CENTRA GAS MANITOBA INC.
2019/20 GENERAL RATE APPLICATION
BOOK OF DOCUMENTS
AUGUST 15, 2019

TAB 1

CPA MANITOBA CODE OF PROFESSIONAL CONDUCT

PUBLIC PROTECTION 25 202 Integrity and due care and Objectivity

RULES: 202.1 Integrity and due care

A registrant shall perform professional services with integrity and due care.

202.2 Objectivity A registrant shall not allow his or her professional or business judgment to be compromised by bias, conflict of interest or the undue influence of others.

GUIDANCE - Rule 202

1. A person who acts with honesty and truthfulness and whose actions, values and principles are consistent is described as having integrity.
2. Objectivity is a state of mind, which has regard to all considerations that are relevant but disregards those that are not. An objective person does not allow bias, conflict of interest or the influence of others to compromise judgment. The judgment of an objective person is intellectually honest. Objectivity should not be confused with neutrality or impartiality.
3. Objectivity and integrity are two of the five fundamental principles of ethics, as stated in the Preamble to the CPA Code. These two principles are closely related and they are essential ethical elements in establishing the credibility of a registrant. Objectivity is essential for any registrant to exercise professional judgment and act with integrity whether in public practice or elsewhere.

....

Objectivity and advocacy

8 . The requirement for an objective state of mind does not preclude a registrant from acting in an advocacy role for a client or from working to advance the best interests of an employer. A registrant's effectiveness as an advocate in these cases is based on professional credibility, which is sustained by objectivity and integrity in addition to competence. However, a registrant must consider the ability to effectively advocate the client's or employer's position, while still maintaining objectivity and integrity. It may be possible to

do so when the advocacy role is apparent in the circumstances and the position being advocated is supportable. In any advocacy service, there is a possibility that circumstances may arise which stretch the bounds of performance standards, go beyond sound and reasonable professional or commercial practice or compromise credibility. Such circumstances may pose an unacceptable risk of impairing the reputation of the registrant, client and/or employer. In those circumstances, the registrant should consider whether it is appropriate to perform the service.

9. When acting as an advocate a registrant should bear in mind other provisions of the CPA Code, such as Rules 203 and 205. Rule 203 requires a registrant to sustain professional competence in relation to all professional services provided by the registrant. Rule 205 provides that a registrant may not associate with any letter, report, statement or representation which the registrant knows, or should know, is false or misleading.

10 A registrant, when acting as an advocate, should ensure that such an advocacy role does not constitute the practice of law.

204 Independence

R**ULES: 204.1 Assurance and Specified Auditing Procedures Engagements**

A member or firm who engages or participates in an engagement:

(a) to issue a written communication under the terms of an assurance engagement; or

(b) to issue a report on the results of applying specified auditing procedures; shall be and remain independent such that the member, firm and members of the firm shall be and remain free of any influence, interest or relationship which, in respect of the engagement, impairs the professional judgment or objectivity of the member, firm or a member of the firm or which, in the view of a reasonable observer, would impair the professional judgment or objectivity of the member, firm or a member of the firm.

Advocacy Threats

33 An advocacy threat occurs when a firm, or a person on the engagement team, promotes, or may be perceived to promote, an assurance client's position or opinion to the point that objectivity may be, or may be perceived to be, impaired. Such would be the case if a person on the engagement team were to subordinate his or her judgment to that of the client, or the firm were to do so. Examples of circumstances that may create an advocacy threat include, but are not limited to: • dealing in, or being a promoter of, shares or other securities of an assurance client; and • acting as an advocate for or on behalf of an assurance client in litigation or in resolving disputes with third parties.

TAB 2

established some years ago in respect of Centra Gas, sir?

MR. DARREN RAINKIE: It brings a tear to my eye, Mr. Peters, when I look at this one. This is exactly the same spreadsheet that I created in 1995, and it doesn't even look any different. It hasn't even changed in terms of the formatting, so it's just been updated over the years.

MR. BOB PETERS: All right. Well, you can autograph mine later. But this was established back in 1995?

MR. DARREN RAINKIE: Yes, between 1994 and 1995. I think it's part of the 1995 test year.

MR. BOB PETERS: And, Mr. Rainkie, the -- the spreadsheet that -- that has been developed by you and is now owned by Centra, it adjusts the allowed return to the Utility based on a formula that was settled on back in 1995?

MR. DARREN RAINKIE: Yes, a very different place and time, a very different interest rate environment it was set, Mr. Peters.

MR. BOB PETERS: While it's -- it's different for Centra Gas Manitoba Inc., but, Mr. Rainkie, but for our neighbours to the west, wouldn't most every other gas utility in Canada be using a

rate-based rate of return methodology?

MR. DARREN RAINKIE: Certainly the -- yeah, the inv -- the investor owned utilities usually use that kind of a methodology. Cost of service is more consistent with, you know, a Crown corporation.

MR. BOB PETERS: And the cost of service methodology, as you mentioned before, is a process the Board has migrated to in terms of setting of the rates. But it still does a calculation under the rate-based rate of return to at least provide a measure as against what -- what it's finding on the cost of service side.

MR. DARREN RAINKIE: I think that would be a fair summation, Mr. Peters.

MR. BOB PETERS: And back in 1995, Mr. Rainkie, the allowed return on equity was established at 12.12 percent, according to this schedule?

MR. DARREN RAINKIE: That's correct.

MR. BOB PETERS: And then there was supposed to be an adjustment made, and that was going to be the difference between the thirty (30) year forecast bond rate, and the thirty (30) year rate that was in effect in 1995?

MR. DARREN RAINKIE: Yes, that's correct.

MR. BOB PETERS: And instead of taking a hundred percent of that rate change, the formula mitigated that by taking only 80 percent of that change, whether that change was up or down?

MR. DARREN RAINKIE: I'm not sure it mitigated it. It just was based on, at that point, an understanding of some empirical evidence about the relationship between the change in rate of return and the change in the overall interest rate environment. I keep saying "at that point in time," because I think in terms of what we've gone through in the last three (3) to five (5) years, that this -- this number of 6.89 percent that we have here doesn't make any -- much sense any more.

