

June 9, 2017

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

Dear Mr. Simonsen,

Re: Process Matters: Manitoba Hydro's 2017/18 and 2018/19 General Rate Application

The Public Utilities Board, in a letter to Manitoba Hydro and Interveners of Record dated May 26, 2017, requested the provision of answers from prospective interveners to questions of GRA scope and process matters.

The Manitoba Industrial Power Users Group (MIPUG) submits the following written response to these questions in an effort to assist the PUB and in preparation for the pending Pre-Hearing Conference on June 12, 2017 (and tentatively June 14).

A. How has their client engaged its stakeholders in support of the client's intervention application?

MIPUG is an association of companies who are substantial users of power, in the General Service Large rate classes (including all three subclasses). This group represents approximately 8,000 GW.h of power purchases (about 35% of Hydro's domestic energy sales). This is a somewhat larger mandate than in previous hearings given the scale of issues raised by Hydro's application – the MIPUG banner has broadened by the addition of a few new members, further outreach to relevant companies/associations, and unsolicited approaches from other companies who are not members but who are increasingly concerned about competitiveness despite their smaller power profile than the traditional MIPUG user.

As a result, it is expected that the MIPUG membership proper now makes up somewhat less than half of the consumption of this GSL class.

MIPUG members at this time include:

- Amsted Rail - Griffin Wheel Company;
- Canada Kraft Paper Industries Ltd.;

- Chemtrade Logistics Inc.;
- Enbridge Pipelines Inc.;
- ERCO Worldwide;
- Gerdau Long Steel North America – Manitoba Mill;
- Integra Castings;
- Koch Fertilizer Canada ULC;
- Maple Leaf Foods;
- TransCanada Keystone Pipeline; and
- Winpak Ltd.

The MIPUG intervention, since the 1980s, has always technically had the membership base as the “client”, however intervention has always represented the interests of industrial power uses and provincial competitiveness broadly and generally. This includes future industrial users, and non-members (and, of course, the complementary interests of non-industrial users of power where these users have a similar interest in competitive rates and a well-run, appropriately managed and properly capitalized utility).

MIPUG as a group makes efforts to meet in-person twice a year, as well as regular update conference calls. Most recently this occurred over two days in May of this year, where members were briefed on the Manitoba Hydro GRA that had been filed to date. Members provided instruction on level of participation, priority areas of interest and approach. Participation levels are dependent in part on the potential for PUB approved intervener funding – the group has a smaller overall load directly as members than in recent years, and the scale of impacts on non-members is growing (7.9%/year) – for fairness reasons as well as free-ridership concerns, MIPUG prefers a full intervention with costs appropriately recovered from affected customers of Manitoba Hydro through rates.

Regular updates and conversation occur within the group individually and collectively, led by the MIPUG Chair, Dale Bossons, Plant Manager of Chemtrade Logistics, throughout the GRA process.

Beyond members proper, MIPUG has active engagement with other industrial stakeholders and associations that are not members of MIPUG, especially in light of the increased attention in Hydro’s activities of late. These other parties have an active interest in the outcomes of this proceeding, are impacted in a similar manner as MIPUG members and often are aligned with MIPUG in matters of priorities and positioning.

In particular, in respect to the current proceeding, MIPUG hosted many non-members for a significant part of the May semi-annual meeting where briefings on the Hydro GRA and PUB process occurred. Also there has been considerable outreach and discussion with

many related parties such as the Canadian Manufacturers and Exporters – Manitoba, the Mining Association of Manitoba, and the Manitoba Chambers of Commerce.

