

PUBLIC UTILITIES BOARD

WRITTEN FINAL ARGUMENT OF MANITOBA HYDRO

2019/20 ELECTRIC RATE APPLICATION

May 1, 2019



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1 **1 INTRODUCTION**

2 **1.1 Approvals Sought**

3 On May 5, 2017, Manitoba Hydro filed a comprehensive 2017/18 & 2018/19 General
4 Rate Application (“GRA”) with the Public Utilities Board of Manitoba (“PUB”) and over
5 the course of the following nine months, a lengthy and extensive review of Manitoba
6 Hydro’s operations, forecasts, financial plans, capital expenditures, and operating
7 expenses was conducted. Following its review, the PUB issued Order 59/18, dated May
8 1, 2018, which approved a 3.6% average electric rate increase effective June 1, 2018.

9
10 On November 12, 2018 Manitoba Hydro corresponded with the PUB advising that since
11 the issuance of Order 59/18, a new Manitoba Hydro Electric Board (“MHEB”) had been
12 appointed and were undertaking a comprehensive review of the Manitoba Hydro
13 operations, forecast and financial plans which will allow them to establish a financial
14 plan for the Corporation. Manitoba Hydro sought the PUB’s concurrence to consider a
15 one-year rate increase sufficient to generate a net income to avoid a then projected net
16 loss in the 2019/20 fiscal year, proposed a limited review of the electric operations
17 based upon information currently available to the Corporation, and provided a report
18 on the status of various directives. Manitoba Hydro also advised the PUB of its intention
19 to submit a full GRA to be filed in late 2019. Manitoba Hydro proposed that the
20 application be considered by way of a streamlined written process and limited
21 Intervenor participation, and sought approval on a final basis, being mindful of the
22 PUB’s comments with respect to the challenges associated with interim rates. After
23 soliciting comments from past Intervenors of Record, on November 20, 2018 the PUB
24 determined that it was willing to consider a one-year rate increase Application based on
25 financial information for 2018/19 and 2019/20 years, and without requiring the filing of
26 a new Integrated Financial Forecast (“IFF”).

27
28 On November 30, 2019 Manitoba Hydro filed its 2019/20 Electric Rate Application. On
29 December 11, 2018 Manitoba Hydro filed Additional Information in response to the
30 direction of the PUB, and subsequently received a Certificate of Completion in respect
31 of the Application. On February 14, 2019 Manitoba Hydro filed a Supplement to the
32 Application providing updated information based on the 2019/20 Approved Budget
33 approved by the MHEB on February 12, 2019, and reflecting actual financial results and
34 water flow conditions to December 31, 2018 as well as certain planning assumptions.

1 The February 14, 2018 Supplement projects net income of \$95 million for Electric
2 Operations for 2018/19, an improvement of \$45 million compared to the 2018/19
3 Outlook filed on November 30, 2018.

4
5 The improvement in net income is primarily due to an increase of \$40 million in
6 Extraprovincial revenues due to above average precipitation in the fall of 2018 resulting
7 in improved water flow conditions, as well as higher realized export prices. The \$45
8 million improvement over a relatively short timeframe demonstrates the variability in
9 net income the Corporation can experience given its operating environment.

10
11 Ms. Bauerlein indicated in Transcript Pages 177-180, that despite a colder than normal
12 winter, actual results for the fiscal year are tracking to the 2018/19 Current Outlook of
13 \$95 million.

14
15 For 2019/20, Manitoba Hydro is projecting an annual net income for Electric Operations
16 of \$115 million for the 2019/20 fiscal year, inclusive of the 3.5% proposed rate increase.
17 The 2019/20 Approved Budget assumes average revenues and costs based on Manitoba
18 Hydro's long term record of water and normal weather for the year.

19
20 The increase in net income compared to the Interim Budget is primarily attributable to
21 lower power purchases as a result of higher opening water storage, lower financing
22 costs primarily as a result of the lower costs of Bipole III as well as slightly higher
23 domestic revenue also contribute to the improvement in net income.

24
25 Manitoba Hydro is seeking final approval of a 3.5% rate increase for all customer classes
26 effective June 1, 2019. If approved, the June 1, 2019 rate increase would result in a
27 \$3.30 increase in the monthly bill of a residential customer without electric space heat
28 using 1,000 kilowatt-hours ("kWh") per month, and a \$6.30 increase in the monthly bill
29 for a residential customer with electric space heat using 2,000 kWh per month.

1 **2 RATE-SETTING REQUIREMENT FOR A LONG TERM FINANCIAL FORECAST**

2 **2.1 Recently Completed Lengthy GRA in 2017/18**

3 Prior to the current process before the PUB, Manitoba Hydro and all parties had
4 recently concluded a very fulsome GRA for the 2017/18 and 2018/19 fiscal years.
5 Manitoba Hydro filed the 2017/18 & 2018/19 GRA with the PUB on May 5, 2017 with
6 final arguments completed on February 14, 2018 and a decision issued by the PUB on
7 May 1, 2018. Order 59/18 outlined the extensive review and process undertaken which
8 included eight Intervenors (Assembly of Manitoba Chiefs (“AMC”), Business Council of
9 Manitoba (“BCM”), City of Winnipeg (“City”), Consumers Coalition (“COALITION”), Green
10 Action Centre (“GAC”), representatives of the GSS/GSM class, Manitoba Keewatinowi
11 Okimakinak (“MKO”) and the Manitoba Industrial Power Users Group (“MIPUG”)) and a
12 total of 13 consultants (Philip Raphals (AMC), Tyler Markowsky (City), London Economics
13 (GSS/GSM), Paul Chernick (GAC), Patrick Bowman (MIPUG), Cam Osler (MIPUG), Gerry
14 Forest (MIPUG), Morrison Park Advisors (COALITION), Metsco (COALITION), William
15 Harper (COALITION), Dr. Janice Compton (COALITION), Dr. Wayne Simpson (COALITION).
16 In addition, the PUB also retained the services of 5 consultants (Daymark, MGF,
17 Amplitude, Klohn Crippen Berger Stanley Consultants and Dr. Adonis Yatchew. The PUB
18 undertook an in-depth assessment of export pricing and revenues, Manitoba Hydro’s
19 load forecast and price elasticities, Manitoba Hydro business operations capital and
20 major generation and transmission projects, Manitoba Hydro’s power sale agreement
21 with SaskPower and economic impacts to the Province.

22
23 **2.2 MHEB Review**

24 Manitoba Hydro’s Board of Directors is presently undertaking a review of the
25 Corporation’s Strategic Plan, from which they will develop financial targets, rate
26 strategies and a long term financial forecast. As part of that process, and working with a
27 consultant recently engaged by the Corporation, the Board of Directors will determine
28 the financial targets for the Corporation, the pace at which those targets will be
29 achieved, and any new strategies or undertakings that come out of the planning process
30 or alter the direction of the company. (Transcript Page 129)

31
32 As part of the corporate strategic planning process, Manitoba Hydro intends to engage
33 various stakeholders at the beginning of the process as part of a SWOT analysis to gain
34 an understanding of what stakeholder concerns are with respect to Manitoba Hydro. As
35 Ms. Pachal noted (Transcript Page 374) it is premature to commit to a technical

1 conference with respect to the Corporation's financial targets until such time as the
2 Corporation has an opportunity to consider its strategic direction, and its implications
3 for the IFF and rate strategy.
4

5 **2.3 The PUB Can Rely on Exhibit 93 for Rate Setting Purposes in 2019/20**

6 As part of the current 2019/20 Electric Rate Application, Manitoba Hydro noted the
7 PUB's comments in its letter of November 21, 2018 regarding use of Manitoba Hydro
8 Exhibit 93 from the 2017/18 GRA ("Exhibit 93") and prepared this Application utilizing a
9 comparison to Exhibit 93. It is clear that for purposes of the current review, the PUB
10 determined that without an IFF, Exhibit 93 was to be used as the comparator for the
11 setting of rates for the 2019/20 Electric Rate Application.
12

13 Intervenors allege that it is not possible for the PUB to assess the longer-term financial
14 implications of awarding a rate increase in 2019/20 in the absence of an updated long-
15 term financial forecast.
16

17 *"The modified cost of service rate-setting framework that has traditionally been*
18 *used to set electricity rates in Manitoba is dependent on a long-term financial*
19 *forecast to assess the longer-term financial and rate implications of current rate*
20 *setting decisions. However, it is not possible for the PUB to use the modified cost*
21 *of service rate-setting framework to set rates for 2019/20 in the absence of a*
22 *reliable and updated long-term financial forecast."* (Exhibit CC-7-1, Page 7)
23

24 *"Without a detailed understanding for the long-term financial considerations and*
25 *risks to help guide the level that ratepayers should pay today, there is no*
26 *empirical or sensible way to assess Hydro's proposal on a one-year basis."*
27 (Exhibit MIPUG-5-1, Page 1)
28

29 The PUB can be comfortable relying on the directional impacts and trends of net finance
30 expense, depreciation expense, net debt and the financial ratios found in MH Exhibit 93
31 to assess the long term impacts of granting a rate increase in 2019/20. The most
32 compelling reason is that the projected revenue requirement impacts (as shown in
33 PUB/MH I-9 Updated) of Keeyask and the associated transmission projects remain
34 largely unchanged from that assumed in MH Exhibit 93. Manitoba Hydro's net debt is
35 still expected to grow by an additional \$4 billion from where it is today by the time the

