFF15, which was reviewed at the previous interim rate application, Hydro continued to project 3.95% increases being needed for 2016/17 and 2017/18, in order to now reach a 2017/18 net income of \$63 million. Note, no adjusting rate increase was required in response to the PUB granting a lower than requested rate increase in 2014/15, but net income was forecast at a similar level nonetheless. Again, the Board rejected Hydro's claims and awarded no new revenue for Hydro, but instead 3.36% towards the Bipole III deferral account.
  - c. In the new IFF16, Hydro now proposes a required 7.9% in increases for 2017/18, in order to achieve a new target of \$111 million net income for 2017/18. Absent the currently proposed 7.9% increase (which totals \$88 million/year in revenue) Hydro would be on track to achieve a net income of \$33 million. In short, Hydro's new proposal is not only seeking to reclaim net income ground that the PUB has implicitly, if not explicitly, previously rejected, it seeks to almost double the previous net income target level for 2017/18 (which was approximately \$63 million) and to achieve this new benchmark via the use of interim rates.
  - d. In addition, IFF16 portrays a scenario with less risk for Hydro than previous IFFs given the following factors:
    - i. IFF16 has better updated capital costs for the new major capital projects, reflecting 16 months of added project spending actuals , and considerable work that Hydro claims to have completed over the past year regarding capital cost forecasts.
    - ii. IFF16 has been prepared with a further 16 months of debt issued, and with actual interest costs locked in. Considering Hydro has been borrowing on the order of \$2.5-3 billion in long-term debt per year , this results in reduced exposure to interest rate changes compared to IFF15.



iii. IFF16 reflects the lowest export price scenario of any IFF since at least 2008 , which means Hydro's export revenues are less dependent on an export market 'home run' than in any previous forecast. As the export market forecast has moderated, so too has the extent to which Hydro is exposed to export price shocks and uncertainties.

iv. Further, it should be noted that IFF16 reflects significantly more inherent financial protection for Hydro compared to these earlier IFFs in that \$119 million/year in rate revenue is being recorded to the Bipole III account (and further increasing to approximately \$135 million/year starting August 1, 2017 if MIPUG's proposals are adopted) compared to only \$36 million/year in IFF14. While these funds are not available to Hydro today for covering current day costs, there is an understanding that these are, in effect, pre-approved revenue increases for Hydro once Bipole III comes into service. In addition, the large deferred balance (now over \$300 million) is a measure of a future revenue guarantee for Hydro, avoiding the need to seek rate shocks it would otherwise have to propose for customers (with attendant uncertainty if these increases may not have been approved).

In short on the financial front, as expected, IFF16 reflects far less exposure to risk than IFF14 or IFF15 . Further, in the event the PUB elects to provide Hydro with no new revenues for 2017/18, the IFF still exhibits a positive net income for this year, which means the year fails the PUB's test for a prima facie case for interim rates (per Order 59/16, page 11):

Adjusting IFF15 accordingly further improves Manitoba Hydro's projected financial situation such that, if the Board were to look at the 2016/17 fiscal year in isolation, no interim rate increase would be required to ensure that Manitoba Hydro achieves a positive net income in 2016/17. As such, the Board is not of the view that Manitoba Hydro has made a prima facie case to receive an interim rate increase that would flow to the company's general revenues.

2. Limited Use of Interim Rates: MIPUG has previously submitted in Interim Rate proceedings, and is still of the view, that interim rates should be awarded only when there is evidence that rate increases are urgently required for short term financial relief, or in the alternative, that there are special circumstances to make such an award. This same view was reinforced by the PUB in Order 59/16 where it noted "The Board is not prepared to consider interim rate applications unless warranted by unforeseen or emergency situations" (page 4). Prior to Order 59/16, Hydro had exhibited a pattern of using interim rate requests to have rates set. Section 48 of the Manitoba Public Utilities Board Act provides as follows [emphasis added]:

Orders involving expense to parties to be after notice and hearing

48 The board shall not make an order involving any outlay, loss, or deprivation to any owner of a public utility, or any person without due notice and full opportunity to all parties concerned, to produce evidence and be heard at a public hearing of the board, except in case of urgency; and in that case, as soon as practicable thereafter, the board shall, on the application of any party affected by the order, re-hear and reconsider the matter and make such order as to the board seems just.



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Interim rates are a challenging but sometimes necessary tool; however, given that they lead to rates being charged that have not been fully or fairly tested, interim rates should be used only in very limited circumstances where there is a real case of short term need or a net benefit to customers. Hydro has failed to demonstrate either situation in this filing (see Attachment 1 for a detailed background on the use of interim rates, which MIPUG has previously filed in regard to Hydro's interim rate increase for September 1, 2012 and April 1, 2016).

