MANITOBA PUBLIC UTILITIES BOARD

MANITOBA HYDRO

2023/24 & 2024/25 GENERAL RATE APPLICATION

Revenue Requirement Evidence

Prepared By

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On Behalf of

The Consumers Coalition

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1.0 Executive Summary

In its 2023/24 and 2024/25 General Rate Application (GRA or Application), Manitoba Hydro (MH) is requesting final approval of the 3.6% interim rate increase that was effective January 1, 2022 2021/22 Test Year) and PUB approval of further overall rate increases of 2.0% on September 1, 2023 (2022/23 Test Year) and April 1, 2024 (2024/25 Test Year).

MH is requesting that the overall revenue increases be recovered based on differentiated rate adjustments by customer class – that range from 1.0% to 2.4% for both Test Years. Residential rate increases of 2.4% are proposed for both Test Years.

This GRA is the first to be filed by MH since the 2018/19 GRA in 2017. It includes a long-term financial forecast, prospective cost of service study, detailed Operating & Administrative Expense (O&A) budgets and a comprehensive response to prior Public Utilities Board of Manitoba (PUB) directives.

The purpose of this evidence is to independently evaluate MH's revenue requirement proposals and provide observations, conclusions and recommendations to the PUB, for rate-setting purposes.

1.1 The Modified Cost of Service Rate-Setting Methodology Requires Substantial Judgement to Balance the Interests of Customers with the Financial Health of MH

In contrast to formulaic rate-setting methodologies used to set utility revenue requirements, the modified cost of service (MCOS) rate-setting methodology that has been used to set MH rates for decades has a focus on rate smoothing.

Under the MCOS, revenue requirements in the current test year(s) are set by making judgements with respect to the pace of attainment financial targets and risks, the necessary and prudent level of costs to include in rates and the appropriate use of regulatory deferral accounts - over the financial planning horizon. The judgement used by the PUB under the MCOS is designed to fulfill its mandate of balancing the interests of customers with the financial health of MH.

1.2 An Independent Evaluation Does Not Support the MH Proposed 2% Rate Path as Appropriately Balancing the Interest of Ratepayers with the Financial Health of MH

The overall conclusion of the independent review of MH's revenue requirement proposals is that the evaluation does not support MH's proposed 2% rate path as appropriately balancing the interest of ratepayers with the financial health of MH.

The key aspects underpinning MH's revenue requirement proposal of a 2% rate path for the 20-year forecast period was independently evaluated, including (i) the impacts of Strategy 2040 (ii)

MH's risk assessment (iii) MH's proposals on financial targets (iv) MH's asserted commitment to cost control through its O&A and Business Operations Capital (BOC) forecasts (v) MH's revised Debt Management Strategy (DMS) and (vi) MH's proposals for the use of Regulatory Deferral Accounts (RDA).

The conclusions from these evaluations can be summarized at a high-level as follows:

1. **Strategy 2040** is a work in progress and there are too many concerns and unknowns for the PUB to fully accept it for rate-setting purposes at this time. Strategy 2040 appears to be premature, unfocused and potentially unnecessary pending the outcomes of a Manitoba Energy Policy and a new Integrated Resource Plan (IRP). It is contributing to upward pressures on rates as a result of $2.3 billion of increased spending since the last MH GRA;

2. A relative assessment of risks since the last GRA does not support the high-level **MH risk assessment** of elevated business and financial risks for rate-setting setting purposes. MH's risk assessment is incomplete and does not consider the reduced risk from the in-service of the major capital projects, the substantial improvement in MH's financial outlook since the last GRA, MH's own risk quantifications and the value of a hydro-electric system under climate change policy. Moreover, MH's risk assessment is inconsistent with past PUB policy direction that financial reserves will only be increased through increased rates, when and if emerging risks actually materialize;

3. It is recommended that primary weight be placed on past PUB policy direction and the use of **traditional financial metric and targets for rate-setting purposes** rather than relying on MH's mechanistic goal seek of a 2% rate path to attain a 40% debt ratio by 2039/40. The PUB has ruled that the new legislative framework that includes debt ratio targets is not yet operative for this GRA. Even if it was to be considered, MH's positioning that the proposed 2% rate path is a requirement under this framework is an overstatement. MH's proposed 2% rate path results in a capital structure (debt to equity ratio) at the end of the forecast period that is approaching that of an investor owned utility (IOU) and exceeds the debt targets in the new legislative framework;