1 major projects are complete, consistent with what is shown in MH Exhibit 93.
2 Regardless of whether interest rates remain at historic low levels, the additional debt
3 required to fund these projects will come at a cost to the Corporation. In fact, there is a
4 greater likelihood that Keeyask may come in-service earlier than scheduled (Oct/20)
5 advancing the projected revenue requirement impacts (\$600 - \$700 million) which
6 further condenses the period of time available for the PUB to smooth in rate increases.
7

8 MH Exhibit 93 assumed 3.57% annual rate increases (23.16% cumulative) up to the in-
9 service of Keeyask. While Mr. Rainkie and Mr. Bowman offered directional commentary
10 of factors that may impact the results in Exhibit 93, there was no quantitative analysis
11 produced by Intervenors in this hearing to suggest that the annual rate increases
12 projected in MH Exhibit 93 are unwarranted. Mr. Rainkie and Mr. Bowman speculate
13 that interest rates could remain low. They also speculate that additional export
14 revenues might be available in the future without acknowledging that any potential
15 benefit of incremental export revenues would only occur once Keeyask is fully in-service
16 which the evidence of Mr. Cormie will address in more detail in below.
17

18 The 3.5% requested rate increase in 2019/20 provides additional revenues on an
19 annualized basis in perpetuity which has a profound impact on the financial reserves,
20 debt levels and financial metrics. Using MH Exhibit 93 for illustrative purposes, Figure 2
21 on page 3 of Manitoba Hydro's Rebuttal Evidence, demonstrates that foregoing a rate
22 increase in 2019/20 exacerbates the projected losses upon in-service of Keeyask,
23 reduces projected earnings by approximately \$900 million, increasing the utility's debt
24 by a similar amount (\$900 million) and further increases the debt ratio in 2028/29 by an
25 additional 3%. It is also noted that the net income projection of \$95 million for 2018/19
26 is almost \$50 million lower than the results forecasted in Exhibit 93 which was relied
27 upon by the PUB in approving a 3.6% rate increase for 2018/19 in Order 59/18.
28

1

10-Year Impacts of 0% Rate Increase in 2019/20

<i>Fiscal Year Ending</i>	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
MH Exhibit 93 with 0% Rate Increase in 2019/20												
Percent Increase	3.36%	3.57%	0.00%	3.57%	3.57%	3.57%	3.57%	3.57%	3.57%	3.57%	3.57%	3.57%
Cumulative Percent Increase	3.36%	7.05%	7.05%	10.87%	14.82%	18.92%	23.16%	27.56%	32.11%	36.82%	41.70%	46.76%
Net Income	94	143	0	51	108	(106)	(193)	(159)	(227)	(175)	(129)	(45)
Retained Earnings	2,842	2,986	2,986	3,037	3,145	3,039	2,846	2,688	2,461	2,285	2,156	2,111
Net Debt	18,473	20,813	22,686	23,880	24,611	24,931	25,046	25,200	25,418	25,599	25,726	25,780
Debt Ratio	85%	86%	87%	87%	87%	88%	89%	89%	90%	91%	91%	91%
EBITDA Interest Coverage Ratio	1.54	1.64	1.52	1.56	1.63	1.51	1.45	1.48	1.44	1.48	1.53	1.60
Capital Coverage Ratio	1.40	1.35	1.07	1.28	1.50	1.19	1.12	1.09	0.97	1.04	1.11	1.21
MH Exhibit 93												
Percent Increase	3.36%	3.57%	3.57%	3.57%	3.57%	3.57%	3.57%	3.57%	3.57%	3.57%	3.57%	3.57%
Cumulative Percent Increase	3.36%	7.05%	10.87%	14.82%	18.92%	23.16%	27.56%	32.11%	36.82%	41.70%	46.76%	52.00%
Net Income	94	143	61	115	178	(29)	(111)	(69)	(128)	(68)	(13)	81
Retained Earnings	2,842	2,986	3,047	3,162	3,340	3,311	3,200	3,132	3,003	2,935	2,922	3,002
Net Debt	18,473	20,813	22,628	23,759	24,424	24,666	24,702	24,765	24,891	24,963	24,971	24,899
Debt Ratio	85%	86%	86%	87%	86%	87%	87%	88%	88%	88%	88%	88%
EBITDA Interest Coverage Ratio	1.54	1.64	1.58	1.62	1.69	1.58	1.52	1.57	1.53	1.58	1.63	1.72
Capital Coverage Ratio	1.40	1.35	1.18	1.41	1.64	1.33	1.27	1.24	1.12	1.20	1.29	1.39
Differences												
Percent Increase	0.00%	0.00%	-3.57%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Cumulative Percent Increase	0.00%	0.00%	-3.82%	-3.96%	-4.10%	-4.24%	-4.39%	-4.55%	-4.71%	-4.88%	-5.06%	-5.24%
Net Income	0	(0)	(61)	(64)	(70)	(77)	(82)	(90)	(99)	(107)	(116)	(126)
Retained Earnings	0	(0)	(61)	(125)	(195)	(272)	(354)	(444)	(543)	(650)	(766)	(892)
Net Debt	0	0	58	121	188	264	344	434	527	636	755	881
Debt Ratio	0%	0%	0%	0%	1%	1%	1%	2%	2%	2%	3%	3%
EBITDA Interest Coverage Ratio	0.00	(0.00)	(0.06)	(0.06)	(0.06)	(0.07)	(0.07)	(0.08)	(0.09)	(0.10)	(0.11)	(0.12)
Capital Coverage Ratio	0.00	(0.00)	(0.11)	(0.12)	(0.13)	(0.15)	(0.15)	(0.15)	(0.14)	(0.16)	(0.18)	(0.18)

2

3

Source: Exhibit MH-24, Page 3

4

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At Transcript Page 718, Mr. Rainkie took issue with Manitoba Hydro's submission that the net income would deteriorate by \$900 million without a rate increase in 2019/20. Mr. Rainkie suggests that a \$567 million overstatement of debt may fully offset the \$900 million net loss over 10 years but admits he doesn't have the ability to calculate the effects. Mr. Rainkie fails to recognize that \$241 million (MIPUG/MH I-3 and Transcript Page 453) is planned to be spent to complete the Bipole III project over the next two years. Assuming an interest rate of 4%, the net difference in debt of \$326 million (\$567 less \$241 million) results in lower annual interest costs of \$13 million compared to Exhibit MH-93. Over 10 years this translates to approximately \$130 million which is substantially lower than the \$900 million offset suggested by Mr. Rainkie.

Mr. Rainkie goes on to state that the lower cost of Bipole III will lower finance and depreciation without recognizing that the lower Bipole costs are the significant factor contributing to the lower debt in 2019/20 and as such has effectively double-counted the Bipole III impact in his discussion.

1 Intervenor also suggest that there are higher revenues than outlined in Exhibit 93. Mr.
2 Rainkie recommends the PUB consider for rate setting purposes the potential sales of
3 additional surplus capacity and dependable energy in 2019/20 (Exhibit CC-7-1, Page 104
4 and Exhibit CC-7-2, Page 17). As explained by Manitoba Hydro on page 3 of its rebuttal
5 evidence (Exhibit MH-24), transmission costs and supply risks associated with potential
6 short-term capacity sales exceed the potential revenues, therefore no additional sales
7 were made. In their response to MH/COALITION I-7, COALITION failed to recognize that
8 even if they were economic the window for registering them with MISO closed on
9 February 1, 2019 making any further sales and resultant capacity revenues for the
10 2019/20 planning year impossible.

11
12 On page 10 of Mr. Bowman's direct evidence (MIPUG-5-1), he suggests in his longer-
13 term directional assessment that potential renewals of Xcel Energy/NSP contracts
14 should result in added export revenue in the forecast.

15
16 Mr. Cormie provides context to the proportion of revenues attributable to capacity:

17
18 *"But -- but most of the -- most of the energy is sold and energy makes up the vast*
19 *majority of our export revenues not capacity. The capacity rents generally are*
20 *about 15 percent of our total export so it's, you know, it's -- it's -- the energy is*
21 *sold, it just has a different -- most of it is sold at long-term fixed prices."*
22 (Transcript Page 431)

23
24 Mr. Cormie also explains the status of the surplus capacity following the expiry of the
25 Xcel Energy sales:

26
27 *"Manitoba Hydro is in conversations with them and other companies on -- on*
28 *what we'll do with that capacity after 2025."* (Transcript page 430)

29
30 Manitoba Hydro's forecasts include revenues associated with all unsold energy. Mr.
31 Bowman is correct that MH-93 did not include revenue projections for unsold capacity
32 following the expiry of the NSP/Xcel Energy contracts. However, as explained by Mr.
33 Cormie, sale of that capacity is only at the discussion level and far from certain.
34 Furthermore, capacity revenue represents only about 15% of total export revenue.
35 Lastly, renewal or replacement of other long term contracts following the expiry of the

1 NSP/Xcel Energy contracts following 2024/25 would not impact Manitoba Hydro's net
2 revenues in 2019/20 or as Keeyask enters into in-service.

3
4 Mr. Bowman raises the issue of the SaskPower sale not being included in MH-93 from
5 the 2017/18 and 2018/19 GRA:

6
7 *"We know that there's added export contracts compared to MH-93, when the*
8 *SaskPower 215 megawatt was highlighted, the potential renewals of Xcel Energy,*
9 *[N]SP agreements, or -- or renewals of aspects of them, at least."* (Transcript
10 Page 576)

11
12 Mr. Cormie confirms at transcript pages 103-104 that the SaskPower sale commences
13 June 1, 2022 and does not impact the 2019/20 test year. Although these additional
14 revenues will be included in the next long term forecast which may partially offset the
15 \$900 million deterioration in cumulative earnings in Exhibit MH-93 absent a 3.57% rate
16 increase in 2019/20, there are numerous other factors as discussed in Section 4.3 which
17 will affect the directional impacts, positive or negative, of the next long term forecast.