But -- but that was the general concept, that utility boards were tired, year after year, of having rate of return capital structure discussions. They tended to be very long, costly affairs with experts coming in and arguing back and forth with different opinions. So in about 1994, I think it was, there was a move in the industry to try to find some -- a formula-based approach of setting this. And then at maybe every five (5) years or so, we would have the full, you know, full review.

Of course, we've kept this calculation

and haven't adjusted it over the years because as we moved to cost of service it didn't make sense for us to spend a bunch of money, time, and energy trying to update this calculation any -- any longer. We continue to produce it every year, but to me it's kind of -- you know, obv -- obviously, and I think you've seen our evidence in the Information Request. It's kind of -- this calculation has kind of fallen by the wayside and it's really outdated. I don't -- I don't think anybody would expect that, you know, a 6.89 percent return would be a fair return.

Because, let's face it, the re -- the reduction in interest costs have a lot to do with government policy in terms of trying to -- this is maybe a prelude to some of the discussion with Mr. Schulz, but obviously monetary policy has been there in terms of trying to encourage in -- investment.

So just because central banks are holding down interest rates doesn't mean your required rate of return would drop. And what other jurisdictions have been doing is adjusting that 80 percent formula, recognizing that there isn't such a high correlation between changes in interest rates and -- and rate of return.

MR. BOB PETERS: Well, Mr. Rainkie,

TAB 3

marked as Exhibit Centra-16. So we are in your hands as to when you want to proceed.

--- EXHIBIT NO. CENTRA-16: Direct evidence of Centra Gas

MS. MARILYN KAPITANY: I just have question. If either Mr. Czarnecki or Mr. Rainkie, or you may just have answered my question, but I hear all of the people here saying what parts they have in gas.

Can you just tell me: Who would have overall responsibility for a decision related to something in Centra Gas?

MR. DARREN RAINKIE: Ms. Kapitany, the gas side of the business is fully integrated with the electric side of the business, so all of the executive members of Manitoba Hydro are also executive members of Centra Gas. So the functional responsibility for gas supply reports to Mr. Kuczek, and -- and -- but it's the same executive committee that would review significant proposals, and -- and approve those proposals.

MS. MARILYN KAPITANY: So it would be Mr. Kuczek then that would take the -- the various roles that we've just heard about here, bring them all

together, and then talk about them with the executive team?

MR. DARREN RAINKIE: That's correct, as well as the Board as well, based on our approval levels for what has to go to the executive committee and the Board.

MS. MARILYN KAPITANY: Thank you.

MR. DARREN RAINKIE: Good morning again, Mr. Chairman. I see that at least the monitors are working on this side, and the big red button is lite so I assume everybody has our presentation in front of them, and we can commence.

So Centra is pleased to appear before the Public Utilities Board today in support of its 2015/'16 Cost of Gas Rate Application. As a public utility, Centra believes that it is essential to clearly explain the need for rate changes to the Public Utilities Board, stakeholders, and customers. This public process is an important part of that communication process.

In this Rate Application, Centra is requesting approval of changes to its supplemental gas transportation and distribution rates to be effective November 1st, 2015. Centra is not applying to change its primary gas rates at this point in time. Centra

will file a Primary Gas Rate Application around the middle of October, as is the normal course, for implementation on November 1st, 2015. And we'll file combined rate impacts with the PUB at that point in time. Centra is not applying to change its non-gas costs in this application. That is accomplished through periodic general rate applications, as the financial circumstances dictate.

So, Mr. Chairman, my portion of the presentation this morning will be uncharacteristically short. The circumstances that underpin this rate application are very technical in nature, to say the least. But as a policy witness on the panel, I did want to provide a brief overview of the corporate perspective on this application and the circumstances that bring us before the PUB today.

As was the case with the recent electric general rate application, we think that it's important to start at the strategic level by considering Centra's mandate, which we've outlined on the chart in front of us. Which is to require, manage, and distribute supplies of natural gas to serve Manitobans in a safe, reliable, cost-effective, and environmentally appropriate manner.

Providing natural gas service to

Manitoba customers not only involves managing costs, but most importantly, ensuring safe and reliable service. In the absence of safe and reliable service of an essential commodity such as natural gas, rates become a moot point. Centra takes all aspects of its mandate seriously, and by necessity needs to balance all of the objectives that you see on the chart to provide value to its customers.

It is within this context that Centra makes decisions on behalf of customers as they relate to customer service, gas supply, and rates. We believe that these objectives are also important considerations for the Public Utilities Board with the respect to the rate-setting process. We are confident that the evidence that Centra witnesses will provide over the next few days will demonstrate that Centra has been very successful in fulfilling this mandate during the gas years that are under examination at this rate proceeding.

This success will be demonstrated in three (3) key ways. First, Centra has a reliable, cost-effective portfolio of assets to ensure security of supply, and to provide diversity to manage risks. For reasons that will be elaborated on later in the presentation, the characteristics of the Manitoba

TAB 4

Excerpt from section *IFRS 10 Consolidated Financial Statements*

Uniform accounting policies

B87 If a member of the group uses accounting policies other than those adopted in the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to that group member's financial statements in preparing the consolidated financial statements to ensure conformity with the group's accounting policies.

TAB 5

DR. HUGH GRANT: Could I -- could I just go back to slide 49 just for a moment? I'm just curious, the main driver in it between the MH-13 and the MH-14 forecast was the decline in projected earnings -- net earnings over the next decade.

Is -- do you know what that's related to?

MR. DARREN RAINKIE: Yes. The -- the -- once we get past the first few years of the forecast, the -- there's higher carrying costs as a result of the higher cost of Bipole III and Keeyask, as well as -- I think there's -- if I remember correctly some deterioration in export prices in that time frame.

DR. HUGH GRANT: All right, thanks.

MR. DARREN RAINKIE: Those would be the key reasons.

(BRIEF PAUSE)

MR. DARREN RAINKIE: So the second view or concern that is expressed from stakeholders is, why shouldn't Manitoba Hydro's rate increases be limited to inflation? You know, somewhere around the 2 percent level currently.

So these charts show -- compare, rather,

the projected net income and the projected retained earnings. The projected net income on the left, projected retained earnings on the right, of our forecast with 3.95 percent rate increases in the dark blue and with 2 percent rate increases, being the current level of inflation, in the light blue.

The difficult part with that view is that the projected increases in the revenue requirement are driven by the extensive investments, and capital to be made on it on behalf of customers. They are not inflationary cost pressures, so trying to match up a revenue stream based on inflation with a cost line that is not moving at inflation is -- is not going to work.