4. The **$2.3 billion cumulative increase in O&A and BOC forecasts** since the last GRA is significantly related to Strategy 2040 and associated initiatives. These levels of spending are inconsistent with and unresponsive to prior PUB findings and regulatory signaling to MH to (i) control and prioritize controllable costs in an era of rate pressures associated with the major capital projects and (ii) implement a mature asset management process to prioritize and justify capital costs. The projected $175 million or 34% increase in O&A between 2019/20 and 2024/25 represents an average growth rate of 6.1% and does not demonstrate a MH commitment to O&A cost control. These increases are contributing to a $1.5 billion increase in cumulative O&A costs since the last GRA. The $0.8 billion

cumulative increase in the BOC forecast since the last GRA demonstrates that $0.5 billion in expenditures relate to Strategy 2040 initiatives, which appear to be prioritized over sustaining capital expenditures;

5. MH's **revised Debt Management Strategy** and reduced tolerance to treasury risks are unnecessarily increasing forecasts of Finance Expense for rate-setting purposes. Current levels of net debt ($23 billion) and projected debt maturities in the next 10 years ($1.1 billion per year) are prompting policy changes by MH to reduce tolerances for interest rate risk and floating rate debt levels and for the maintenance of multiple layers of liquidity protection. These policy changes are increasing Finance Expense, despite MH own assessments that forecast debt maturities are well within interest rate risk guidelines and represent reasonable levels of debt concentration. They are out of step with updated independent analysis and peer group comparisons that suggest that MH should maintain higher levels of floating-rate debt (with a lower forecast cost) and improved liquidity through the larger $1.5 billion short-term debt facility; and

6. It is recommended that considerations of rate stability and intergenerational equity be afforded the most weight by the PUB in approving **Regulatory Deferral Accounts** (RDA's) for rate-setting purposes. Less weight should be provided to MH's objective to reduce the reliance on RDA's, given that they represent less than 5% of MH's total assets. Recommendations are made on all of the MH RDA proposals, the most significant of which are the SAP RDA and Depreciation RDA's. It is recommended that the PUB leave the establishment of an SAP RDA to MH's own decision making and interpretation of IFRS standards (rather than granting PUB pre-approval), given the lack of justification and business cases related to the projected $156 million of expenditures. In addition, if a final determination on depreciation methods for rate-setting cannot be reached in this proceeding, there are pragmatic options available to the PUB to continue the deferral of depreciation differences and commence the amortization of the resulting RDA's over reasonable periods of time (which would slightly increase RDA's to 6.4% of MH's totals assets).

The above noted MH's proposals, policies and cost forecasts all underpin MH's reasons for the Application and proposed 2% rate path and are evaluated as not appropriately balancing the interest of ratepayers with the financial health of MH.

1.3 Three Analytical Perspectives Result in a Continuum of Between a 0% and 1.5% Rate Increase on April 1, 2024 to More Appropriately Balance the Interests of Ratepayers and MH's Financial Health

Three analytical perspective were evaluated and result in a continuum of between a 0% and 1.5% rate increase on April 1, 2024, as a recommendation to the PUB to more appropriately balance the interests of ratepayers with the financial health of MH. This recommendation also includes consideration of more active cost containment on the part of MH.

The above noted conclusions from the evaluation of the key aspects that underpin MH's revenue requirement proposals were then used to inform the analysis of financial information on the record of this proceeding, from three distinct analytical perspectives:

1. Do the financial metrics in the 2023/24 and 2024/25 Test Years justify 2% overall rate increases in and of themselves;
2. Rate-smoothing in the 20-year financial forecast period to 2041/42; and
3. Longer-term intergenerational equity considerations for the 30-year period between 2011/12 and 2041/42.

The results from **analytical perspective #1 (Test Year Only Analysis)** is that there is no justification for 2% rate increases in the forward 2023/24 & 2024/25 Test Years, based on traditional rate-setting metrics, contained solely in the Test Years themselves. These metrics are all above long-standing targets or showing progress towards the attainment of longer-term targets used for rate-setting purposes.

The results from **analytical perspective #2 (20 Year Rate Smoothing Analysis)** is that a single 1.2% to 1.5% rate increase on April 1, 2024 and similar indicative annual rate increases in the forecast period, together with active cost containment on the part of MH - represent a more appropriate balancing of the interest of customers with the financial health of MH. This range of rate increase is most consistent with MH's status as a Government Business Enterprise (GBE) with a Provincial debt guarantee and the preliminary and uncertain nature of significant expenditures on Strategy 2040 and related initiatives. This range of rate increase is more aligned with prior policy directives and regulatory signalling from the PUB with respect to risks, appropriate financial metrics and the need for cost containment, as well as considerations of public acceptance of rate increases in a year when MH expects to post a record level of net income.