18 19 20 **2.4 Legislative Framework Does Not Require a Long Term Forecast**

21 The PUB's mandate with respect to the regulation of Manitoba Hydro is derived from
22 *The Public Utilities Board Act, CCSM c P280 (the "PUB Act"), The Crown Corporations*
23 *Governance and Accountability Act, CCSM c C336 (the "Crown Act"), and The Manitoba*
24 *Hydro Act, CCSM c H190 (the "Hydro Act").*

25
26 There are distinctions between what Intervenors may advocate are requirements or
27 tests for the review of rates and what is actually contained in the legislation.

28
29 Section 39 of the Hydro Act specifies the costs which are to be recovered by Manitoba
30 Hydro in the price for power:

31 32 **Price of power sold by corporation**

33 39(1) The prices payable for power supplied by the
34 corporation **shall** be such as to return to it in full the
35 cost to the corporation, of supplying the power,

1 including

2
3 (a) the necessary operating expenses of the
4 corporation, including the cost of generating,
5 purchasing, distributing, and supplying power and of
6 operating, maintaining, repairing, and insuring the
7 property and works of the corporation, and its costs
8 of administration;

9
10 (b) all interest and debt service charges payable by
11 the corporation upon, or in respect of, money
12 advanced to or borrowed by, and all obligations
13 assumed by, or the responsibility for the
14 performance or implementation of which is an
15 obligation of the corporation and used in or for the
16 construction, purchase, acquisition, or operation, of
17 the property and works of the corporation, including
18 its working capital, less however the amount of any
19 interest that it may collect on moneys owing to it;

20
21 (c) the sum that, in the opinion of the board¹, should
22 be provided in each year for the reserves or funds to
23 be established and maintained pursuant to
24 subsection 40(1). (*emphasis added*)

25
26 Part IV of *The Crown Corporations Governance and Accountability Act*, S.M. 2017, c. 19
27 also includes factors for the PUB to consider in reaching a decision which is consistent
28 with the objectives set forth in the Hydro Act:

29
30 **Factors to be considered, hearings**

31 **25(4)** In reaching a decision pursuant to this Part,
32 The Public Utilities Board may

¹ The "board" referenced in ss. (c) refers to the Manitoba Hydro Electric Board, as set out in the definition section of the Act.

1
2 (a) take into consideration

3
4 (i) the amount required to provide sufficient
5 funds to cover operating, maintenance and
6 administration expenses of the corporation,

7
8 (ii) interest and expenses on debt incurred for the
9 purposes of the corporation by the government,

10
11 (iii) interest on debt incurred by the corporation,

12
13 (iv) reserves for replacement, renewal and
14 obsolescence of works of the corporation,

15
16 (v) any other reserves that are necessary for the
17 maintenance, operation, and replacement of
18 works of the corporation,

19
20 (vi) liabilities of the corporation for pension
21 benefits and other employee benefit programs,

22
23 (vii) any other payments that are required to be
24 made out of the revenue of the corporation,

25
26 (viii) any compelling policy considerations that
27 the board considers relevant to the matter, and

28
29 (ix) any other factors that the Board considers
30 relevant to the matter;

31
32 An IFF is not required for the PUB to approve a rate increase for 2019/20, or to assess
33 the long term reasonableness of any rate application. It is clear that there is no
34 legislative requirement for the PUB to review an IFF prior to making a determination on
35 a rate request. The factors to be considered by the PUB are set out in legislation. While

1 an IFF is a useful tool to provide a long term, directional impact of rate increases; it is a
2 simply tool that may be used by the PUB in determining just and reasonable rates.

3
4 Mr. Williams on behalf of the COALITION also acknowledged the IFF as a tool, although
5 he suggested it was a necessary component for rate determination in his opening
6 comments.²

7
8 Manitoba Hydro submits that the PUB is not required to utilize an IFF in order to come
9 to a rate decision. The decision of the Manitoba Court of Appeal in Consumers Assn. of
10 Canada (Manitoba) Inc. v. Manitoba Hydro Electric Board, 2005 MBCA 55, is instructive
11 in this regard. The tool at issue in that case was the cost of service study (“COSS”),
12 however, the findings of the Court apply equally to an IFF. The Court held that “the PUB
13 has two concerns when dealing with a rate application: the interests of the utility’s rate
14 payers and the financial health of the utility.” (para 65). Intervenor arguments that the
15 PUB failed to ensure that the rate it fixed for its share of the increase was just and
16 reasonable as there was insufficient evidence for it to justify the conclusion it arrived at.
17 (para 27). The Court of Appeal stated the following at paras 60-64:

18
19 60 In its order 143/04, the PUB expands on the concerns that drove it to the
20 decision it arrived at, and it is clear that in arriving at its order, the PUB was
21 concerned with the overall financial stability of Hydro as that stability had been
22 affected by the drought of previous years....

23
24 61 When one sifts through all of the material and arguments put forth by the
25 applicants in support of their position, it becomes more and more clear that
26 their arguments that the PUB failed to reach a “just and reasonable” rate is not a
27 matter of law but a dispute with the opinion at which the PUB arrived.

28
29 62 A review of the record demonstrates that the PUB did in fact review extensive
30 financial information and then exercised its discretion. **It may well be that the**
31 **PUB could not, or would not, review the specific financial tool that the**
32 **applicants argue it should have, but that is insufficient in my mind to justify a**

² Manitoba Hydro “came before you without bringing that fundamental element of a Hydro General Rate Application, an integrated financial forecast, of IFF, a tool which is essential in assessing the long-term reasonableness of any rate application”. (April 23, 2019, Transcript Page 50)

1 **finding that, as a whole, the PUB did not fix rates that were just and**
2 **reasonable.**

3
4 63 The intent of the legislation is to approve fair rates, taking into account such
5 considerations as cost and policy or otherwise as the PUB deems appropriate.
6 Rate approvals involve balancing the interests of multiple consumer groups with
7 those of the utility. The PUB's decision to build retained earnings more rapidly
8 than proposed in order to better protect the utility and consumers from the
9 financial impacts of a future drought, clearly meets the intent of the legislation
10 and is within the jurisdiction afforded the PUB in s. 26 of the Accountability Act.

11
12 64 The role of the PUB under the Accountability Act is not only to protect
13 consumers from unreasonable charges, but also to ensure the fiscal health of
14 Hydro. It is clear the PUB understood its role in this regard.

15
16 Manitoba Hydro submits that in making a determination in this Application, the PUB can
17 look to the current financial information before it and be satisfied that a 3.5% rate
18 increase is not only just and reasonable, but will also better position the Corporation to
19 address the impacts of Keeyask and its associated transmission coming into service. The
20 PUB has ample evidence before it of the impacts on revenue requirement, and the long
21 history of having reviewed, studied and analyzed these projects since the 2014 NFAT.
22 Indeed, MIPUG acknowledges that these impacts, and the need to transition to a higher
23 rate structure are relevant to the PUB's consideration in this proceeding. COALITION
24 experts also propose the option that if the PUB were to consider the impacts of Keeyask
25 for future potential rate volatility, the Board could grant the full rate request of 3.5% on
26 an interim basis (Exhibit CC-7-1, Page 10).

1 **3 HISTORICAL RATE PATHS**

2 During the 2017/18 & 2018/19 GRA, a number of scenarios were reviewed by
3 Intervenors. Order 59/18 sets forth the positions of those Intervenors:

4
5 *“According to the Consumers Coalition, the GRA evidentiary record demonstrates*
6 *that a 7.9% rate increase is more likely to harm Manitoba ratepayers and the*
7 *Manitoba economy compared to the impacts of a smoothed rate increase at or*
8 *below the 3.95% NFAT range. Smoothing rate increases at or below the 3.95%*
9 *NFAT range makes sense, according to the Consumers Coalition, given the long*
10 *lived and ‘lumpy’ nature of the Keeyask and Bipole III assets and considerations*
11 *of regulatory stability, intergenerational equity, risk, and affordable access to the*
12 *capital markets...” (PUB Order 59/18, Page 166)*

13
14 *“This Intervener submits that the rate increase for the 2018/19 Test Year could be*
15 *in the range of 2.95% to 3.5%, where the higher end of the range recognizes the*
16 *risks related to Keeyask costs and the lower end of the range would send a*
17 *message of accountability to the Utility for its forecasting inaccuracies.” (PUB*
18 *Order 59/18, Page 167)*

19
20 *“The Manitoba Industrial Power Users Group maintains the analyses*
21 *demonstrate that there is no overall financial deterioration compared to the*
22 *NFAT or the previous GRA and there is therefore no need to deviate from the*
23 *prior rate trajectory.” (PUB Order 59/18, Page 60)*

24
25 As shown in the evidence provided by COALITION’s consultants, the last five IFF’s that
26 have been used for rate setting purposes have shown significant variation in net income
27 in each of those forecasts (Exhibit CC-7-1, Page 50). The cumulative net income from
28 2021-2026 has ranged from a positive net income of \$1.095 billion in MH12 to a
29 cumulative net loss of \$772 million in MH14 with MH13 and MH15 showing cumulative
30 net income ranging from \$240 million to \$303 million respectively. All parties are aware
31 that when Manitoba Hydro forecasts net income, it is based on the best information
32 available at the time it is made. Parties are also aware however that those forecasts will
33 change. Water flows, export prices, interest rates, weather and customer demand will
34 all vary from what is forecast and cannot be guaranteed. What has been clear however
35 over the many forecasts is that, regardless of the variation in net income, the approach

1 to address the impacts of the major capital expansion has been to smooth rates to
2 promote rate stability and balance the fiscal health of Manitoba Hydro and the rate
3 impacts on customers over the long term.