With 2 percent rate increases, financial reserves would be all but depleted by 2024, and this situation would jeopardize our ability to provide rate stability to customers as we'd be unable to recover our real costs of providing service and ensure financial services -- financial -- sorry, sufficient financial reserves are in place.

So this -- this slide, slide 52, was projected net income and projected retained earnings with both our 3.95 percent and comparing that to 2 percent rate increases, but the slide that follows is the -- is the equity ratio comparison for those same

scenarios.

And you can see that with 2 percent rate increases in the next decade, our equity ratio would essentially be approaching zero by the time the -- the decade is done. You can see in the far-right side that that -- that data point is probably 2 or 3 percent equity, so we'd be essentially funded by 100 percent debt at that point.

And then slide 54, which is unfortunately not marked, provides the projected interest cover and capital coverage ratios under those same two (2) scenarios. And you can see that -- with 2 percent rate increases in the yellow -- sorry, in the light blue bars, that both interest and capital coverage ratios would be well below our one point two-o (1.20) targets. They would be, you know, largely in the range of point four (.4) to point six (.6). Just averaging over that ten (10) year period. So we would simply not -- be not generating enough income or cash to meet our debt servicing requirements or to fund our sustaining capital expenditures.

Now, I've mentioned throughout the presentation that, if you think back to the revenue requirement graph that was doubling over the next ten (10) years from 1.5 to $3 billion, I mentioned that our

operating costs were not contributing in a large way to the 3.95 percent rate increase level. And I've just mentioned that what's driving our cost line right now is not inflation cost pressures, but rather the carrying costs of capital investments.

But obviously a matter that's always a concern of -- of both interested parties and the Board is: How well is Manitoba Hydro doing at managing its own house, its own affairs, before it comes requesting rate increases?

So Manitoba Hydro has always been committed to carefully managing it -- its costs and utilizing resources efficiently and effectively. As part of those efforts, we undertook an extensive review of our staff complement in the -- in 2014. And this process was from the executive committee right on down and was started by the executive committee and carried out by the executive committee and all the management of Manitoba Hydro.

And that process resulted in plans to reduce approximately three hundred and thirty-three (333) -- sorry, three hundred and thirty (330) operational positions over the next three (3) years while at the same time maintaining service levels.

There's a typo on this graph, but that

reduction of three hundred and thirty (330) operational positions represents about 8 percent of the current equivalent full-time employees that are charged to operating costs.

I would also note that Manitoba Hydro has a target in its forecast to limit operating cost increases to 1 percent over the ten (10) year period. So while the three hundred and thirty (330) operational position reduction will allow us to meet those targets in the next three (3) years, we also have that 1 percent target going out into the end of the decade.

So just mathematically, if the three hundred and thirty (330) operational position reductions gets us through the next three (3) years, allows us to meet that target, some of the calculations we did in the recently filed Information Requests indicate that we would need reductions in the order of an additional six hundred (600) reductions to 2022/'23 in order to make the 1 percent target that we've set.

So that represents currently then, you know, eight (8) times three (3), almost 24 percent of EFTs charged to operations. So that is no small -- no small commitment to cost containment. That is a large stretch target for Manitoba Hydro.

So consistent with this plan, we see in

this chart that shows a comparison of capital construction EFTs, so those -- those folks that work on capital projects, operation and maintenance EFTs, and governance and support EFTs.

And we see that, consistent with our plans, you see the blue bars which are capital construction EFTs are going up during this period of intensive capital activity, as you would expect.

You can also see the red bars and the green bars which represent those staff members that are charged to operating and administrative costs are declining, consistent with our plans to reduce positions.

Now, there has been some concern that Manitoba Hydro wouldn't deliver on this commitment. And I can indicate to you that, in the first year, our progress has been excellent. We've actually been able to exceed the targeted reductions for the 2014/'15 fiscal year.

Now, this will probably get -- become more apparent once we go through some of the -- the finance panel and the very schedules that we produce at the -- at the -- for the GRA, but -- on operating costs, but I think there's been a difficult -- it's been a difficult -- it's been difficult to explain to

the Board our continuing efforts on cost containment in the past general rate applications because I think this capital construction EFTs is getting in the way.

I mean, it's actually been two (2) things that's been getting in the way: a number of accounting changes that have occurred to make our accounting practices more consistent with other electric utilities and, as well, to transition to IFRS, as well as the fact that we, in our -- all of our schedules, we show you all of the gross wages and salaries, which includes the capital construction staff. And then we pull out those costs that are charged to capital.

And I think the Board has concluded in the last couple rate orders that Manitoba Hydro didn't have a strong commitment to cost containment. But I think what's happening is we haven't done a good job at presenting that to the Board because I think Manitoba Hydro always has had a strong commitment to cost containment.

It's unfortunate that accounting changes and -- and how our schedules are set up, how our system works of charging costs has muddied the waters on this particular issue. And I hope that we can clarify that for the Board this time around.

THE CHAIRPERSON: Mr. Rainkie, just one (1) question. With respect to this table we just looked at, this assumes that DSM continues to be the responsibility of the Manitoba Hydro?

MR. DARREN RAINKIE: Yes, it does, sir, yes. Now, when we look at -- or when the Board assesses whether or not limiting operating costs to 1 percent is -- is a stretch target or something hard, easy, or anywhere in between, what's the proper perspective on it?

We know that when we look at contracted wage settlements, you know, progression and merit increases, I mean, like any other company, Manitoba Hydro provides a fair day's pay for a fair day's work. People progress through the ranks. They get promotions, et cetera. We know that overall wages tend to increase at 3 to 4 percent annually.

So limiting operating costs to 1 percent increases is essentially equal to a 3 percent productivity saving each year. So in our view, that's definitely a stretched target, and it's reflective of a company that's committed to controlling its costs in an era where we have to ask for 4 -- close to 4 percent rate increases.

Between 2014 and 2017, our projections

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with our plans are -- is that the operating costs, excluding the effects of accounting changes, will increase annually by about .9 percent, and that compares to projected Manitoba CPI or -- of about 1.9 percent. And that's what this chart is -- is demonstrating, is that, yes, we've had these accounting changes, which I -- to my -- to my belief, have muddied the waters on this whole issue in terms of our efforts on cost containment.