Interim rates are by their very definition uncertain. They can lead to Manitoba Hydro charging customers more than what is ultimately granted on a final basis. This has occurred over the course of the past decade, such as the "1% rollback" rate reduction ordered by the PUB (originally from 2010) which was never applied to customer bills; instead a deferral account was set up to collect the funds of this roll-back separately, and ultimately the amount was finalized into Hydro revenues in Order 43/13 rather than to the benefit of customers.

3. Attempted Fundamental Change in Hydro's Attitude: The Hydro filing, on its face, exhibits an attempt by Hydro to impose a fundamental change from IFF15, and similarly from all scenarios and evidence provided by Hydro since the Needs For and Alternatives To (NFAT) review. The fundamental change is not in the numerical values themselves – IFF16 appears to include the usual range of pluses and minuses compared to IFF15, with the added benefits that comes from patience while the utility develops better estimates of capital costs and locks in more and more debt at known (and low) interest rates. In IFF16, these pluses and minuses appear to be largely offsetting compared to IFF15. The fundamental change between forecasts appears to relate to an attempt by Hydro to impose a new attitude and philosophy into the financial forecasts – one that represents a betrayal of the basic compact of the NFAT concept despite no changes in Hydro's constating legislation, Corporate objects, regulations, or Ministerial directives.

The NFAT review was fundamentally an acquiescence among many ratepayers and the PUB that Hydro could move forward with the large new projects, under a model that was an effective quid pro quo that Hydro would continue to apply a measured and patient outlook on its investment and on financially digesting these new legacy assets. The evidence adduced on behalf of Hydro was based on 20 year scenarios for beginning to build equity in new projects that would themselves last 100+ years. Longer term metrics were also advanced by Hydro, and relied on by Hydro, to justify building these major projects.

Hydro's 2017/18 & 2018/19 GRA is in stark contrast to the approach accepted in the NFAT scenarios, and the same approach used earlier to incorporate large assets like Wuskwatim or Limestone. This new approach suggests a preference for aggressive build-up of equity, even during a difficult decade while the largest projects in the corporation's history are absorbed into the asset base.



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MIPUG notes that it will be sufficiently challenging to understand and assess the new Hydro attitude and philosophy at a full GRA. It is not reasonable to think that any meaningful progress could be made in an expedited interim rate review.

MIPUG considers that the most fundamental comfort and confidence in the utility (whether from ratepayers or bond holders) comes from consistency, from governance by laws and policies, not random or frenetic changes in strategic direction due to a new Chair or Board or Senior Executive. The PUB can use the current interim rate request to enhance this confidence by maintaining a commitment to consistency, and to the principles the Board has repeatedly cited, via a rejection of the interim rates.

It is also clear that the current situation, with delays in filing deadlines and rate proposals, is of Hydro's own making. It appears there has been sufficient time for Hydro to engage with all manner of media and community meetings to set out a case for higher rate increases, undertake internal and external consulting reviews and make fundamental decisions on the major projects of direct relevance to rates, but no apparent priority to bring this same information to the PUB until very recently. This delay has resulted in the unreasonable suggestion of an interim rate review. Order 59/16 was very prescriptive in the timing and process Hydro is required to meet for an August 1, 2017 increase to be granted, namely that Hydro had to file by December 1, 2016 to secure an August 1, 2017 increase, and that any August 1, 2017 increase should not be proposed on an interim basis. Hydro has not met these requirements.

Notwithstanding all of the above, MIPUG shares the Board's conclusion in Order 59/16 that measured and predictable rate changes are in the interest of customers. In particular, the Board noted as follows (page 12):

... the Board considers it to be in the public interest to look beyond the test years and mitigate potential rate shock to consumers that, due to the additional costs imposed by Bipole III in a few years, may be inevitable unless the Board implements a form of rate smoothing.




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In light of the above comments regarding the lack of immediate financial pressure, the fact that relying on interim rates in any material way is ill-advised, and the complete inability to test the core of Hydro's case in an interim setting, MIPUG recommends that the Board adopt a measured inflationary increase targeted entirely to the Bipole III deferral account. Such an approach can be suitably linked to Manitoba CPI (1.6% increase) and be viewed as an adjustment in favour of managing customer bill impacts, and not incenting Hydro's disregard of previous Board Orders. Imposing such a rate adjustment need not be rooted in any further review of Hydro's new filing than has been completed to date, on the basis that a cursory assessment confirms that IFF16 is not materially different than IFF15, in that its long-term trajectory inherently requires some degree of rate transition over the coming years.

Yours truly,

THOMPSON DOREMAN SWEATMAN LLP

Per: 

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Encl.

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\*Services provided through A. F. Hacault Law Corporation