The results from **analytical perspective #3 (Longer-term Intergenerational Equity Over 30-years)** would suggest the potential for a mid-term course correction in the form of a rate pause for current customers in the forward Test Years (2023/24 and 2024/25) for a more even distribution of funding the costs of the major capital projects. This analysis points to the potential intergenerational inequity between current and future ratepayers. Current ratepayers have paid average annul rate increases in the order of 3% in the last 12 years, for the most part without the benefit of the major capital projects being in-service. Future ratepayers for the next 19 years are

projected to pay average annual rate increases of 2% or less and are receiving the benefits of the major capital projects now being in service.

The three analytical perspectives result in a **continuum of between a 0% and 1.5% rate increase on April 1, 2024**, as a recommendation to the PUB to more appropriately balance the interests of ratepayers with the financial health of MH. This recommendation considers the need for more active cost containment

1.4 It is Recommended that the PUB Approve a Single Overall Rate Increase of 1.3% Effective April 1, 2024 & Confirm the 3.6% Interim Rate Increase that Was Effective January 1, 2022 as Final

It is recommended that the PUB approve a single overall rate increase of 1.3% effective April 1, 2024 and confirm the 3.6% interim rate increase that was effective January 1, 2022 as final.

MH's proposed 2% rate path is based on a goal seeking exercise to attain a 40% debt ratio in 2039/40 under the new legislative framework that is not to become operative until April 1, 2025.

The PUB has ruled that the current GRA is to be reviewed under the existing legislative framework. The MCOS rate-setting methodology that has been used to set MH rates for decades contains no rules-based or formulaic rate-setting framework that can be used to exactly specify a precise overall rate increase recommendation for the forward Test Years. Judgement must be exercised in order to balance the interests of customers with the financial health of MH.

Providing some weight to each of the three analytical perspectives, but the most weight to the PUB's policy of rate smoothing and requirements of active and prudent cost control, results in a **recommendation of a single 1.3% overall rate increase on April 1, 2024** and **final confirmation of the 3.6% interim rate increase** that was effective January 1, 2022.

The cumulative overall rate increase that results from these recommendations is 4.94%[1], which when considered over the four test years that are the subject of this Application (2021/22, 2022/23, 2023/24 and 2024/25) is about 1.24% per test year – which is consistent with the recommended indicative rate increase for rate smoothing purposes.

[1] 4.94% = 1.036 * 1.013

2.0 Introduction & Overview of MH's 2023/24 & 2024/25 General Rate Application

This Section of the Evidence provides a summary of MH's GRA proposals, a brief overview of the qualifications and duties to the PUB of Mr. Rainkie and outlines the purpose, scope and organization of the Evidence.

2.1 Summary of MH's 2023/24 & 2024/25 General Rate Application

The last comprehensive public review of MH's electricity rates by the PUB occurred in 2017 and 2018. It focused on the 2018/19 Test Year and confirmation of prior interim rate increases and resulted in Order 59/18. Since that time, MH rates have been reviewed on an expedited basis and without the benefit of a long-term financial forecast, prospective cost of service study, detailed O&A forecasts and comprehensive response to prior PUB directives. These reviews include the 2019/20 Rate Application that resulted in Order 69/19 and the 2021/22 Interim Rate Application that resulted in Order 9/22.

On November 15, 2022, MH filed a 2023/24 and 2024/25 GRA with PUB, requesting approval of the following:

1. Final approval of the 3.6% interim rate increase that was effective January 1, 2022 (2021/22 Test Year), flowing from Order 9/22;
2. Approval of further overall rates increases of 3.5% effective September 1, 2023 (2023/24 Test Year) and 3.5% effective April 1, 2024 (2024/25 Test Year);
3. Endorsement of changes to existing deferral accounts and establishment and amortization of new regulatory deferral accounts related to (i) Keeyask In-service (ii) SAP cloud computing arrangements (iii) Depreciation methodology for rate-setting purposes (iv) Major Capital Projects deferral account and (iv) write off the Demand Side Management (DSM) debit and credit deferral accounts; and
4. Final approval of interim Orders related to (i) Light Emitting Diode (LED) rates (ii) Surplus Energy Program (SEP) and Curtailable Rate Program (CRP) and (iii) endorsement of modifications to the SEP and CRP rate programs Terms and Conditions of Service.