But the green -- the green line on this chart is CPI and the red line is our operating cost projections, excluding accounting changes. So we definitely believe that the 1 percent limit per year is a stretch target when you recognize that wages and salaries are increasing typically at 3 to 4 percent annually. And the limiting of only increases to 1 percent per year is consistent with the PUB's expectations that it outlined in Order 43/'13.

I'm going to move to the exciting topics of accounting policies and depreciation, which seem to be major issues at the hearing, or at least major concerns expressed by stakeholders.

So the concern here is that accounting changes are driving the need for rate increases. I think we've heard that in the material thus far.

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Now, I think to have a proper understanding of this, you have to split the accounting changes into two (2) parts. One (1), those that were made prior to and up to 2013/'14, which were made for purposes of Manitoba Hydro being more consistent with other electric utilities, and as well, heating, past recommendations of the Public Utilities Board itself to stop capitalizing as much overhead as we had been doing.

So I think we wanted to remind all parties that in Order 43/'13, the Board accepted the accounting changes that had been made by Manitoba Hydro up to the 2013 fiscal year for rate-setting purposes. And as I said, this -- this was recommended by the Public Utilities Board in previous orders.

So what's unclear to Manitoba Hydro is if the opinions expressed in the Intervenor evidence that's been received to date are suggesting that the Board should some -- somehow review and vary its past decision or not. It's unclear to me exactly what the point... We -- we see charts that take both the prior accounting changes and add the proposed accounting changes together, but those charts seem to be forgetting that the prior accounting changes have been accepted by the Board for rate-setting purposes.

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So what about -- if I move to slide 58 -- the prospective accounting changes? So as we've outlined in our material, we are making a number of prospective accounting changes for financial reporting purposes in both 2014 and 2015/'16, including further changes to our level of capitalized overhead and reducing the level of capitalized overhead and changes to our depreciation methodologies as part of our conversion to International Financial Reporting Standards, or IFRS, in 2015/'16.

When you look at the chart on this page, we have grouped all of those prospective accounting changes. Most of them are IFRS change. There's one (1) change that we've made to depreciation expense in the current year, resulting from our depreciation study. But what you see is that the cumulative total of all of these accounting changes is actually reducing revenue requirement in the test years by 25 million, 4 million, and 4 million. And that -- and that reduction in the revenue requirement increases to about 48 million by 2024.

So the depreciation changes that we're making are more than offsetting the operating costs that -- changes that are increasing O&A. And as such, accounting changes are not driving the need for rate

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increases in the future, and are not driving the increase in revenue requirements. So Manitoba Hydro's position is given that there's no harm to ratepayers, as revenue requirements are actually reduce -- reducing, not increasing, the use of IFRS for rate-setting purposes is fair and appropriate.

And by the way, while the International Accounting Standards Board is the one that decides the accounting standards, it was the Canadian Accounting Standards Board that decided that Canada would move to -- move to IFRS. It's a -- it's a global world where capital flows across borders endlessly, and this was generally thought to be in the public policy that Canada would follow International Accounting Standard Board financial reporting policies. And that decision was made by the Canadian body.

But I don't see this as a war between the accounting bodies and the rate-setting bodies across Canada. I mean, certainly, we have a very complex, large company, and rate setting does depend on the -- and relies on audited financial information.

And I don't -- in -- in fact, so-called rate-setting methods are just usually accounting methods. There's always a few different methods and rate-setting methods. They're just a selection of

TAB 6

and takes, it -- it isn't.
It's -- it's unfortunate that these changes are masking the issues that are causing problem, in terms of understanding, but they're not driving the need for -- for rate increases. It's -- it's fairly clear to me.
THE CHAIRPERSON: Well, let's go back - - let's go back to 56 then, Diana, please.
MR. DARREN RAINKIE: Slide 56, sir?
THE CHAIRPERSON: Yeah --
MR. DARREN RAINKIE: Yeah.
THE CHAIRPERSON: -- 56. See that -- that's the point that's being made by some of the parties. Look at that top graph there. Accounting changes included. You got a dramatic increase in costs.
MR. DARREN RAINKIE: Yeah.
THE CHAIRPERSON: So I'm trying to relate what you just said about accounting changes and dr -- non-driving costs. When you look at this graph, it's telling the opposite story.
MR. DARREN RAINKIE: And that's -- that's correct. But the problem is, is this is one half (1/2) of the story, it's chapter 1 of 2. What I probably should have put in the slide deck is I should

have graphed the depreciation reductions that I have on slide 59 because what's happening is those depreciation reductions are neutralizing the -- the increases in operating costs such that we get back to no harm to customers, no negative impact on revenue requirements.
So -- so that -- that's the problem with looking at one (1) side of the equation, is -- is that you're going to come to false conclusions, in our humble opinion.

(BRIEF PAUSE)

MR. DARREN RAINKIE: Sir, if it would help in terms of communicating these -- the need for rate increases to customers, we could prepare a similar graph on the depreciation side to the operating cost side and perhaps even put them on the same slide. Would that be helpful?
THE COURT REPORTER: Is that an undertaking?
MR. DARREN RAINKIE: Yes, that's another undertaking. I love these kinds of undertakings though, when they -- when they help demonstrate the higher level points. Manitoba Hydro will undertake to prepare a graph of the accounting

changes with respect to depreciation expense.

--- UNDERTAKING NO. 3: Manitoba Hydro to prepare a graph of the accounting changes with respect to depreciation expense

MR. DARREN RAINKIE: So, sir, I'm going to move to page 60 if -- if that's the end of your questions on that particular graph. So -- so, sir, the discussion we were just having -- having is really the point on -- on page 60. At the last general rate application, both MIPUG and Consumers' Association had recommended that the Public Utilities Board not accept various accounting changes that Manitoba Hydro had made. And they also are recommending that we remove net salvage value from depreciation rates a few years earlier than our transition to IFRS in order to justify lower rate increases.
And the quote that I have here from page 10 of Order 43/'13 is that the Board rejected this approach. And they rejected it for the reasons we were just talking about, the potential weakening of Manitoba Hydro's financial position and increased borrowing costs. And I note it was the Board that used the word

'reject'. This is not me overlying my views of the world on -- on the Board.
And I think there was -- and while we only look at the Board orders and we -- we don't get to talk to you specifically about them, we try to interpret what they're -- what they're saying to us over time. I -- I did sense the careful use of the word 'approach'. It was suggesting to me that this wasn't just about the specific recommendations but -- but generally the approach of adjusting accounting policies just to justify lower rate increases was not one (1) that the Board found favour with.
So I'll -- I'll leave you with that thought, Mr. Chairman. Hopefully our position on the matters is little clearer after our exchange, but...