B. How, and on what issues, has their client collaborated with other prospective interveners?

In regards to this GRA, MIPUG has met with counsel for the Consumer's Coalition a number of times and plans to collaborate significantly for this hearing, in light of the breadth of issues to cover. Specific issues on which collaboration will take place is still being discussed. In general, MIPUG plans to collaborate with the Coalition in a few key areas:

1. Areas of special interest outlined in the Manitoba Order In Council No. 00092/2017 including Hydro's planned capital expenditures and priorities for major capital projects and base/sustaining capital and Hydro's access to capital and implications of increased borrowing requirements;
2. Hydro's abrupt change from the long established financial strategy and formulation of proposed rate increase forecasts;
 - a. Long-term debt/equity ratio and approach to use of financial targets,
 - b. Purpose of a crown-owned hydroelectric utility, and
 - c. Regulatory policy and the mandate of Hydro as set out in the Manitoba Hydro Act.
3. Priority areas typical of a GRA that both MIPUG and Coalition have been reviewing for some time such as;
 - a. Review of Hydro's financial forecast results and implications (including interest expense, forecast exports, cashflow, level of reserves, risks, etc.),
 - b. Depreciation methodology and implementation of 'IFRS-compliant' standards for rate regulation (including proposals to establish deferral accounts in rates),
 - c. Review of OM&A forecasts in light of Hydro's cost cutting measures, and
 - d. Hydro's debt management strategy.
4. Direct and indirect economic impacts of Hydro's new financial plan; and
5. Other areas that may be identified after further review of Hydro's GRA and the PUB issue list.

C. What is their client's initial position with respect to Manitoba Hydro's GRA?

Fundamentally, MIPUG believes that Manitoba Hydro rates should be cost-based and reflect the provisions of section 39(1) of the Manitoba Hydro Act. This applies to all classes.

As of April 29, 2016, when Board Order 59-16 was issued, it was already clear that Manitoba Hydro's 2017/18 GRA would be a major undertaking, beyond a "normal" GRA as has occurred in recent years.

For "normal" GRAs, MIPUG notes that the previous Hydro GRA (2014/15 and 2015/16) was a large undertaking, comprising 19 hearing days, the one before (2012/13 and 2013/14) taking 23 days. All participating parties are well versed in the scope of these rate reviews. These reviews included all manner of topics related to forecasts (financial, load, capital, export price, interest rate, etc.), financial policies (depreciation, IFRS, overheads), and plans for the utility (resource plan, DSM, capital).

By the time of Board Order 59-16, parties were already aware that the 2017/18 GRA would encompass far more topics than the recent normal GRAs:

- Parties were aware that Hydro would finally have a review of the Cost of Service (COS) methodology completed, such that COS results could be used to implement rate changes. Also delayed until the COS methodology was reviewed, rate designs such as conservation rates were slated to be part of the 2017/18 GRA. COS was not a topic of discussion at the previous 2 GRAs.
- Hydro had finally brought forward a useful risk analysis approach in the Interim Rate review, which had been desired by the Board since at least 2009. While these materials were not included in the scope of the interim rate review, it was expected this would be a major focus of the 2017/18 GRA.
- Hydro was already proposing changes to its financial targets in the interim rate review (including the KPMG study), which under normal GRAs are basically applied unaltered. A review of these targets was also deferred to the 2017/18 GRA.
- Hydro was expected to file a full Asset Condition Report in response to PUB directives, to support a review of "pacing and prioritization" of capital spending, which had been absent in previous GRAs.

Despite this GRA already heading towards an unusually large scope, two major events have expanded the scope:

- **The decision by Hydro's new Board and Management to attempt to fundamentally alter the attitude and approach to the Corporation's core mandate and purpose in respect of finances:** The deeply flawed understanding of Crown corporations and their capital structure, regulated utilities, capital intensive industries, and the source of Hydro's existing equity is a significant shift from all past Hydro rate reviews for many decades. In particular, (a) the attempt to achieve target equity levels within an accelerated 5-10 year window while major capital projects are being newly put into service, and (b) new cash flow targets that seek to generate significant surplus cash for debt repayment on an advanced schedule, are major changes compared to all past rate hearings, including the Needs For and Alternatives To (NFAT) review which closely examined the reasonableness of Hydro's financial forecasting methods specifically in the context of these specific major capital projects.
- **OIC 92/2017:** which indicates capital expenditures should be considered as part of the current GRA, and Hydro should make available to the Board all necessary information to consider these expenditures.