On November 23, 2022, the Province of Manitoba announced that it would be reducing the provincial guarantee fee and water rental fees paid by MH by 50%, effective April 1, 2022.

On December 9, 2022, MH amended its GRA to reduce the further overall rate increases requested to 2.0% effective September 1, 2023 and 2.0% effective April 1, 2024, in recognition of the material impact that such fee reductions would have on MH's finances. The fee reductions increased MH's projections of its net income for 2023/23, 2023/24 and 2024/25, from the original values of $568 million, $298 million and $162 million, to the amended values of $751 million, $469 million and $295 million, respectively.

On December 21, 2022, MH also filed its Cost of Service and Rate Design proposals, requesting differentiated rate adjustments by customer class, as follows:

- Residential rate increases of 2.4% for both test years;
- General Service Small Demand, General Service Medium and General Service Large 750V-30kV increases of 2.1% for both test years;
- General Service Large 30kV-100kV and General Service Large >100kV increases of 1.5% for both test years; and
- General Service Small Non-Demand and Area and Roadway Lighting increases of 1.0% for both test years.

2.2 Overview of Mr. Rainkie's Qualifications & Duties to PUB

Through a joint regulation consulting practice, Mr. Rainkie and Ms. Derksen provide services to a wide range of clients that participate in and are impacted by rate-regulation and regulatory proceedings. In this proceeding, Mr. Rainkie is providing evidence on behalf of the Consumers Coalition (Consumers' Association of Canada (Manitoba Branch), Harvest Manitoba and the Aboriginal Council of Winnipeg).

Mr. Rainkie has 33 years of hands on and multi-faceted expertise in public utility leadership, rate-regulation and financial management, with demonstrated experience in applying and integrating this diverse experience into the rate-making framework of complex regulated enterprises. He specializes in providing public utility regulatory and financial advisory services to clients, with an emphasis on the evaluation of regulatory policy and strategy and revenue requirement and fiscal matters.

Mr. Rainkie has a deep specialization in all aspects of ratemaking, progressively throughout his career, including acting as an advisor to the PUB from 1990 to 1994, analyst and managerial roles in the Regulatory Services department of MH and Centra Gas between 1994 and 2006, senior and executive level responsibilities associated with regulatory affairs between 2006 and 2017 and an independent expert regulatory consultant between 2017 to present.

His experience relevant to the evidence to be provided in this proceeding includes executive level public utility experience as a former Corporate Treasurer, Corporate Controller, Vice-President of Finance & Regulatory Affairs and Chief Financial Officer and Acting President & Chief Executive Officer of MH between 2006 and 2017.

As Chief Financial Officer of MH, he was responsible for the executive leadership of the Controller, Treasury and Rates & Regulatory Affairs divisions, and Financial Planning and Corporate Risk Management departments. In these roles, Mr. Rainkie had responsibility for overseeing, setting and developing MH's:

1. Corporate and business unit strategies and financial plans,

2. Financial targets,
3. Long-term financial forecasts,
4. Operating and capital cost budgets,
5. Financing plans and debt management strategies,
6. Regulatory policies and rate applications,
7. Corporate risk management activities; and
8. Financial reporting.

Mr. Rainkie has testified before the PUB on multiple occasions over the last two decades, as an executive policy and subject matter witness for MH and Centra Gas and as an independent expert witness. Mr. Rainkie's full curriculum vitae is attached as **Appendix A** to this Evidence.

Mr. Rainkie acknowledges that in accordance with his retainer by the Consumers Coalition, that he has a duty to provide evidence that is fair, objective and non-partisan, related only to matters within his areas of expertise and to provide such additional assistance as the PUB may reasonably require to determine issues.

2.3 Purpose, Scope & Organization of the Evidence

The purpose of this Evidence is to evaluate MH's revenue requirement proposals and provide related observations, conclusions and recommendations to the PUB, for rate-setting purposes.

The scope of this Evidence focuses on the following topic areas:

1. MH's rate requests and approvals;
2. Enterprise planning, risk management and corporate strategic planning;
3. Financial targets;
4. O&A costs and cost control measures;
5. BOC capital plans;
6. Debt management strategy;
7. Regulatory deferral accounts, and
8. Long-term financial forecast scenario, including proposed and alternate rate paths.