(BRIEF PAUSE)

MR. DARREN RAINKIE: I do think that we have to be careful that -- in this hearing that the proposals on overheads and ELG appear to Manitoba Hydro for the -- the Intervenor proposals appear to be the use of the same approach that the Board rejected in Order 43/'13.
More accounting, sir. The need for two

(2) sets of books, so... I would suggest, Mr. Chairman and Board, that the two (2) sets of books is just a means to try to implement the very approach that the Board rejected in Order 43/'13. Two (2) sets of books is not a revenue requirement -- the technical revenue requirement discussion in terms of dollars and cents, but it's one (1) -- it's a means to an end.

So a few points on this is that the cost-of-service rate-setting methodology that we use in Manitoba does not determine rates strictly on the basis of costs. We spend -- tend to smooth costs in over time. Other regimes, as you're probably aware, use a rate-based rate of return methodology where all of the costs are added up together and financing costs and a net income is -- is added on top of that in order to set rates. But at Manitoba Hydro we've always had more of a judgmental way of looking at the cost flows over time and gradually getting at rate increases that would eventually get to the costs.

So -- so the -- the whole purpose of two (2) sets of books is rendered completely unnecessary by the way that we have approached rate setting in Manitoba in the last number of decades at least that I have been involved. In Manitoba Hydro's view one (1) set of books is preferable. It reduces the confusion

of various users of financial statements looking at different schedules, trying to rely on different information to make decisions and evaluate performance.

It improves the transparency of the rate setting process. We can trace numbers in between the financials and -- and the -- the rate setting orders. It improves the reliability of rate setting. As I mentioned earlier I think one (1) of the users of our audited financial statements is definitely the Public Utilities Board. And -- and there's reliability that all of our users of our financial statements weigh on that audit opinion from the -- well, in this case our auditors are Ernst and Young currently. But, I mean, that -- that says to the Board it doesn't have to go about auditing the information. It can use the information on that basis.

And interestingly enough, CAMPUT supported a single set of financial statements as best serving the public interest as demonstrated in the letter to the International Accounting Standards Board of August 3 -- 30th, 2013, which is part of the material in the Information Requests when the -- when the -- when CAMPUT commented on the interim standard on regulatory deferral accounts. So to the extent that this has been a heated issue at -- so far in the run up

to this hearing that's Manitoba Hydro's thoughts on the issue, sir.

THE CHAIRPERSON: I didn't quite get your point about audit opinion.

Could you repeat that please?

MR. DARREN RAINKIE: Oh, I -- Manitoba Hydro has a very complex, large operation and the Board isn't looking at it -- the Board -- the Board usually looks at our rate applications once every couple of years. So certainly all users, including the Public Utilities Board, rely on the audited information. And the fact that it's reliable, you know, re -- reasonable states the pos -- the financial position of Manitoba Hydro.

So you don't have to worry about that it's -- it's not good information. You can go about your rate setting -- setting process and relying on the audit opinion that Ernst and Young has done its job so that was the point I was trying to make.

THE CHAIRPERSON: Seems to me that it's a pretty tenuous argument in the sense that, you know, even if the Board was to set rates based on another methodology than what you're proposing the audit -- auditors of Manitoba Hydro will continue to issue audited statements on your behalf and would have a

schedule that would show the -- you know, reflect that the rate-setting methodology that's been used by -- by PUB and you still have audited statements. So I'm not su -- I'm not sure I get your point.

MR. DARREN RAINKIE: Well, sir, I guess that's one (1) of the question is I'm not -- I'm not quite sure when folks are talking about two (2) sets of books or alternate sets of calculation really the extent that they want it to go to and whether or not they would want that information audited.

There's been suggestions over time that this is just a simple issue of producing separate sets of calculations, but would the Board want that audited then? If there was a separate set of calculations for rate-setting purposes would the Board want it -- want that audited then so that they could place reliance on it is the issue.

The -- I think the last area of concern that I wanted to chat about was could relaxing Manitoba Hydro's long-term financial targets result in lower rate increases. And -- and as I mentioned early on in my presentation if we were looking at this just from a financial perspective we would need rate increases in the order of 5 1/2 to 6 percent over the next four (4) years at least to reduce the losses that we see in our

TAB 7

PUB/CAC(Rainkie)-12 Reference**:** Rainkie-Derksen Evidence p.39 Line 23-26

Request:

Given that all O&A is assigned through allocators, please provide how Mr. Rainkie proposes ensuring 1% escalation in O&A costs. (i.e. the constraint put on the amount of costs allocated through ICAM to Centra being restricted to 1% of growth)

Response:

In the event that MH is able to manage its O&A costs within the 1% escalation factor that the PUB found was acceptable for rate-setting purposes on Page 24 of Order 69/19, then there should be a natural flow-through of this level of escalation in the O&A costs that are allocated to Centra through the ICAM. In this case, there would be no requirement for a discrete rate-setting adjustment.

In the event that MH is unable to manage its O&A cost within the 1% escalation factor, then a discrete adjustment to the O&A costs that are allocated to Centra through the ICAM would have to be made for rate-setting purposes. This adjustment could be made in a manner that is consistent with the calculations provided on pages 47 to 49 of our Evidence, by considering the level (percentage) of escalation inherent in the MH consolidated O&A forecast and making a corresponding adjustment down to the 1% escalation level, based on the total O&A costs allocated to Centra.

TAB 8

REFERENCE:

Tab 13 – Public Utilities Board Directives & Other Matters

PREAMBLE TO IR (IF ANY):

QUESTION:

a) Please provide copies of the letters dated March 10, 2016 and April 4, 2016, related to natural gas accounting matters, noted on page 7 of Tab 13, lines 2 to 7,

b) Please further elaborate what Centra is requesting from the PUB with respect to the ICAM study from the 2019/20 GRA (ICAM is discussed on page 12 and 13 of Tab 13).