At present, MIPUG's position can be summarized in five parts:

1. **PUB Role:** The Board must provide consistency and predictability to ratepayers, and comprehensively continue with the overall trajectory of regulatory oversight and financial plans that have been put in place since before the NFAT review.
2. **Normal GRA:** A serious and comprehensive examination is required, in light of all past Board directives and highlighted issues, of whether 3.95% rate increases into the future are indeed required. MIPUG considers that (a) the underlying facts available in this filing (as reviewed to date) do not, in aggregate, indicate a fundamental change from the financial projections that underpinned each of the last few Integrated Financial Forecasts, and (b) that the previous 3.95% rate increase scenarios were based on flawed and overly conservative scenarios, or excessive cost assumptions, for matters such as normal capital spending and DSM, financial policies, etc. A comprehensive review will in likelihood align with the Board's conclusion during the more limited review in Order 59/16 that 3.95% annual increases are not required, scaling back the 3.95% request at that time.
3. **Hydro's changed attitude and approach to finances:** The attempt by Hydro to fundamentally alter the financial approach must not be accepted without a critical review of the consistency of this view with the objects and purposes for the Corporation set out in the Manitoba Hydro Act, the appropriate way to integrate major capital spending into a regulated capital-intensive utility, credible risk scenarios over an appropriately long horizon, the scale of payments already being made to the Provincial Government that this approach is meant to "protect", and the

underlying premise of the NFAT review as to the pace and patience for integration and payback of major new capital into Hydro's financial targets. On each of these matters, MIPUG expects the new attitude and approach will be shown to be fundamentally flawed, and based on an incomplete and inappropriate set of financial metrics drawn from experiences not related to Manitoba Hydro.

4. **OIC scope:** MIPUG views that the fundamental effect of the OIC is to mandate document production from Hydro. In particular, section 1 of the OIC sets out nothing different than existing practice (capital expenditures have always been a factor in the Board's Orders setting Hydro's rates). It is section 2 ("...Hydro shall provide...") that is new and explicitly stated – that there is to be no further objections and obfuscation from Hydro from providing the Board with a set of information that the Board considers is required to assess capital expenditures. In short, in MIPUG's submission, the OIC does not suggest a new mandate for the Board nor new duties or powers that it did not previously have, nor is the OIC a directive for forensic investigation of "what went wrong". It is simply a clarification, aimed at Hydro, to ensure no further delays or objections occur in respect of document production.

5. **Other matters:**

- a. COS study results should be applied: MIPUG considers the results of the COS hearing (subject to final confirmation of implementing the Board directives correctly) to be useful and reasonable for determining a fair allocation of Hydro's costs. In fact, MIPUG can see no reasonable basis for delaying taking what are now accepted to be reliable COS results into account when setting overall class rate levels.
- b. Alternative rate designs need to be explored: MIPUG will be canvassing options for industrial customers to control their costs through existing or possible new rate designs, particularly in light of the extreme cost pressures resulting from Hydro's rate proposal.

Also see MIPUG's submission in respect of interim rates May 25, 2017 regarding the material improvements over the last GRA's financial projection (IFF14), including projected financial implications of various risk factors (drought, interest rate increases, etc.).

MIPUG's key concerns are that rates are cost-based, stable, and predictable, regulated on a transparent basis, and fair to all classes of customers. Cost-based electric power is a factor which can provide a competitive advantage and help attract investment, jobs, and benefits for communities and business in the province, consistent with the overall intent and purpose of a Crown-owned Manitoba Hydro. MIPUG members have been faced with large rate increases over the past 10 years, and the majority of MIPUG members are unable to pass the impacts on to customers as these companies are price takers in their respective market. Electricity prices can also adversely affect potential expansion decisions.

D. What aspects of Manitoba Hydro's GRA do their client agrees with and why?

MIPUG is supportive of Hydro's efforts at putting forward a full GRA for review, despite the delayed timing. MIPUG agrees that a full GRA review is required.