Recognizing that the Consumers Coalition has assembled an interdisciplinary team of independent experts, Mr. Rainkie has prepared this Evidence cognizant of the parallel work of Midgard Consulting Ltd. and Morrison Park Advisors to ensure the contents of this report are not duplicative of other evidence filed by the Consumers Coalition. To the extent that the comments of Mr. Rainkie may address issues also raised by Midgard Consulting Ltd. and Morrison Park Advisors, particularly in the areas of capital asset management, sustaining capital, the corporation's financial health and debt management, these issues are canvassed for different purposes.

The Sections of the Evidence that follow, are organized as follows:

- Section 3.0 provides the evaluation of Strategy 2040 and related initiatives;
- Section 4.0 provides the evaluation of MH's risk assessment;
- Section 5.0 provides the evaluation of MH financial targets proposals;
- Section 6.0 provides the evaluation of MH's cost control related to O&A and BOC;
- Section 7.0 provides the evaluation of MH revised debt management strategy;
- Section 8.0 provides the evaluation of MH's regulatory deferral account proposals; and
- Section 9.0 provides the evaluation of MH's revenue requirement proposals and makes recommendations with respect to overall rate increases to balance customer interests and the financial health of MH.

Please note the following for the Sections of the Evidence that follow:

- All dollar figures are in $Millions, unless otherwise noted; and
- In the Figures, fiscal years are shortened to the end point – for instance, the 2023/24 fiscal year is denoted as 2024.

3.0 There are Too Many Concerns & Unknowns for the PUB to Fully Accept Strategy 2040 for Rate-Setting Purposes at This Time

Strategy is important for rate-setting as it drives strategic initiatives, corporate policy and attitudes towards risks and fiscal matters and ultimately spending priorities and plans of the utility. This Section of the Evidence contains the evaluation of MH's new strategy, Strategy 2040, for rate-setting purposes.

Based on the evidence on the record of this proceeding, Strategy 2040 is a multi-year journey (10+ years), consistent with a corporate restructuring - involving 21 Strategic Initiatives, a new IRP, realignment of the MH business model, evolution of the corporate culture and a revamp of numerous enterprise planning & risk management processes.

The conclusion from this Section of the Evidence is that there are too many concerns and unknowns for the PUB to fully accept strategy 2040 for rate-setting purposes at this time, based on the following evaluation:

1. The implementation of Strategy 2040 appears to be premature, in advance of foundational pre-cursors of the release of the Manitoba Energy Policy and completion of a new IRP;
2. Strategy 2040 appears to be unfocused, with 21 strategic initiatives and 47 separate deliverables in 2022/23 alone and may not yet provide sufficient strategic clarity that a corporate strategy should;
3. The magnitude of transformation inherent in Strategy 2040 is consistent with a corporate restructuring, which may be potentially unnecessary depending on the outcomes of the Manitoba Energy Policy and IRP;
4. There is a weak underpinning for MH's interpretation with respect to customer preferences involving trade-offs between reliability and lower rates and it is unclear how customer research and engagement has influenced underlying spending priorities in Strategy 2040;
5. Strategy 2040 is a multi-year journey and a work in progress by MH's own admission and may not be sufficiently advanced to be accepted by the PUB for rate-setting purposes; and
6. Strategy 2040 is contributing to upward pressure on rates and self-imposed risks on MH's future financial health and cash flows, as a result of $2.3 billion of increased spending in O&A and BOC, since the last GRA.

3.1 Strategy is Important for Rate-Setting as it Drives Strategic Initiatives, Corporate Policy and Ultimately Spending Priorities & Plans of the Utility

The impacts of corporate strategy are often under-analyzed for rate-setting purposes as strategy might be considered simply as background information for the general rate application.

However, strategy is an important consideration for rate-setting as it drives the corporate priorities and strategic initiatives of the organization. In turn, the corporate priorities and strategic initiatives shape policy and attitudes with respect to risk tolerances, required financial targets and ultimately drive the spending priorities and plans of the utility. This is especially the case when there are significant changes in the strategy of the public utility.

As public utilities are large, complex and publicly accountable organizations, it is common that their strategic plans are reviewed on an annual basis. The annual strategic planning process will vary by organization, but they typically involve a SWOT analysis (strengths, weakness, threats and opportunities), considerations of risk, setting of corporate objectives and related performance metrics and targets, as well as development of strategies and operational and financial plans to achieve the corporate objectives over the planning horizon.

Depending on the assessment of the policy and planning environment, the outcome of the strategic planning process may result in an update of the prior strategy to take into consideration new information. If the assessment is that there is major disruption in the industry, the outcome of the strategic planning process might result in a more transformational strategy that represents a reorganization of the organization.