4
5 As can be seen at page 14 of Exhibit 93 (Exhibit PUB-14, Page 17), during the needs for
6 and alternatives to proceeding before the PUB (“NFAT”), the financial evaluation which
7 provided for high capital cost for Keeyask and Level 2 demand side management
8 showed a comparative impact on future customer rates and showed rate increases
9 required of 3.95% in 2014/15 and indicative rate increases each and every year of 3.99%
10 from 2015/16 to 2031/32. The financial forecast prepared by Manitoba Hydro for
11 electric operations immediately following the NFAT (MH14), showed indicative rate
12 increases of 3.95% from 2015/16 through to 2030/31. Manitoba Hydro’s financial
13 forecast filed the following year for electric operations (MH15) also included indicative
14 rate increases of 3.95% from 2016/17 to 2028/29.

15
16 In considering Exhibit 93, the PUB stated *“the Manitoba Hydro Exhibit 93 Integrated*
17 *Financial forecast scenario results in equal annual rate increases of 3.57%. The Board*
18 *finds that with minor adjustments, this scenario is directionally consistent with the*
19 *Board’s decisions in this Order.”* (Order 59/18, Page 173)

20
21 Since the NFAT, each and every IFF and scenario run by Manitoba Hydro has included
22 variations in net income and has also recognized the need for steady annual rate
23 increases of more than 3.5% to address the impacts of major capital expansion.

24
25 In Order 73/15, the PUB finalized an interim 2.75% rate increase for fiscal 2014/15 and
26 awarded a 3.95% rate increase for fiscal 2015/16. In Order 59/16 the PUB approved an
27 interim 3.36% rate increase for fiscal 2016/17 which was finalized in Order 59/18. The
28 previous application before the PUB resulted in Order 59/18 where the PUB finalized
29 the interim rate increase for fiscal 2016/17, finalized an interim rate increase of 3.36%
30 for fiscal 2017/18 and awarded a final increase of 3.6% for fiscal 2018/19. Mr. Rainkie
31 has attempted to dismiss the rate paths in previous forecasts by suggesting that they
32 were the result of a “goal seeking exercise” to achieve a specific debt:equity target. The
33 PUB, in Order 59/18, declined to consider pace of achievement of a debt:equity ratio in
34 its decision to grant the 3.6% rate increase and Manitoba Hydro has not relied on the
35 achievement of a debt:equity target to support the current application.

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In addition, MIPUG suggests to Manitoba Hydro that in each of the previous IFFs there was a shortfall between the revenue generated by Keeyask and the expenses and that the shortfall was known and was going to be absorbed over time. Ms. Carriere responded:

"I would say that those -- we recognize that the forecasts are uncertain, that anything could happen. But those forecasts had in excess of -- I'm looking at it here - three point nine-nine (3.99), three point nine-five (3.95), four point one-four (4.14), four point three-four (4.34), and then three point five-seven (3.57).

Those all had in excess of 3 1/2 percent in there, and that was intended to address, despite the uncertainty going forward, that those rate increase -- those rate increases are needed to address the costs going into service."(Transcript Page 485)

The PUB has consistently granted rate increases over a number of years with a view of smoothing the impacts of the major capital projects coming into service. Manitoba Hydro submits that the PUB should not deviate from this approach for the current fiscal year.

1 **4 REASONS FOR APPLICATION**

2 **4.1 Keyask in Service is 18-28 Months Away**

3 As discussed in Manitoba Hydro’s Direct Evidence (Exhibit MH-25), an October 2020 in-
4 service date will result in the recognition of the additional carrying costs, primarily
5 finance and depreciation expense, beginning in the 2020/21 fiscal year. As outlined in
6 Manitoba Hydro’s response to PUB/MH I-9 Updated, the estimated carrying costs for
7 Keeyask and the associated transmission are approximately \$600 million to \$700 million
8 once fully in-service. As such, if Keeyask is commissioned 10 months ahead of schedule,
9 the period in which to smooth in customer rates will be condensed and without the
10 proposed 3.5%, the likelihood of a financial loss following an earlier in-service date for
11 Keeyask is exacerbated.

12
13 **4.2 Keyask Still Expected to be \$8.7 Billion**

14 Entering the 2018 construction season, the Keeyask Project required at least a 10%
15 improvement in performance by the General Civil Works Contractor (“GCC”) for the
16 remainder of their work and no substantive risks to materialize to achieve the control
17 budget of \$8.7 billion. At the start of 2018 the first unit in-service date (“ISD”) for
18 Keeyask was trending 4 to 6 months ahead of the control schedule (PUB/MH I-55a).

19
20 Strong performance in 2018 by the GCC has improved the schedule for the Keeyask
21 Project with the first unit ISD trending towards October 2020; 10 months ahead of the
22 control schedule. Schedule advances have helped to maintain the project costs and are
23 the main reason the project is now tracking to meet its control budget of \$8.7 billion.
24 While the Keeyask Project is currently trending to meet the control budget and
25 schedule, there are still significant risks remaining that could impact the cost and
26 schedule of the project.

27
28 During the 2017/18 & 2018/19 GRA, a number of key risks were identified including:
29 contractor performance; loss of site access/work stoppage due to a blockade or major
30 safety/environmental incident; unseasonable weather that shortens the summer
31 construction season; and unknown geotechnical/geological conditions at the South Dam
32 (PUB/MH I-56a). With the exception of the unknown geological conditions on the South
33 Dam, which has since been uncovered, the top risks for Keeyask will continue for the
34 duration of construction. If these risks were to materialize and significantly impact
35 construction, there could be schedule delays and cost increases to Keeyask. As noted by

1 Mr. Cormie at Transcript Page 411, had the August 2021 in-service date been
2 maintained, Manitoba Hydro would not have been able to achieve \$8.7 billion budget.

3
4 The challenge for 2019 will be to continue to meet and exceed the project plan as the
5 work becomes more complex and additional coordination between various contractors
6 and trades is required (PUB/MH I-55a).

7 8 **4.3 Variability in Net Income**

9 **4.3.1 Variability in Net Income Due to Water Flow Conditions**

10 At the time of filing the November 30, 2018 Application, Manitoba Hydro was projecting
11 net income for 2018/19 of \$51 million and, absent the proposed rate increase for
12 2019/20 was projecting a net loss of \$28 million from Electric Operations.

13
14 Based on the information available at the time of the Supplement, Manitoba Hydro's
15 projected net income was \$95 million for 2018/19 and \$64 million for 2019/20 absent a
16 rate increase. For 2018/19, the improvement in net income is primarily attributable to
17 changes in water flow conditions. Mr. Cormie testified that:

18
19 *"At the time our application was prepared, our expectation in the fall was that*
20 *the low-flow conditions that we had experienced all summer would continue*
21 *through the year. Statistically, that was the likely outcome. However, the*
22 *rainfall was above average. And by the time... we get into the second half of*
23 *October, we were – we were just modestly above – above average."* (Transcript
24 Page 78 and following)

25
26 For the 2019/20 fiscal year, the improvement in net income is reflective of a number of
27 factors including the higher starting water storage levels resulting lower power
28 purchases. The amount of energy in storage at the beginning of the fiscal year does not
29 diminish the potential variability in net export revenue over the ensuing twelve month
30 period. The most important contributor to water supply is the spring and summer
31 rainfall and on average, precipitation contributes 80 percent of the annual supply.

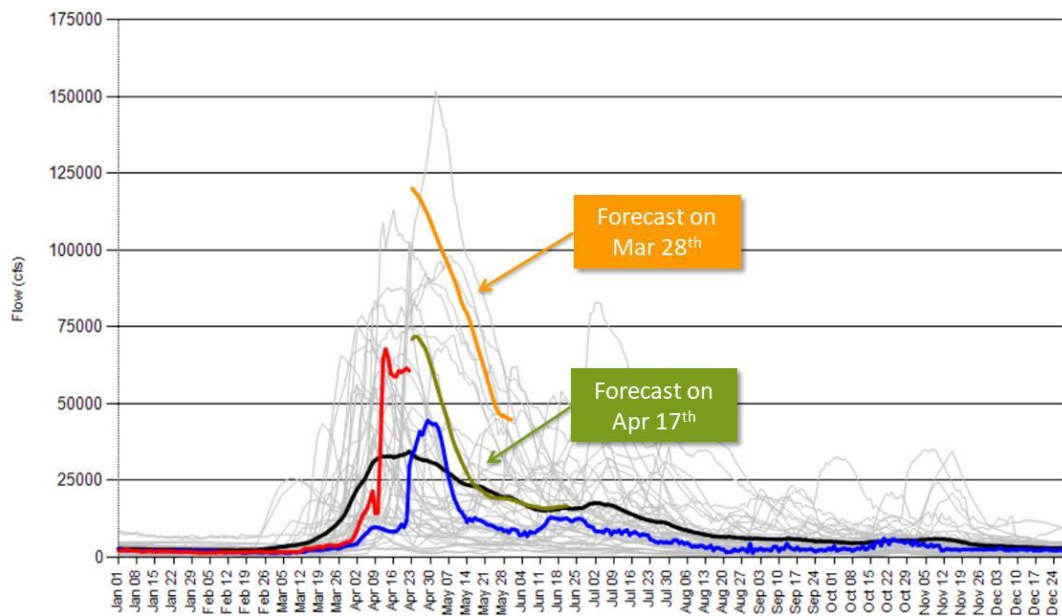
32
33 As explained by Mr. Cormie in his direct evidence, there remains significant uncertainty
34 in water supply for 2019/20 and significant risk of losses associated with below average

1 water flows. The Red River flood forecast is an example of how a forecast can change
2 dramatically in a very short time as explained by Mr. Cormie:

3
4 *“Rather than stretching well into June, as the initial flood had been indicated,*
5 *water levels are now expected to return to normal within a month or so. This is a*
6 *good example of the uncertainty we face just in the short term -- in the short*
7 *term, let alone what will happen over the next eleven (11) months on our other*
8 *major river systems.”* (Transcript Pages 80-81)

9
10 Slide 12 from Exhibit MH-25, shown below, demonstrates the marked change in the
11 spring flood forecast between March 28 and April 17, 2019.