MIPUG agrees that a GRA should consider both the financial health of the utility and the impacts on customers. Unlike the OIC, which portrays these two aspects as being in competition (e.g., that the PUB must "balance the interests of ratepayers and the financial health of Manitoba Hydro"), MIPUG agrees with Hydro's general comments in Tab 2 that rate increases should be viewed from the perspective that the two are complementary. In MIPUG's view, ratepayers and Hydro share an interest in competitive rates and a financially healthy utility:

Ratepayers:

- It does not serve customer interests to have a utility that is financially unhealthy, where adverse events, such as a drought, could lead to rate shocks or major deterioration in the quality of service. Rates should be high enough that they can maintain stability and predictability in the face of reasonable risk scenarios.
- It does not serve customer interests nor is it consistent with past rate setting practice and policy, to fund shareholder equity in Hydro beyond that needed to provide appropriate reserves towards rate stability as described in the *Manitoba Hydro Act* section 40(1).

Manitoba Hydro:

- It does not achieve the interests of financial health for Manitoba Hydro to impose rate increases that undermine the profitability of Hydro's business customers, drive loads outside the province, and leave unsold hydraulic power to be dumped into export markets at low prices. This is particularly true at a time with large hydraulic surpluses.
- It does not serve the interests of financial health for Manitoba Hydro to set rates so high they generate large net incomes and equity levels such that, even in the face of extreme adverse risk scenarios, Hydro demonstrates positive contributions to "reserves". Further, under conditions where Hydro's net income is not at risk under almost any occurring scenario, what is the purpose of reserves?
- It does not achieve the interests of financial health for Manitoba for Hydro to pay substantial sums to the province for debt guarantees where Hydro imposes effectively no risk (including cost or adverse impact whatsoever) on the guarantors

debt ratings. Large fees paid to a counterparty who experiences no net costs to provide the service are not part of the framework for a financially healthy company.

Despite the fact that MIPUG agrees with Manitoba Hydro on the importance of considering impacts on customers, MIPUG is disappointed that the Hydro GRA includes basically no information on the impacts on industrials, business competitiveness, nor load response. Hydro specifically does not include “elasticity” impacts in the GRA. This is particularly striking in the current GRA in that Hydro asserts its debt levels could be problematic for the provincial economy and provincial finances. However, Hydro provides no information or data on the impacts on the provincial economy or finances of pulling significant dollars out of ratepayers pockets at the expense of other possible uses for this money (such as stimulating economic growth), nor on the impacts to the provincial economy of reduced business investment or plant closure due to decreased competitiveness from onerous compounding rate increases.

MIPUG is supportive of Hydro finally responding to the longstanding PUB concerns over staffing levels (going back to at least Order 116/08 in 2008). In particular, Order 5/12 noted that from 2004 to 2011, Hydro’s staffing complement grew by 15% (over 900 Equivalent Full-Time positions (EFTs), from 5,769 to 6,669) despite no major change in overall Corporate duties. Note that a further 233 increase was seen by 2015/16 (to 6,902) per the 2016 interim rate filing Attachment 34.

MIPUG is particularly supportive of Hydro’s work in Tab 4 of the GRA to significantly enhance the ability to analyze and portray projections of the Corporation under scenarios of risk and uncertainty. This has been a longstanding initiative of MIPUG and the PUB to get Hydro to take on more advanced risk modelling. MIPUG is pleased to see that it has reached a product that can now be assessed and tested. However, MIPUG also considers that assessing the scenarios over a 10 year horizon is misguided. The most critical horizon of concern at the present time has to be the next 4 years, after which the exact costs for major borrowings and major capital projects will be known and thus many of the currently cited risks will be resolved. The second most critical period of concern has to be the 20 year horizon that considers not only the very challenging years of integrating new projects, but also the years where those projects start to generate revenue and provide other benefits (such as decreased drought risk), which are the very route contemplated for starting to have the projects paid off. This 20 year horizon is of particular relevance given the purpose of this type of risk modelling and to ensure impacts on intergenerational equity associated with 100+ year assets are considered.