Broadly, reorganizations can be classified into two main types[2], reconfigurations and restructurings, which can be distinguished by the pace and degree of change, considering the level of turbulence in the industry and the urgency of the need to transform:

1. Reconfiguration can be described as adding, splitting, transferring, combining business units without modifying the organizations underlying structure. In reconfiguration, quick and smaller scale changes are made to targeted business units but continuity in other areas of the organization are maintained; and
2. Restructuring can be described as changing the structural archetype around which resources and activities are grouped and coordinated. In restructuring, more fundamental changes are made across the organizations business units, which may take a number of years and include significant changes in management processes, information technology and corporate culture.

This is a useful framework to use to evaluate Strategy 2040 for rate-setting purposes.

[2] Harvard Business Review, Restructure or Reconfigure, March – April 2017

3.2 Strategy 2040 is a Multi-Year Journey Consistent with a Corporate Restructuring - Involving 21 Strategic Initiatives, Realignment of the Business Model, Evolution of the Corporate Culture and a Revamp of MH Planning & Risk Management Processes

MH indicates that the implementation of Strategy 2040 is a multi-year journey and that it is in the early stages of the implementation of the new strategy.

Since the last MH GRA (2018/19) and in response to its assessment with respect to evolving trends in the energy sector and changing customer expectations, MH has adopted a new mission statement: *Help all Manitobans efficiently navigate the evolving energy landscape, leveraging the clean energy advantage, while ensuring safe, clean, reliable energy at the lowest possible cost*.

In order to achieve the new mission statement, MH is undertaking a number of concurrent work streams:

1. **Strategy 2040**, a new long-term vision and plan for MH, with five **strategic pillars**: (1) Provide **safe**, **reliable energy** that responsively meets the evolving energy needs of Manitobans (2) Serve customers **efficiently**, responsively, and **digitally** (3) Help all Manitobans **understand** their **energy options** and make **informed choices** (4) Ensure Manitobans get **maximum value** from their clean, dependable energy **infrastructure**; and (5) Keep energy **prices** as **low** as **possible**, while providing the **level** of **service** Manitobans expect;
2. The development of the five strategic pillars into **16 strategic objectives**, involving **21 strategic initiatives**. For the **2022/23 fiscal year** Enterprise Plan, there are **47 separate deliverables** related to the 21 strategic initiatives;
3. A **10-year roadmap** of **Enterprise initiatives** through to the 2030/31 fiscal year, which represents the initiatives for the full implementation of Strategy 2040;
4. Development of an Enterprise Performance Management (**EPM**) framework and an Enterprise Scorecard, as well as an Enterprise Risk Management Program (**ERM**);
5. A new IRP to enable MH to understand, plan and respond to how the changing energy industry forces of decarbonization (reductions in fossil fuels and carbon-emitting energy resources), decentralization (shift from centralized power resources towards personal and individualized power infrastructure), digitalization (ever-advancing technology growth in both consumer goods and industrial mechanisms), customer energy choices and changing policy may impact the future energy needs of Manitoba;
6. A realignment of its **business model** (*the "hard wiring" of people, process and technology*) into eight business units (including President & CEO) to enable the execution of Strategy 2040, and evolve its approach towards customer centricity, asset management, work management, project delivery, transformation, digital, enterprise risk management and enterprise planning; and

7. Evolving its approach to **corporate culture** (*the" soft wiring" of ways of working, thinking and leading*) including a customer-centric culture and change management, continuous improvement and enterprise alignment capabilities.

MH indicates that the implementation of Strategy 2040 is a multi-year journey and that it is in the early stages of the implementation of the new strategy. In addition to foundational aspects like the IRP, the enterprise planning, EMP, ERM, Enterprise Planning Management Office (EPMO), IT strategic plan and business cases, investment framework and enterprise and business unit scorecards have all being confirmed by MH to be a work in process or in preliminary stages of development.

The sub-sections that follow, provide an evaluation of the concerns raised by Strategy 2040 for rate-setting purposes in the context of the 2023/24 and 2024/25 MH GRA.

3.3 The Implementation of Strategy 2040 in Advance of the Manitoba Energy Policy & Completion of a New IRP Appears to be Premature

The first concern with respect to Strategy 2040 for rate-setting purposes, is that the implementation of Strategy 2040 in advance of the release of a new Manitoba Energy policy and completion of the new IRP, appears to be premature.

MH confirmed in the response to information requests, that the Manitoba Government has not indicated when it plans to release potential energy policies or programs, beyond providing a milestone date of Spring of 2023[3].