12
13 **Example of Uncertainty - Red River Flow**



14
15 **Source: Exhibit MH-25, Slide 12**

16
17 Manitoba Hydro bases its forecasts on the average of revenues and costs using its long
18 term flow record. The graph presented in the response to COALITION/MH I-8, page 10
19 demonstrates that although opening storage balances for water reservoirs have
20 improved, there remains significant variability in the range of net export revenues which
21 Manitoba Hydro may ultimately generate over the course of the 2019/20 fiscal year.
22 The shaded area on the graph demonstrates the range of possible outcomes from P20
23 to P80. While Manitoba Hydro’s Approved Budget incorporates \$174 million in net

1 export revenue, the range of potential outcomes (P20 to P80) for the 2019/20 fiscal year
2 is approximately +/- \$75 million (Transcript Pages 197 – 199).

3
4 The impact of low flows are greater than high flows due to the requirements for
5 thermally generated and imported energy in low flow years and spilling of water beyond
6 system constraints in high flow years. Due to this asymmetry, the average revenues and
7 costs of the historic water flow record is equivalent to approximately the 40th
8 percentile or P40 and not the median or P50.

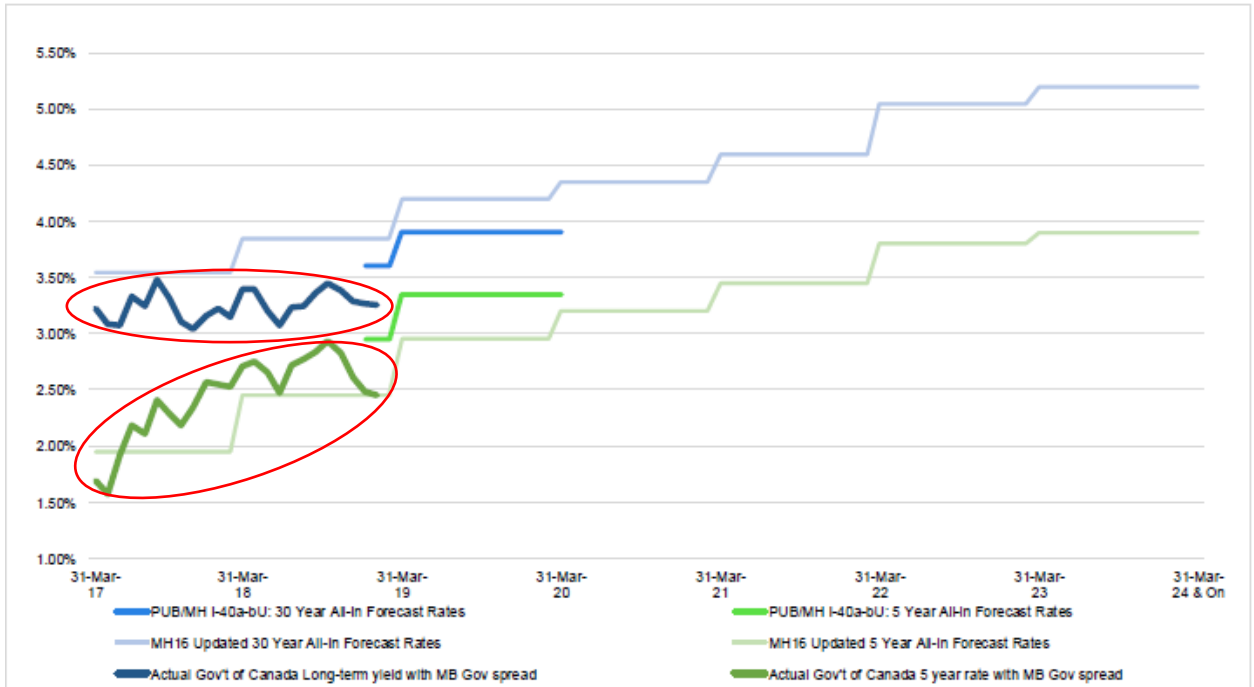
9
10 Manitoba Hydro uses the average or P40 net export revenues for planning purposes to
11 arrive at the net income contained in the 2019/20 Approved Budget. Without a rate
12 increase in 2019/20, Manitoba Hydro is projecting net income of \$64 million. If slightly
13 less than average (the 25th percentile or P25) water flow conditions are experienced in
14 2019/20, Manitoba Hydro's net income could be reduced by 75% lowering net income
15 to \$16 million. At transcript pg. 199-200, Mr. Epp explained the potential downside
16 impacts to net income as a result of the variability in net export revenue with and
17 without the 3.5% proposed rate increase.

18 19 **4.3.2 Interest Rate Risk**

20 As demonstrated in Exhibit 93 (Exhibit PUB-14, Page 8), Manitoba Hydro has
21 approximately \$4 billion of incremental borrowings to undertake over the next few
22 years to complete the major projects as well as approximately \$4.8 billion (Exhibit MH-
23 24, Page 12,) of debt requiring refinancing over the five year period following 2019/20,
24 all of which is subject to interest rate risk. As history has shown, today's interest rate
25 environment is not a good predictor of the future. It is impossible to predict interest
26 rates with certainty and interest rates do not remain static. At Transcript Page 229, Mr.
27 Epp explained that day-to-day fluctuations in interest rates can occur in reference to
28 Figure 4 of Exhibit MIPUG-5-3.

1

Figure 4 Exhibit MIPUG-5-3 (with actual variation denoted within red circles)



2

Source: Exhibit MIPUG-5-3

3

4

5

Borrowing requirements occur throughout the year and Manitoba Hydro has very little ability to delay issuing debt if the interest rate environment is not ideal. Also, Manitoba Hydro cannot influence or negotiate the rate of interest when the time comes to issue debt.

6

7

8

The majority of the financing costs associated with new debt issued over the next year will be capitalized and as such will not impact the revenue requirement until the major projects are in-service. However, this new debt will come at a cost to the utility. The future cost of the debt cannot be predicted with any certainty and 18 to 28 months from now will be expensed and recovered in rates.

9

10

4.4 Additional Sensitivities

11

In addition to the risks identified above, Manitoba Hydro is also exposed to the impacts of colder or warmer winter weather and higher or lower export prices than forecast. The table below from the response to COALITION/MH I-8b demonstrates the impacts of these key sensitivities on Manitoba Hydro's revenue.

12

13

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1 **Key Variable Sensitivity Impacts on 2019/20 Approved Budget Net Income/ (Loss)**
 2 **With and Without the 3.5% Proposed Rate Increase and a 1.0% and 2.0% Rate Increase**

	Projected Net Income/(Loss)			
	3.5% Proposed Rate Increase	No Rate Increase	1.0% Rate Increase	2.0% Rate Increase
Approved 2019/20 Budget	\$ 115 M	\$ 64 M	\$ 78 M	\$ 93 M
Low Water Flow (10th percentile net interchange revenues and generation costs)	(\$ 23) M	(\$ 75) M	(\$ 60) M	(\$ 45) M
High Water Flow (90th percentile net interchange revenues and generation costs)	\$ 202 M	\$ 150 M	\$ 165 M	\$ 179 M
Low Water Flow (20th percentile net interchange revenues and generation costs)	\$ 41 M	(\$ 10) M	\$ 4 M	\$ 19 M
High Water Flow (80th percentile net interchange revenues and generation costs)	\$ 191 M	\$ 139 M	\$ 154 M	\$ 168 M
Colder than normal winter weather	\$ 161 M	\$ 110 M	\$ 124 M	\$ 139 M
Warmer than normal winter weather	\$ 66 M	\$ 15 M	\$ 30 M	\$ 44 M
Low Export Price Case	\$ 91 M	\$ 39 M	\$ 54 M	\$ 68 M
High Export Price Case	\$ 188 M	\$ 136 M	\$ 151 M	\$ 165 M

3
4 **Source: COALITION/MH I-8a-g, Page 6**

5
6 As noted in Manitoba Hydro’s response, since actual debt issuances have been locked-in
 7 to December 31, 2018, the financial impacts to the 2019/20 Approved Budget are
 8 reduced since there is a smaller volume of new debt issuances exposed to fluctuations
 9 in interest rates. However, the full year's impact of a change in interest rates (+/- \$15
 10 million) would be realized in the 2020/21 fiscal year.