RATIONALE FOR QUESTION:

To understand the status of outstanding and on-going PUB directives to Centra.

RESPONSE:

a) Please see the Attachment to this response for copies of the letters dated March 10, 2016 and April 4, 2016 related to natural gas accounting matters.

b) Please see Centra's response to PUB/CENTRA I-37c).

Manitoba Hydro

PO Box 815 • Winnipeg, Manitoba Canada • R3C 2P4
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March 10, 2016

Mr. D. Christle
Secretary and Executive Director
Public Utilities Board
400-330 Portage Avenue
Winnipeg, Manitoba
R3C 0C4

Dear Mr. Christle:

RE: CENTRA GAS MANITOBA INC. ("CENTRA") ACCOUNTING MATTERS

In advance of the closing of its financial statements for the 2015/16 fiscal year, Centra is requesting confirmation from the Public Utilities Board of Manitoba ("PUB") that the Corporation's proposed accounting treatment, as outlined below, of certain matters for its natural gas operations is consistent with the intent of the PUB's rate-setting objectives and previous findings. These include a change in accounting treatment for costs associated with meter testing and exchange activities, new depreciation rates for 2015/16 for rate-setting purposes, as well as overhead costs no longer eligible for capitalization.

1. Accounting for Meter Testing & Exchange Activities

Currently, Centra expenses the cost associated with natural gas meter testing and exchange activities in the year they are incurred. For Manitoba Hydro's electric operations, the cost of electric meter testing and exchange activities are capitalized and depreciated.

The Corporation transitioned to International Financial Reporting Standards ("IFRS") effective April 1, 2015 with restatement of the 2014/15 fiscal year for comparative reporting purposes. Under IFRS, there is a requirement to harmonize the accounting policies of a parent company and its subsidiaries.

As outlined in the IFRS Status update report filed in Manitoba Hydro's 2015/16 & 2016/17 General Rate Application, Centra will harmonize its accounting treatment with that of the Corporation's electric operations to capitalize the costs associated with meter sampling, testing and exchange activities. Centra intends to apply this change in policy on a prospective basis commencing in the 2015/16 fiscal year (with restatement of the 2014/15 fiscal year for comparative reporting purposes) and is requesting the PUB's confirmation that this approach is appropriate for rate-setting purposes.

2. Depreciation Rates

As the PUB is aware, Centra periodically updates its asset life estimates and depreciation rates by way of comprehensive depreciation studies. Centra most recently completed a depreciation study in October 2014, based on plant assets as at March 31, 2014, to develop Canadian Generally Accepted Accounting Principles ("CGAAP") compliant depreciation rates (for fiscal 2014/15) based on the Average Service Life (ASL) method. In addition, this study also developed IFRS compliant depreciation rates (for fiscal 2015/16) using the Equal Life Group ("ELG") method. Please find the 2014 Depreciation Study prepared by Gannett Fleming Canada ULC ("Gannett Fleming") as Attachment 1 to this submission, which includes ELG depreciation rates effective for financial reporting purposes effective April 1, 2015, and Attachment 2 includes ASL depreciation rates including negative salvage effective April 1, 2014 and ASL depreciation rates excluding negative salvage for rate-setting purposes effective April 1, 2015.

Centra's depreciation rates were last updated April 1, 2011 and approved by the PUB in Order 85/13. In Order 85/13 at page 23, the PUB indicated that Centra is not to make any accounting changes related to depreciation for rate-setting purposes until it has received PUB approval.

For financial reporting purposes, Centra implemented the revised CGAAP ASL depreciation rates effective April 1, 2014 for fiscal 2014/15 and IFRS compliant ELG depreciation rates effective April 1, 2015 for fiscal 2015/16 with comparative year restatement.

On July 24, 2015, the PUB issued Order 73/15 with respect to Manitoba Hydro's 2015/16 & 2016/17 Electric General Rate Application ("GRA"). In that Order at page 46, the PUB found that Manitoba Hydro should retain its existing CGAAP ASL methodology for rate-setting purposes until Directives 8 and 9 from Order 43/13 have been complied with and the PUB has been provided with an IFRS-compliant depreciation study based on ASL. At page 45 of Order 73/15, the PUB accepted Manitoba Hydro's proposal to remove negative salvage from its depreciation rates effective April 1, 2015.

Consistent with the PUB's findings for the electric operations, Centra assumes that the CGAAP ASL methodology, excluding negative salvage costs, should also be applied to the natural gas operations for rate-setting purposes. Accordingly, Centra is seeking approval, on an interim basis, of CGAAP ASL depreciation rates excluding negative salvage costs for rate setting purposes.

In addition, Centra proposes to apply the same accounting treatment for the difference between depreciation expense calculated for financial reporting purposes (based on the IFRS compliant ELG method) and depreciation expense calculated for rate setting purposes (based on the CGAAP ASL method excluding negative salvage) as set out in Manitoba Hydro's letter to the PUB of February 25, 2016 with respect to its electric operations. In that letter, Manitoba Hydro proposes to record the difference between depreciation expense calculated for financial reporting purposes based on IFRS compliant ELG depreciation rates and depreciation expense calculated for rate-setting purposes based on CGAAP ASL depreciation rates (excluding negative salvage), as a regulated liability along with a corresponding regulated asset for the 2015/16 fiscal year.

Centra will seek final approval of the CGAAP ASL depreciation rates, as well as the disposition of the regulated liability and corresponding regulated asset at its next Gas GRA.

3. Change in Service Life to Meter Account

In addition to the change in depreciation rates outlined in the depreciation study, for 2015/16 the service life for the "meters" account will also be updated to 20 years from 25 years. While the Corporation's current practice is to undertake a depreciation study every 5 years, IFRS requires that the method of depreciation be reviewed at least annually with any changes being applied as a change in accounting estimate on a prospective basis. The change is based on an analysis of asset retirement gains and losses performed in fiscal 2015/16, and the annual impact of this change in depreciation rate is $0.6 million (assuming the ELG method). A letter from Gannett Fleming regarding this change is provided as Attachment 3 to this submission.

The change in service life for the meters account will apply to both the IFRS compliant ELG depreciation rates implemented effective April 1, 2015 for financial reporting purposes, as well as the CGAAP ASL no salvage depreciation rates that Centra is requesting interim approval of in this submission.