While issues surrounding the new MH IRP was determined by the PUB to be beyond the scope of this proceeding, MH did confirm that the planned publication date of the new IRP is July of 2023[4].

MH downplays that it began to implement Strategy 2040 in advance of the release of the Manitoba Energy Policy and completion of its IRP, asserting that it is normal to update corporate strategy on an annual basis. Further, MH asserts that Strategy 2040 is adaptable to consider changes that result from these two foundational policy and analytical initiatives[5].

In terms of order of operations, it would have been preferable for MH to wait for the release and evaluation of the Manitoba Energy Policy before proceeding to commence the implementation of Strategy 2040 and the related objectives, initiatives and numerous deliverables. Strategy 2040 was not just an annual planning exercise, but has moved into the implementation of the strategy, including the realignment of the business model and several other implementation deliverables.

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[3] Coalition/MH I-2 a b
[4] Coalition/MH I-8 a
[5] Coalition/MH I-2 c d and Coalition/MH II-2 a b

In Section 2.1.3.1 of the Application, MH emphasizes the role and influence that Federal and Provincial policies are having in terms of shaping changes in the energy sector. The Manitoba Energy Policy will potentially set overall energy policy and objectives as it relates to decarbonization and decentralization, as well targets and timelines for emission reductions, decarbonization and electrification.

The Manitoba Energy Policy is somewhat akin to the strategic plan of a parent company, with MH being like a subsidiary of the Manitoba Government. MH is obviously a significant player as it relates to energy policy, but there are other agencies of the Manitoba Government, such as Efficiency Manitoba, that would have significant roles to play in implementing a Manitoba Energy Policy. MH moving into the implementation of Strategy 2040 ahead of the release and analysis of the Manitoba Energy Policy is like a subsidiary company beginning to implement its own strategy before the strategy, strategic initiatives and plans of the parent company are released and sufficiently understood.

In Section 2.8 of the Application, MH emphasizes the importance and role of the new IRP, positioning it as one of the key initiatives under Strategy 2040. MH indicates that the new IRP will provide a long-term roadmap for it to effectively plan and respond to the energy industry forces that are at the very centre of the new strategy.

Despite the importance of the IRP to framing the roadmap in terms of decarbonization and decentralization, MH began the implementation of Strategy 2040 before the new IRP was complete and its implications were assessed.

In addition, information technology is an enabler to the business and operational aspects of Strategy 2040. However, it appears that MH has decided to invest significantly in technology in advance of the confirmation of the business and operational changes that are necessary because of decarbonization and decentralization.

It is difficult to understand why MH chose to proceed with the implementation of Strategy 2040 in advance of the Manitoba Energy Policy and the new IRP. This results in a significant concern that Strategy 2040 is premature.

3.4 Strategy 2040 Appears to be Unfocused & May Not Provide Sufficient Strategic Clarity

The second concern with respect to Strategy 2040 for rate-setting purposes, is that Strategy 2040 appears to be unfocused and may not provide sufficient strategic clarity.

As was outlined in Section 3.2 of this Evidence, the implementation of Strategy 2040, involves 16 strategic objectives, 21 strategic initiatives and for the 2022/23 fiscal year, has 47 separate deliverables. There is also a 10-year roadmap of enterprise initiatives to fully implement Strategy 2040.

Presumably, as time goes on, the pace of implementation of Strategy 2040 will increase and the number of deliverables for each fiscal year will also increase over the 47 deliverables that were being worked on by MH in 2022/23. The sheer volume of work effort that is involved in the near-term deliverables and the associated costs are evident throughout the Application, year over variance analysis and information requests. The cost implications of Strategy 2040 are further discussed in Sub-section 3.8 and throughout Section 6.0 of this Evidence.

A good corporate strategy should provide strategic clarity, be coherent and well-articulated and delineate the key areas that the organization needs to do well on and should focus on – as well as those areas that it should not focus on or stop doing.

Stepping back and considering the entire record of the proceeding thus far, it is noted that (i) MH is two to three years into the implementation of Strategy 2040 (ii) the sheer volume of work effort on the strategic deliverables and (iii) the MH enterprise planning and performance management processes are positioned as multi-year journeys and still to be a work in progress for many years[6]. As such, there is significant concern that MH is in a state of analysis paralysis – with no clear strategic focus.