11
12 Much of the focus by MIPUG and COALITION has been on the “good news”. While
 13 certain assumptions and factors today point towards improvement in longer term
 14 forecast results, the reality is that forecasts have uncertainty and no one really knows
 15 what the future will bring. As has been noted by Manitoba Hydro, significant Keeyask
 16 cost and schedule risks remain and about a third of total project expenditures will be
 17 incurred over the next two to three years for which borrowings are exposed to interest
 18 rate risk. It seems counter-intuitive to gamble on uncertain future assumptions and
 19 factors when we know that the Keeyask in-service will result in a significant increase in
 20 costs.

1 As noted in Manitoba Hydro's Direct Evidence at slide 6, if financial results prove to be
2 more favourable than previously forecast, as a Crown Corporation any surplus revenues
3 remain in the Corporation for the benefit of its customers and reduce interest costs that
4 would otherwise be recovered in rates, unlike a privately-held utility, where those
5 surplus revenues may be paid to its shareholders as dividends.

1 **5 CONTROLLABLE COSTS**

2 **5.1 Operating & Administrative Costs**

3 Manitoba Hydro has made significant cost reductions primarily through an accelerated
4 workforce reduction strategy. Manitoba Hydro completed a Committed Position
5 Reduction program in March 2017, achieving a total reduction of 429 positions
6 compared to a commitment of 300 positions. The Corporation also launched the
7 Voluntary Departure Program (“VDP”) in April 2017 which resulted in a further
8 reduction of 821 staff over the 2017/18 and 2018/19 fiscal years, contributing to an
9 overall decrease in Operating & Administrative (“O&A”) costs of 7% between 2016/17
10 and 2018/19.

11
12 Further, as outlined in the response to PUB/MH I-19b, the total budgeted EFTs of 5878
13 in 2018/19 are comparable to those in 2004/05 of 5870 – 15 years ago and that the
14 Corporation is currently tracking below the 2018/19 EFT budget. As discussed in
15 Manitoba Hydro’s Direct Evidence (Exhibit MH-25, Page 16), Manitoba Hydro has
16 achieved comparability to 2004/05 EFT levels despite a 15% growth in the number of
17 electric customers, additional operational requirements for the Wuskwatim GS and the
18 Riel and Keewatinohk Converter Stations, aging infrastructure demands given assets are
19 15 years older and increased regulation including environmental, NERC, NEB and safety
20 regulations.

21
22 The O&A target for 2019/20 of \$511 million reflects an inflationary increase of 2%,
23 which is aligned with the Manitoba Consumer Price Index. The \$511 million O&A target
24 incorporates experienced deployment of staff between construction (capital) and
25 operations/maintenance activities (O&A), as well as known wage settlements. As
26 Manitoba Hydro has testified (Transcript Page 105), it has reviewed and re-validated the
27 appropriateness of the \$511 million target for 2019/20 considering current staffing
28 levels and business requirements. Mr. Rainkie’s recommendation for a 1% inflationary
29 increase between 2018/19 and 2019/20 (Exhibit CC-10, Slide 12) does not consider
30 these factors.

31
32 Mr. Rainkie at Transcript Page 741 suggests that the 1% inflationary increase be
33 achieved through 50% from staff attrition and 50% from supply chain savings. Manitoba
34 Hydro notes that given the departure of 900 employees through the VDP, attrition rates
35 are expected to be low as a substantive portion of those eligible to retire have left the

1 Corporation. As noted in the response to Undertaking #4, filed on April 30, 2019, supply
 2 chain savings have not materialized as planned and are predominantly related to capital
 3 expenditure reductions. Accordingly Manitoba Hydro cannot be expected to achieve the
 4 \$22 million O&A reduction as suggested by Mr. Rainkie.

5
 6 To illustrate the impact of achieving a \$22 million reduction in O&A, the table below
 7 shows that a reduction of 100 employees would equate to annual O&A savings of
 8 approximately \$7 million in the year following departure and a reduction of slightly over
 9 300 employees would be required to achieve the reduction in O&A as suggested by
 10 COALITION (Exhibit MH-24, Pages 6-7).

11
 12 **O&A Savings on a Reduction of 100 Employees**

Gross Savings for 100 employees <i>(in millions)</i>				
	One Time Departure Expense	Gross Salary & Benefit Savings	Net Savings before O&A/Capital Deployment	Estimated Impact to O&A*
Year 1 (Net Savings)				
One time Severance	(\$4.8)			
Salary & Benefit Savings		\$11.2		
Net Savings Year 1			\$6.4	\$4.1
Year 2 (Full Year Savings)				
Salary & Benefit Savings	\$0.0	\$11.2		
Net Savings Year 2			\$11.2	\$7.2
*Current Deployment Ratio (64% Operating/36% Capital)				

13
 14 **Source: Exhibit MH-24, Page 7**

15
 16 Transcript Pages 251-252, Ms. Bauerlein acknowledges that the net loss when Keeyask
 17 comes into service could be in the range of \$160 million under a best case scenario. The
 18 \$7 million O&A reduction will not have a significant impact on the net loss of \$160
 19 million.

20
 21 Prior to the decision to advance the staffing reductions and associated savings, the
 22 Corporation's previous cost reduction plan had been to limit the growth in O&A
 23 expenditures to 1% primarily through attrition with incremental cost increases for the
 24 operation of major capital infrastructure once in-service. As discussed in Manitoba

1 Hydro's response to PUB/MH I-20, the accelerated cost reduction plan has resulted in
2 overall annual O&A savings of \$70 million compared to the previous plan which was
3 acknowledged by Mr. Rainkie at Transcript Page 713.

4
5 Manitoba Hydro is committed to continue to streamline its operations and control costs
6 by limiting growth to inflationary levels, however further significant staffing reductions
7 cannot be sustained given the Corporation's mandate to ensure the safe & reliable
8 supply of electricity.

9 10 **5.2 Sustaining Capital (BOC)**

11 As discussed in the response to PUB/MH I-51b-c, Manitoba Hydro's capital expenditures
12 are operationally driven in support of the Corporation's responsibility to provide for an
13 ongoing safe and reliable supply of electricity to its customers. The operability and
14 sustainability of the system are continually being eroded by inevitable asset
15 degradation, shifting customer demands, and growing operational requirements, which
16 are mitigated through investment. The timing of investment is a complex risk decision
17 with significant cost and operational consequences. Only those investments associated
18 with unacceptable risks are advanced to execution.

19
20 The BOC target for the year is the aggregation of the cash flows for all of the
21 investments occurring in the 12 months of the fiscal year, which comprise thousands of
22 projects and program items (COALITION/MH I-30f). Variances to the approved annual
23 cash flow budget for a particular investment are driven by execution risks as outlined in
24 the response to PUB/MH I-52a-b. For example, rescheduling of equipment and material
25 deliveries, bid pricing on contracts, contractor performance and weather impacts can
26 result in differences in the timing of the annual cash flow compared to forecast. Thus,
27 the underspending of targets is related to uncertainty in the timing of the cash flows
28 required to deliver the investments rather than the scope and budget for the
29 investments needed to ensure the short term operability and long term sustainability of
30 the electric system.

31
32 As noted in Manitoba Hydro's response to COALITION/MH I-30a-b, a \$100 million in
33 Business Operations Capital in 2019/20 impacts expenses by \$11 million. Thus the
34 average variance of \$14 million suggested by the COALITION in their pre-filed evidence
35 (Exhibit CC-7-1, Page 72) for 2019/20 would impact expenses by \$1.5 million.

1
2 Ultimately, the COALITION has not made a quantitative rate-setting adjustment on
3 account of a reduction to Business Operations Capital (Transcript Page 737). However,
4 similar to reductions in O&A, Manitoba Hydro submits that cutbacks to the
5 Corporation's capital program will not address the revenue shortfall once Keeyask is in-
6 service and would place significantly greater risk to the reliability of the electrical
7 system.

8 9 **5.3 DSM Costs and Impacts are Appropriately Reflected in Manitoba Hydro's Revenue** 10 **Requirement**

11 In PUB Order 59/18, the PUB recommended that Manitoba Hydro review its demand
12 side management programming for cost effectiveness and cease or modify spending on
13 programs that are no longer cost effective, except for programs targeted at lower-
14 income and First Nations on-reserve consumers. Ms. Morrison testified that:

15
16 *"We did not undertake an analysis of our one-year plan from a cost-effective*
17 *perspective. I should probably characterize that in the past, when Manitoba*
18 *Hydro has come before this Board and presented DSM plans and those plans*
19 *included a cost-effective analysis, that cost-effective analysis was based on a*
20 *fifteen (15) year plan. And so when you're looking at entering into the market*
21 *and building uptake of an efficient technology or measure in the marketplace,*
22 *you're not in it for a year. You're looking at building that over time.*

23
24 *And so to try and characterize a one-year plan and whether or not it's cost*
25 *effective really isn't the best approach to take, and it isn't one that I would*
26 *recommend. You'd be wanting to look at: What is the long-term projection of*
27 *cost effectiveness for engaging in this marketplace?*

28
29 *And so we did not -- given that Manitoba Hydro is not the one that's preparing*
30 *the long-term plan for demand-side management, we are simply, as I've stated,*
31 *maintaining the programs that are in place and continuing those offerings in the*
32 *marketplace while we transition to Efficiency Manitoba, and then Efficiency*
33 *Manitoba will come before this Board, as per the legislation, presenting a three-*
34 *year plan, outlining how they anticipate to meet the targets that are outlined in*
35 *the legislation."*

1 (Transcript Pages 393-394)

2
3 Mr. Bowman in his Evidence asserts that, *“Absent a properly prepared DSM program*
4 *reflecting up-to-date and fully tested marginal costs, it should be assumed that the DSM*
5 *programs underlying both the 2019/20 forecast and the Exhibit MH-93 forecasts include*
6 *higher spending levels than should be accepted into customer rates.”* (Exhibit MIPUG-5-
7 1, Page 19)

8
9 Manitoba Hydro has updated projections for the 2019/20 test year. The 2019/20
10 Approved Budget reflects a reduced budget of \$61 million and lower projected energy
11 savings of 232 GWh (COALITION/MH I-32c-iii) based upon the preliminary update to
12 2019/20 Demand Side Management activities as noted on page 1 of the Supplement to
13 the 2019/20 Electric Rate Application filed on February 14, 2019. This update was
14 developed based on a status quo approach and continuation of current DSM program
15 offerings based upon consultations with the Province as outlined under the Energy
16 Savings Act and, as such, are appropriately included within the 2019/20 Electric Rate
17 Application.