4. Ineligible Overheads

At page 15 of Order 85/13, the PUB noted that since 2010/11, Centra has expensed approximately $5 million of overhead costs that, previously, would have been capitalized. In addition, the PUB noted that Centra will expense a further $2 million in capitalized overhead when it implements IFRS in 2015/16.

At pages 35-36 of Order 73/15, the PUB noted that overheads no longer eligible for capitalization have increased since the 2012/13 & 2013/14 GRA and the PUB indicated that the additional ineligible overheads should continue to be capitalized for 2015/16 for rate-setting purposes.

Consistent with the PUB's findings for the electric operations, Centra assumes that the PUB's findings with respect to overhead should also be applied to the natural gas operations for rate-setting purposes. As indicated in the February 25, 2016 letter, Manitoba Hydro is proposing to record the difference between Operating & Administrative ("O&A") expense calculated for financial reporting purposes and O&A expense excluding the additional overheads to be capitalized, as a regulated liability along with a corresponding regulated asset for the 2015/16 fiscal year.

Centra is respectfully seeking the PUB's confirmation that its proposed accounting treatments are consistent with the intent of the PUB's rate-setting objectives and previous findings, which will allow Centra to close its financial statements for the 2015/16 fiscal year. A review of the disposition of the proposed regulated liability and asset balances can be considered at the next Gas GRA.

Given that the amounts in question are material to the financial statements and that the Corporation is preparing for its year-end audit process, Centra respectfully requests that confirmation be provided by the PUB by March 24, 2016.

Should you have any questions with respect to the forgoing, please do not hesitate to contact the writer at 204-360-3633 or Shannon Gregorashuk at 204-360-4270.

Yours truly,

MANITOBA HYDRO LAW DIVISION
Per:

ODETTE FERNANDES
Barrister & Solicitor

Att.

Public Utilities Board — Régie des services publics

April 4, 2016

Manitoba Hydro
Legal Department
22nd Floor, 360 Portage Avenue
Winnipeg, MB R3C 2P4

Attention: Odette Fernandes

VIA EMAIL

Dear Madam:

Re: Centra Gas Manitoba Inc.
March 10, 2016 Request for Accounting Clarification

The Board is in receipt of Centra Gas Manitoba Inc.'s ("Centra") attached correspondence of March 10, 2016 seeking the Public Utilities Board's ("Board") clarification with respect to the 2015/16 fiscal year treatment of various accounting matters in light of Centra's implementation of International Financial Reporting Standards ("IFRS"). In particular, Centra seeks the following:

1. Confirmation from the Board that capitalizing expenditures related to meter testing and exchange activities is appropriate for rate-setting purposes.
2. Confirmation that, similar to the Directive to Manitoba Hydro in Order 73/15 to continue to determine depreciation for rate-setting purposes based on the Average Service Life ("ASL") methodology without net salvage, Centra should utilize ASL without net salvage for rate-setting purposes. In addition, Centra proposes to apply the same accounting treatment for the difference between depreciation expense calculated for financial reporting purposes and rate-setting purposes as set out in Manitoba Hydro's letter to the PUB dated February 25, 2016, a copy of which is also attached.
3. Approval of a service life change to the Meter account.
4. Confirmation that with respect to the capitalization of overhead, Centra should apply the same rationale as the Board set out for Manitoba Hydro in Order 73/15. As indicated in its February 25, 2016 letter, Manitoba Hydro is proposing to record the difference between Operating and Administrative (O&A) expense calculated for financial reporting purposes and O&A expense excluding the additional overheads to be capitalized, as a regulated liability along with a corresponding regulated asset for the 2015/16 fiscal year.

At the outset, the Board clarifies that its mandate with respect to prescribing accounting methods is limited to determining the appropriate accounting for rate-setting purposes, but not for financial reporting purposes. While in the Board's view, it would be preferable for Centra's financial statements to be consistent with the current rate-setting methodology approved by the Board, the Board cannot provide the requested guidance as to how Centra should prepare its financial statements for financial reporting purposes. As such, both Manitoba Hydro and Centra should seek the appropriate guidance from their internal and external accounting advisors with respect to their obligations under IFRS to comply with the directives of Board Order 73/15. This should include a consideration of the risk of the utility having to re-state its financial statements if the financial reporting methodology does not align with the Board-approved rate-setting methodology.

The Board stated as follows in Order 85/13, emanating from the hearing of Centra's last General Rate Application:

> The Board understands that Centra has been making changes to its accounting practices to be consistent with International Financial Reporting Standards. These changes reflect a consistent approach with its parent Manitoba Hydro to address capitalization policies. In the Board's view, Centra's proposed accounting changes are appropriate for the test year. The Board will direct Centra to file an International Financial Reporting Standards status update at the next General Rate Application. Until such time, the Board expects Centra not to make any further accounting changes for rate-setting purposes. With respect to meter exchange costs, the Board will not direct a change in the accounting policy at this time. The Board will expect Centra to put forward a proposal on harmonizing this accounting policy with Manitoba Hydro in its IFRS status update report directed in this Order.

Among other things, Order 85/13 requires Centra to continue to use the Average Service Life (ASL) methodology of depreciation for rate-setting purposes, which is the same methodology the Board directed Manitoba Hydro to use in Order 73/15. The Board notes that this means the depreciation methodology is currently consistent between Centra and its parent company Manitoba Hydro. However, the Board accepts that with respect to the other issues raised in Centra's March 10, 2016 letter, there could be inconsistency between Manitoba Hydro and Centra.

In the Board's view, whether each of the accounting changes proposed by Centra in its March 10, 2016 correspondence should be implemented for rate-setting purposes will be examined in the next Centra General Rate Application and does not warrant an interim proceeding at this time. It is the Board's intention to examine and make a final ruling with respect to each of these issues for rate-setting purposes at the hearing of the next General Rate Application in 2017.

In the meantime, the Board expects Centra to seek such advice as it considers appropriate in preparation of its financial statements.

Yours truly,

"Original Signed By"

Kurt Simonsen
Associate Secretary

Attachment

cc: Interveners of Record

TAB 9

<u>PUB/CENTRA I-21</u>

Subject: **Tab 5: Financial Results & Forecast**

Reference: **Tab 5 Appendix 5.7 Page 1 of 23; 2009/10 & 2010/11 GRA PUB/Centra 36 – Integrated Cost Allocation Methodology**

c) **For 2013/14, please provide a table showing the discrete forecasted amounts for each of the Resource Primary costs, each of the Administrative Primary Costs, each of the Interest, Depreciation & Taxes costs and each of the Work Order primary Costs in a similar format to that provided in response to PUB/Centra 36(c) at the 2009/10 & 2010/11 GRA.**

<u>ANSWER</u>:

Please see the attachment to this response.