MIPUG is pleased with Hydro’s inclusion of the Cost of Service results in the current GRA. It is beneficial to draw to a close the Cost of Service proceeding directives. MIPUG is disappointed that the results of the Cost of Service study have not been applied in determining differential rate increase scenarios. MIPUG expects to pursue this area during the hearing.

MIPUG agrees with Hydro that the timing is not appropriate for introduction of any mandatory time-of-use rate for industrials.

E. What aspects of Manitoba Hydro's GRA do their client disagree with and why?

MIPUG fundamentally disagrees with Hydro's attempt to impose a new attitude and approach to the Corporation's core mandate and purpose in respect of finances. MIPUG views that the direction imposed by Manitoba Hydro's new Board and Management is deeply flawed in its understanding of the purpose of Crown utilities, of the function of regulated utilities, of the proper financial management of capital intensive companies, and of the appropriate response to periods of major capital investment by companies such as Hydro.

As an example to the change in financial strategy, in the NFAT review Manitoba Hydro projected rate increases that achieved financial targets in a 20 to 30 year timeframe, viewing these targets as more flexible during periods of intensive capital investment:

[I]t's always been recognized that the targets may not be obtained during periods of major investment in a generation and transmission system and that ratios will necessarily weaken during those periods of investment.

Credit-rating agencies and other stakeholders are prepared to accept short-term weaknesses in financial ratios due to the investments in revenue-generating assets as long as Manitoba Hydro can demonstrate steady progress towards those targets over the long-term.¹

MIPUG disagrees with Hydro regarding the scale of risk at this time. Hydro continues to issue large quantities of new debt at locked-in long-term interest rates; updated capital cost projections are based on increasingly known conditions and include greater portions of spent versus budgeted costs. Within 4 years, these values will be entirely locked in, and revenues will begin to flow from Keeyask. The breadth of risk scenarios will continue to narrow as more of these variables are locked in. The appropriate mature outlook at this time is for consistency, responsible adherence to established plans, and patience.

In light of this responsible view of Hydro, MIPUG submits that not only are 7.9% rate increases not required or factually supported, but the previously proposed 3.95% increases need to be critically assessed and likely not awarded in full.

MIPUG is also of the view that Hydro has failed to put forward any serious efforts at assisting industrial customers with competitiveness concerns. This includes new alternative rate designs that could help industrial customers manage their overall energy cost, as are common in other jurisdictions. This also includes consideration of how to use the conclusion

¹ Testimony of previous CFO, Mr. Darren Rainkie, NFAT Review transcript, March 19, 2014, page 2736.

that industrials are paying well above their level of costs per the COS study (even before the newly proposed rate increases) to help alleviate pressures on this class.

F. On what specific issues is expert evidence being planned and why?

MIPUG intends to call expert evidence on the issues identified in question B above, as well as D and E. This relates primarily to (a) ongoing and normal GRA topics MIPUG has traditionally pursued (including financial forecasts, capital spending, implementation of Cost of Service results) and (b) broader questions of Hydro’s purpose, role and objects and the attitude change Hydro is proposing to impose, which is completely responsible for the increases in Hydro’s proposed rates. This is a major issue of importance to members and Manitoba industry generally.

G. How many rounds of Information Requests of Manitoba Hydro are requested in light of the MFR Responses? How many Round One Information Requests (including sub-parts) is the Intervener expecting to ask of Manitoba Hydro?

MIPUG expects two rounds of information requests will be required to protect the necessity of follow-up questions if responses from the first round so require.