18
19 In addition, as Ms. Morrison testified, Manitoba Hydro is confident that the programs
20 currently offered to customers remain cost effective under the lower marginal values
21 even without an updated analysis.

22
23 *“...the programs that are currently available to customers that they can enroll in*
24 *today, I would -- and you compare their levelized cost that was presented under*
25 *the 2016 long-range plan to that five point seven (5.7) cents levelized marginal*
26 *value, to give you a kind of a broad in -- indication as to whether those current*
27 *programs would still remain cost-effective under the total resource cost test*
28 *which is the test that we've used historically to determine cost effectiveness of*
29 *our programs, you would see that the vast majority of those programs, using*
30 *that indicative value, do remain cost- effective. ...”* (Transcript Page 460)

31
32 Efficiency Manitoba is preparing to assume its role in determining and managing the
33 programs to be offered. As Ms. Morrison noted at Transcript Pages 466-467, it is
34 expected that provincial regulations will be developed to provide guidance to the Board
35 and to Efficiency Manitoba, including defining cost effectiveness. Given *The Efficiency*

1 *Manitoba Act* specifies a savings target 1.5% annually over the next 15 years and has not
2 yet provided the guiding regulations, Manitoba Hydro believes that the projections
3 included within this Application are appropriate in order to establish rates for 2019/20.

1 **6 CASH FLOW SUFFICIENCY**

2 As Mr. Bowman stated, “Customers need financially sufficient Hydro...” (Exhibit MIPUG-
 3 7, Page 3) and a “financially sufficient Hydro” should be defined as a utility that can
 4 generate enough cash flow from operations to cover both its interest payments and its
 5 business operations capital, at a minimum.

6
 7 On page 13 of Exhibit MIPUG-5-1, Mr. Bowman declares that Manitoba Hydro’s cash
 8 flow from operations in 2019/20 is sufficient even without a rate increase while making
 9 no mention of the impending end to large amounts of capitalized interest once the
 10 major projects are complete. Regardless of whether capitalized interest should be paid
 11 by cash from operations or not, once Keeyask and the associated transmission come
 12 into service, 18 to 28 months from now, none of this matters. The vast majority of
 13 interest currently being capitalized (approximately \$300 million of the \$1 billion of gross
 14 interest in 2019/20) will be expensed and will need to be recovered in rates. For that
 15 reason, preparing for this known fact today is the prudent course of action.

16
 17 The second column in the table below (Exhibit MH-24, Page 9,) indicates that even with
 18 a 3.5% rate increase in 2019/20, the utility will be challenged to cover the \$1 billion of
 19 interest payments (which will increase as the Corporation is expected to borrow an
 20 additional \$4 billion to complete the major projects) and cover its business operations
 21 capital evidenced by the \$197 million cash deficit.

22
 23 **Cash Provided by Operating Activities Without and With Capitalized Interest on Major**
 24 **Projects Comparison**

(In Millions)

	2019/20	
	Without Capitalized Interest on Major Projects	With Capitalized Interest on Major Projects
Cash Receipts from Customers	\$2,187	\$2,187
Cash Paid to Suppliers	(843)	(843)
Interest Paid	(1,029)	(1,029)
Capitalized Interest	20	312
Interest Received	16	16
Cash Paid to the City	(16)	(16)
Cash Paid to Mitigation	(54)	(54)
Cash Provided by Operating Activities	281	571
Business Operations Capital	(478)	(478)
Surplus/(Deficit)	(197)	93

25
 26 **Source: Exhibit MH-24, Page 9**

1 **6.1 Moody’s Potential Reassessment of Manitoba Hydro’s Self-Supporting Status**

2 Mr. Bowman asserts in his pre-filed evidence at page 6 that, “*negative net income is not*
3 *in and of itself evidence of heading towards a ditch.*” In Manitoba Hydro’s Rebuttal
4 Evidence (Exhibit MH-24, Page 4), the Corporation indicates financial metrics are
5 weakening as a result of minimal net income and cash flow and escalating debt levels.
6 These weakening financial metrics have garnered additional scrutiny from the credit
7 rating agencies.

8
9 The EBIT acronym stands for Earnings Before Interest and Taxes. By removing interest
10 expense, EBIT represents the approximate amount of operating income generated by a
11 business to fund Gross Interest payments.

12
13 The EBITDA acronym stands for Earnings Before Interest, Taxes, Depreciation and
14 Amortization. By removing Depreciation and Amortization from the EBIT calculation, all
15 non-cash expenses are deleted from operating income. In Manitoba Hydro’s case,
16 Depreciation is approximately equal to the amount that Manitoba Hydro spends
17 annually on Business Operations Capital (“BOC”). As such, cash flow generated by
18 operations must, at a minimum, fund Gross Interest payments as well as Business
19 Operations Capital in order for Manitoba Hydro to be self-sufficient.

20
21 According to Moody’s EBIT interest coverage metric below, Manitoba Hydro will have a
22 cash shortfall of approximately \$300 million dollars and will be unable to service
23 approximately 30% of its outstanding debt servicing costs. It is partly for this reason that
24 Moody’s is currently reassessing Manitoba Hydro’s self-sufficiency. Absent sufficient
25 rates, the metrics will continue to worsen.

1 **Moody's Calculation of Earnings and Interest**

In Millions of Dollars	2020
Rate Increase	3.50%
Consolidated Net Income	\$121
Consolidated EBIT	\$612
Gross Interest	\$886
Surplus/(Deficiency)	(\$274)

2 **EBIT / Gross Interest** **0.7**

3 **Source: Exhibit MH-24, Page 5**

4

5 In addition, the Moody's report references an EBITDA interest coverage of 1.2 times.
6 Manitoba Hydro quoted from the Moody's December 24, 2018 report in its Direct
7 Evidence (Exhibit MH-25, Slide 22) that, "...these financial metrics are among the
8 weakest, if not the weakest, of any of Manitoba Hydro's peers...".

1 **7 RATES/REGULATORY PROCESS**

2 **7.1 COALITION – Robust Compliance and Directives filing with Intervenor Participation**

3 In the evidence prepared by Darren Rainkie, William Harper and Kelly Derksen on behalf
4 of COALITION, it was suggested that the PUB consider the COALITION’s comments and
5 recommendations with respect to the compliance and directives process for
6 implementation prior to the next GRA. It argued that Intervenors have a significant role
7 to play in clarifying the scope of a PUB directive, suggesting alternative approaches and
8 resources to satisfy the directive, assisting the PUB and Manitoba Hydro in determining
9 the priority and timing of the directive and assisting in determining the intent of a
10 particular directive (Exhibit CC-7-1, Page 141).

11
12 As was noted in Manitoba Hydro’s correspondence of August 1, 2018, Intervenors bring
13 value to the regulatory process by testing the evidence of Manitoba Hydro through
14 information requests, presenting its own consultants evidence, through cross
15 examination and providing their arguments during the process. This was contemplated
16 in Part IV of the Crown Act where in the process of a hearing the PUB may take into
17 consideration

18
19 **Factors to be considered, hearings**

20
21 **25(4)** In reaching a decision pursuant to this Part,
22 The Public Utilities Board may

23
24

25
26 (b) hear submissions from any persons or groups or classes or
27 persons or groups who, in the opinion of the Board, have
28 an interest in the matter.

29
30 It is clear that the legislature contemplated participation by Intervenors during the
31 course of a review of an application seeking a change to rates for service. The
32 legislation however does not contemplate continued participation by Intervenors in
33 terms of interpreting PUB Orders or directives. The PUB is an administrative tribunal
34 whose decisions are granted deference because of their expertise in the matters. The
35 PUB speaks through their Orders and it takes the position of Intervenors into

1 consideration when it issues its findings and direction contained in its Orders. The PUB
2 Orders are final and it is not the role of Intervenor to clarify the scope of such
3 directives, or to determine the approach of the Corporation to responding to such
4 directives. While the PUB may accept a recommendation suggested by an Intervenor, it
5 is not appropriate for an Intervenor, following the conclusion of a hearing, to provide
6 comments on its interpretation of a PUB directive based on positions taken during the
7 course of a hearing. It is also inappropriate for an Intervenor to attempt to speak for the
8 PUB.

9
10 It would be extremely concerning if the PUB requires intervenors assistance, input or
11 recommendations or required Intervenor to interpret the PUB's intent as set forth in a
12 directive. As the regulator, the PUB drafts its Orders and is the only party that can
13 determine its intent, requirements and whether Manitoba Hydro has complied with the
14 PUB's directives.