Centra Gas Manitoba Inc.		**PUB/Centra 21(c)**
2013/14 Gas GRA		**Attachment**
2013/14 Forecast Primary Costs - Integrated Operations		**Mar 31, '14**
		($000,000's)
Resource Primary Costs		
Direct Labour	$	543
Employee Benefits		133
Material & Tools		7
Motor Vehicles		38
Office & Administration		9
Operating Expense Recoveries		(1)
Purchased Services		3
Travel		28
Payroll Tax		12
Contingency		(8)
	$	**764**
Administrative Primary Costs		
Material & Tools	$	1
Purchased Services		5
Travel		3
	$	**9**
Depreciation on Tools		
PC's	$	16
Tools & Work Equipment		7
	$	**23**
Work Order Primary Costs		
Buildings & Property	$	6
Collections		4
Customer & Public Relations		6
Materials & Tools		30
Office & Administration		7
Operating Expense Recoveries		(6)
Purchased Services		69
Travel		2
Capital Disbursements		1,247
	$	**1,365**

Interest on Tools

PC's	$	3
Work Equipment		3
Motor Vehicles		7
	$	**13**

Depreciation, Interest & Taxes on Admin Assets

Buildings	$	43
Communication Equipment		3
IT Infrastructure Hardware, Software & Systems		16
Furniture & Fixtures		3
Inventory		4
	$	**69**

Figure 5.5.13 OM&A by Cost Element

MANITOBA HYDRO
OPERATING, MAINTENANCE AND ADMINISTRATIVE COSTS BY COST ELEMENT

(In thousands of $)	2012/13 Actual	2013/14 Actual	2014/15 Forecast	2015/16 Forecast	2016/17 Forecast	Average Annual % Inc/(Dec)	Note
Wages & Salaries	$ 466 165	$ 480 511	$ 502 692	524 552	533 997	3.5%	1
Overtime	61 031	62 365	61 709	71 080	73 121	4.8%	2
Employee Benefits	130 886	157 094	160 592	155 892	158 992	5.3%	3
Sub-Total	658 082	699 970	724 993	751 523	766 109		
Less: Labour & Benefits Charged to Capital	(215 491)	(234 510)	(256 588)	(282 335)	(287 969)	7.6%	4
Labour & Benefits Charged to Operations*	442 591	465 460	468 405	469 188	478 140	2.0%	5
Other Costs							
Employee Safety & Training	4 463	4 596	5 225	5 188	5 175	3.9%	6
Travel Expenses	31 194	31 915	31 766	31 628	31 634	0.4%	
Motor Vehicle	29 516	29 670	29 682	29 699	29 699	0.2%	
Materials & Tools	24 806	27 920	26 700	26 090	26 090	1.5%	
Consulting & Professional Fees	10 817	14 657	14 349	12 395	12 237	4.6%	7
Construction & Maintenance Services	16 259	16 775	19 364	18 580	18 580	3.6%	8
Building & Property Services	25 644	28 978	27 738	27 297	27 297	1.8%	
Equipment Maintenance & Rentals	14 680	15 007	16 120	16 191	16 191	2.5%	9
Consumer Services	5 050	5 277	5 323	5 323	5 323	1.3%	
Computer Services	849	678	985	1 020	1 019	7.2%	
Collection Costs	4 261	3 125	4 078	4 078	4 078	1.0%	
Customer & Public Relations	6 731	5 610	5 334	5 344	5 316	-5.5%	10
Sponsored Memberships	1 767	1 249	1 764	1 737	1 737	2.6%	
Office & Administration	13 874	14 724	15 722	15 721	15 717	3.2%	11
Communication Systems	1 817	1 963	1 928	1 928	1 928	1.6%	
Research & Development Costs	3 372	2 195	2 747	2 747	2 747	-2.4%	
Miscellaneous Expense	2 040	1 485	954	900	900	-17.2%	12
Contingency Planning	-	-	2 594	2 610	2 657		
Operating Expense Recovery	(13 997)	(17 808)	(13 468)	(13 649)	(13 647)	0.0%	13
Strategic Initiative Funding			870	3 640	6 317		14
Sub-Total	183 143	188 016	199 774	198 468	200 994		
Less: Other Costs Charged to Capital	(29 327)	(31 503)	(33 329)	(34 647)	(34 818)	4.4%	15
Other Costs Charged to Operations*	153 815	156 513	166 444	163 821	166 177	2.0%	5
Total	**596 406**	**621 973**	**634 849**	**633 009**	**644 317**	2.0%	
Less:							
Capitalized Overhead	(69 720)	(74 446)	(81 265)	(24 578)	(24 824)	-13.2%	16
Operating and Administration Charged to Centra	(63 735)	(66 810)	(67 829)	(66 691)	(67 818)	1.6%	
Electric OM&A, including Accounting Changes	**462 952**	**480 717**	**485 755**	**541 740**	**551 675**	4.6%	
Less: Accounting Changes	(78 345)	(91 155)	(93 858)	(145 644)	(151 345)		
Electric OM&A, excluding Accounting Changes	**$ 384 607**	**$ 389 562**	**$ 391 897**	**$ 396 096**	**$ 400 330**	1.0%	
Year over Year % Change, including Accounting Changes		3.8%	1.0%	11.5%	1.8%	4.6%	
Year over Year % Change, excluding Accounting Changes		**1.3%**	**0.6%**	**1.1%**	**1.1%**	**1.0%**	

*Includes amounts capitalized through Overhead

Figure 5.4.13 above includes costs which are direct charged to the operations and maintenance activities of the Corporation (e.g. materials, contracted services, consulting, etc) as well as staff related costs, of which a portion is allocated to capital. Staff related costs, such as wages & salaries, benefits, travel, and motor vehicles, are costs associated with providing a pool of resources required for the operation, maintenance and capital construction activities of the Corporation. These costs are allocated to both capital projects and operating programs through the use of an hourly activity rate charged