MIPUG has always sought to be efficient with the number of information requests, and despite the fact that MIPUG submits a full scope intervention in Hydro’s GRA, has repeatedly worked to focus and prioritize the Information Requests sought in order to keep the number of questions to a minimum. In MIPUG’s view, this increases the likelihood that Hydro will produce thorough and thoughtful answers to the questions posed. In support, MIPUG notes the following table from Hydro’s February 23, 2015 letter regarding Information Requests in the 2015/16 GRA to the Board:

<u>2015 GRA</u>		<u>2012 GRA</u>		<u>Increase/(Decrease)</u>
PUB	256	PUB	487	(231)
Coalition	423	CAC	565	(142)
MKO-Coalition	57			57
		CAC-GAC	43	(43)
GAC	250	GAC	171	79
MIPUG	90	MIPUG	157	(67)
MMF	217			217
City of Winnipeg	9			9
MKO	40			40
TOTAL	<u>1342</u>		<u>1423</u>	<u>(81)</u>

MIPUG encourages the Board to ensure parties have the full right to pursue issues that are of interest. MIPUG cannot estimate the precise number of IRs it may issue, but does expect

that the current scope will require somewhat more than in the two hearings referenced above.

MIPUG will minimize Information Requests to the extent possible to ensure efficiencies in the process.

H. What topics does their client identify as being issues for this GRA, the scope of those issues and why?

Please see the response to question B, D and E above.

While the Manitoba Order-in-Council 92/2017 has highlighted capital expenditures as an area for review, these expenditures are long-term in nature. Further, while certain retrospective and potentially forensic reviews may be necessary at an appropriate time, it is not clear that this form of review would be a major factor informing the Board on its primary task – how to set rates going forward.

The remainder of MIPUG's primary issues appear to be largely set out adequately on the issues list circulated by Board Counsel. The only exception is ongoing review of issue scope driven by the Intervenor Applications submitted by other parties. MIPUG continues to review these submissions and the purpose and focus set out by the other parties and will offer any necessary comments in this regard at the Pre-Hearing Conference on June 12.

I. What, if any, position does their client take on the proposed schedule for the hearing of this GRA?

MIPUG has reviewed the draft timetables proposed by each the Board's Counsel and Manitoba Hydro and takes the following position on process and timing:

- The major difference in timing between the two timetables is in relation to the filing date of Manitoba Hydro's remaining application materials and responses to capital-related MFRs. As Hydro proposes to file these Wednesday June 21, 2017 the filing of Round 1 IRs as proposed by Board Counsel for June 29 is in MIPUG's perspective excessively tight. This could be exacerbated depending on the PUB's schedule for the overlapping interim rate increase process.
- Both schedules propose Round 2 IRs within the process and MIPUG agrees with the inclusion of Round 2 IRs within this process. For timing, MIPUG expects the two weeks between Round 1 answers and Round 2 questions is reasonable as long as Manitoba Hydro has completed responses by the filing date (in the past Hydro has submitted some responses at a later date which does not leave interveners sufficient time to consider before drafting Round 2 questions).

- The Board Counsel timetable proposes a tentative technical conference. MIPUG is not of the view that such a session is necessarily of benefit given the scale of effort required to undertake such a session.
- MIPUG agrees with Hydro's proposed timing for Intervener Evidence of at least two weeks following receipt of Round 2 IR responses as adequate. Board Counsel proposed timing of six working days is excessively tight. Again this is based on the caveat that Hydro has filed all Round 2 IR responses by the due date.
- Neither schedule has explicitly included written argument as a specific step in the process. MIPUG's experience is that the Board benefits most when parties are given the opportunity for written argument. MIPUG has consistently been informed that well referenced written arguments allow the Board to easily understand and follow the intervener positions and make the Board's job easier in preparing its Order.
- Both schedules are probably overly generous for intervener experts to answer IRs (2 weeks). Interveners don't typically get that many IRs and they are usually not time consuming to answer. Allocating this extra time to prepare the evidence is far preferred over more time to answer IRs. Further, with respect to the Board's schedule, we do not see a need to prospectively schedule an IR motions day for questions to interveners (Oct 18). MIPUG can't recall there ever being an issue with questions posed to interveners that required PUB resolution.
- The Board Counsel's schedule assumes interveners require Hydro's rebuttal evidence 3-4 weeks before the hearing starts. Hydro assumes 4 days. MIPUG agrees with Hydro's more realistic scheduling – there normally isn't much time needed to review and assess rebuttal evidence prior to a hearing.