15 16 **7.2 Rate Design and the Cost of Service Study**

17 As indicated by Manitoba Hydro in the response to COALITION/MH I-41, Manitoba
18 Hydro continues to use its established rate design principles and guidelines when
19 proposing rates. Manitoba Hydro's rate design principles, which were provided in
20 Attachment 1 of COALITION/ MH I-41 include:

- 21
- 22 • Recovery of revenue requirement
- 23 • Fairness and Equity
- 24 • Rate Stability and Gradualism
- 25 • Efficiency
- 26 • Competitiveness of Rates
- 27 • Simplicity and Understandability
- 28

29 The priority given to the various principles is determined with consideration to the
30 prevailing circumstances at the time of each rate application. While the current
31 proceeding may be unique in its one year focus, the prevailing circumstances since NFAT
32 have been that Manitoba Hydro requires annual rate increases in order to recover its
33 revenue requirement and ensure rate stability while gradually transitioning customer
34 rates to the levels necessitated by adding Bipole III, Keeyask and associated transmission
35 into rate base.

1
2 Manitoba Hydro has requested that the proposed 3.5% rate increase be applied equally
3 across all customer classes excluding the non-grid equivalent Diesel general service and
4 government rates. Manitoba Hydro proposed applying the increase to all components
5 of the rates monthly basic charges, energy charges and demand charges.
6

7 The recommendation to apply the increase on an across the board basis appear to be
8 generally accepted by COALITION and MIPUG, with only minor exceptions.
9

10 While a Prospective Cost of Service Study (“PCOSS”) was not provided to support rate
11 differentiation at the time of the initial application, Manitoba Hydro did provide an
12 interrogatory response demonstrating the significant impact on class Revenue to Cost
13 Coverage (“RCC”) ratios due to Bipole III coming into service (PUB/MH I 61a). The
14 analysis indicates that the addition of the significant Bipole III assets would move most
15 classes to within the zone of reasonableness (“ZOR”), with only General Service Small –
16 Non Demand and Area & Roadway Lighting above 105%.
17

18 Mr. Bowman accepted the directional impact shown for the large General Service
19 classes in this revised PCOSS (COALITION/MIPUG I-5). However Mr. Bowman
20 characterized the adjustments to the PCOSS as “coarse”, and questioned the reliability
21 of the results for use in rate differentiation. Mr. Bowman therefore concurred in the
22 recommendation that any rate increase be applied on an across-the-board basis (Exhibit
23 MIPUG-7, Slide 15).
24

25 The experts for the COALITION appear to generally accept both the revised PCOSS
26 results as well as support the use an across the board rate increase, noting “*the addition*
27 *of Bipole III will result in most class RCCs to be within the ZOR and thus, it is reasonable*
28 *that any rate increase granted be applied on an across-the-board basis*” (Exhibit CC-7-1,
29 Page 128)
30

31 However, Ms. Derksen goes on to recommend that since the General Service Small Non-
32 Demand class has persistently remained outside the ZOR the class should receive a less
33 than average increase.
34

1 Manitoba Hydro concurs with Ms. Derksen that there is a strong likelihood that due to
2 the current RCC differential the General Service Small Non-Demand class cannot be
3 brought into the ZOR while maintaining the current consolidated rate structure with the
4 General Service Small Demand and General Service Medium classes. However,
5 Manitoba Hydro's recommendation to apply the proposed increase on an across-the-
6 board basis is not an indication that Manitoba Hydro is putting a priority on class
7 consolidation over RCC adjustments but rather is prioritizing rate stability in the near
8 term until possible rate alternatives can be evaluated.

9
10 In the near term (1-2 years) it is likely possible to maintain the current rate structure
11 and implement a lesser than average increase for the General Service Small Non-
12 Demand class but it will depend on the level of differentiation. As Ms. Carriere testified
13 at Transcript Pages 290-292, due to the load characteristics of the classes, a less than
14 average increase for the General Service Small Non-Demand class will result in a less
15 than average increase for the General Service Small Demand class and a higher than
16 average increase for the General Service Medium class.

17
18 Furthermore as discussed in the response to PUB/MH I-61b and in Manitoba Hydro's
19 Rebuttal Evidence at page 16, to effect the differentiation would require a rebalancing
20 of customer, energy and demand charges which will have intra-class impacts, may mute
21 appropriate price signals and may exacerbate rate rebalancing requirements in the
22 future. While Manitoba Hydro could develop rates that would yield overall class revenue
23 resulting in RCCs falling within the ZOR the underlying rate components may not yield
24 price signals or customer impacts that are aligned with cost causation and the outputs
25 of the COSS. In light of this, Manitoba Hydro submits that the most appropriate course
26 for the current Application is to implement the average rate increase to the General
27 Service Small Non-Demand class until an analysis of class cost characteristics, load
28 profiles, and bill frequencies is completed.

29
30 The experts for the COALITION also recommend extending the rate increase to include
31 the non-grid equivalent Diesel rates due to an RCC for the overall diesel class in the
32 order of 80% (Exhibit CC-7-1, Page 109). As noted by Manitoba Hydro, the RCC for the
33 Diesel class in the PCOSS lacks a number of key refinements which are included in the
34 Diesel COSS used to determine the non-grid equivalent diesel rates. Adjusting the Diesel
35 class for these items would increase the RCC shown in the PCOSS to greater than 100%,

1 and indicates that increasing non-grid equivalent Diesel rates in the absence of a Diesel
2 COSS is not warranted. (Exhibit MH-24, Pages 16-17)

3
4 The expert for AMC was silent on the issue of rate rebalancing with the exception of the
5 rate freeze for the First Nation On Reserve class which will be discussed in Section 6.3.

6
7 Manitoba Hydro intends to continue the migration of customer classes into the ZOR in
8 its next GRA, based on the results of its next PCOSS. The across-the-board increase
9 proposed as part of this Application will not negatively impact the migration of class
10 revenues that has been achieved to date following the implementation of differentiated
11 rates approved by the PUB in Order 59/18.

12 13 **7.3 First Nation on Reserve**

14 As directed in Order 59/18, Manitoba Hydro created a First Nation On-Reserve customer
15 class and held the rates for this class at the August 1, 2017 approved rates. Manitoba
16 Hydro sought to Review and Vary this Order and subsequently filed a Motion with the
17 Court of Appeal seeking Leave to Appeal portions of Order 59/18 and 90/18 with
18 respect to the creation of the new customer class. While this issue remains before the
19 Court of Appeal, Manitoba Hydro has not sought to eliminate this customer class or to
20 adjust the rates being sought from this class to include the rate freeze awarded by the
21 PUB in Order 59/18.

22
23 Consistent with Manitoba Hydro's approach to apply the rates equally across all
24 customer classes, Manitoba Hydro is also proposing to apply the 3.5% increase to the
25 First Nation On-Reserve customer class. This will maintain the current rate differential
26 between the First Nation On Reserve customer class at 4.04% pending the decision of
27 the Court of Appeal. Manitoba Hydro respectfully submits that until such time the Court
28 of Appeal renders its decision, rates should not be differentiated further. This will
29 mitigate hardship to this class should the appeal be successful by maintaining the
30 current rate differential between the First Nation On-Reserve customer class and the
31 Residential customer class. Should the Court of Appeal dismiss Manitoba Hydro's leave
32 application, any further differentiation which the PUB determines is appropriate can be
33 addressed in a subsequent rate review.

1 Manitoba Hydro acknowledges the potential impact of the requested rate increases to
2 lower income and First Nation on-reserve customers. As outlined by Ms. Morrison at
3 Transcript Pages 526-527, Manitoba Hydro continues to offer bill affordability and
4 energy efficiency programming to help customers in managing their energy costs,
5 including the recent introduction of a pilot arrears management program which allows
6 customers to enter into a long term budget plan to provide for payment of bill arrears
7 over up to 36 months with no late payment charges on the arrears.

8 9 **7.4 Deferral Accounts**

10 Following the review of an application for rates requested by Manitoba Hydro for the
11 2012/13 and 2013/14 fiscal years, the PUB established a deferral account to address the
12 impacts of Bipole III when the project was placed in service. At page 10 of Order 43/13,
13 the PUB determined:

14
15 *“Manitoba Hydro is to establish a deferral account in which the revenues from*
16 *the 1.5% increase accrues until further Order of the Board (2% to general*
17 *revenues + 1.5% to deferral account = 3.5%. The capital deferral account is to*
18 *assist in funding the planned Bipole III transmission line. The cost of this project*
19 *will be capitalized during the construction phase, but significant annual*
20 *depreciation, operation, maintenance & administration, and interest costs will*
21 *have to be recovered from domestic ratepayers once the project is placed in-*
22 *service. The deferral account allows Manitoba Hydro to collect funds as the*
23 *Bipole III project is being built, which will help to mitigate rate increases required*
24 *once the infrastructure is placed in-service.”*

25
26 At Transcript Page 300, Ms. Stephen noted that the rating agencies viewed the Bipole III
27 deferral account favourably.

28
29 While Manitoba Hydro continues to have concerns regarding further erosion of its
30 financial position due to the remaining potential for a loss in 2019/20, Manitoba Hydro’s
31 main concern is with reducing overall borrowing requirements and associated debt
32 service costs for its customers in the longer term while maintaining rate stability. The
33 accrual of revenues to a Keeyask deferral account, if directed by the PUB, achieves this
34 objective and would be acceptable.