As part of the information request process, MH was asked to provide a SWOT analysis that was part of the formulation of Strategy 2040 and to indicate which of the SWOT areas that MH was focusing on. MH was unable to indicate its areas of focus, other than to refer to the 2022/23 Enterprise Plan for a list of initiatives and deliverables[7].

One can't help but wonder, that the apparent lack of strategic focus is in large part driven by the absence of a Manitoba Energy Policy and a completed IRP. These foundational frameworks are not yet in place, so MH is examining multiple dimensions of strengths, opportunities, weaknesses and threats, with little clarity on those areas with which to focus on.

3.5 The Magnitude of Transformation Inherent in Strategy 2040 May Be Potentially Unnecessary Depending on the Outcomes of the Manitoba Energy Policy and New IRP

The third concern with respect to Strategy 2040 for rate-setting purposes, is that magnitude of the transformation that is inherent in the strategy may be unnecessary depending on the outcome of the Manitoba Energy Policy and new IRP.

As was briefly described in Section 3.1 of this Evidence, the outcome of a strategic planning processes is a continuum ranging from strategy updates, to reorganizations through smaller and quicker reconfigurations, all the way to more fundamental transformation through restructuring.

Based on the concurrent work streams that were summarized in Section 3.2 of this Evidence and considering that Strategy 2040 involves realignment of the MH business model, enterprise

[6] MH Application Tab 2 and supporting Appendices
[7] Coalition/MH I-1 a and Coalition/MH II-1 a

planning and risk management processes and technology and changes to the corporate culture, it appears that Strategy 2040 is closer on the continuum to a restructuring, as opposed to a reconfiguration.

While there is much discussion on the record of the current proceeding with respect to changes in the energy industry, it is useful to remember that the energy industry has been under a constant state of evolution for decades.

MH has been successful in navigating these past energy industry evolutions and other significant business challenges. These include the purchase and integration of Centra Gas and Winnipeg Hydro and the planning and construction of major capital projects to strengthen the energy infrastructure, add generation capacity and exploit export opportunities. This has been accomplished primarily through updates to its strategy to recognize and deal with changing industry trends and reasonably focused reconfigurations of its business model.

With the Manitoba Energy Policy and new IRP as works in progress, there is an open question and concern for rate-setting purposes with respect to whether it was necessary to pursue a restructuring strategy (Strategy 2040) and the prudence of the associated costs. Alternatively, a reconfiguration strategy might have been a reasonable approach to deal with the evolving energy industry, as it has been for MH in the past.

3.6 There is a Weak Underpinning for MH's Interpretation with Respect to Customer Preferences Involving Tradeoffs Between Reliability and Lower Rates

The fourth concern with respect to Strategy 2040 for rate-setting purposes, is that there is a weak underpinning with respect to MH's interpretation with respect to customer preferences involving tradeoffs between reliability and lower rates.

It is unclear how customer research and engagement as to customer preferences has influenced Strategy 2040 and the underlying spending priorities and costs. There are some passages in the Application that allude to these considerations, such as Section 3.3 of the Application, where MH states that:

> "When establishing its projected rate path, Manitoba Hydro is guided by…priorities are informed by and reflect what Manitoba Hydro has heard directly from customers. Customer research and engagement indicates that although Manitobans continue to stress the importance of low Manitoba Hydro rates, when asked to weigh the importance of lower rates versus tradeoffs in reliability, customers have indicated that reliability of products and services is more important and must be balanced."

While MH conceded that it did not undertake any direct engagement with customers specific to the rate increases sought in the Application, it did provide a 2019 Customer Perceptions Study and a 2022 Reputation Study[8].

The key findings from the 2019 Customer Perceptions Study conducted by PRA Inc., can be summarized as follows[9]:

- When it comes to MH's priorities, Manitobans strongly favor keeping rates as low as possible over other aspects. Of concern is that MH received the lowest performance rating for keeping rates as low as possible;
- Secondly, Manitobans want reliable energy and the corporation to be environmentally responsible;
- Generally, Manitobans prefer MH to continue with current business practices. The only areas where respondents see some value in added costs is in order to reduce the frequency and length of power outages; and
- Overall, Manitobans have a preference for steady and predictable rate increases over keeping rates as low as possible for as long as possible (with larger rate increases).

As part of the information request process, MH also provided a recent Customer Satisfaction and Perceptions Tracking Study conducted by MH in September of 2022, with the key results summarized as follows[10]:

- Customer satisfaction with overall electric service was rated 8.14 out of 10;
- Customer satisfaction with reliability of electric service was rated 8.70 out of 10; and
- Customer satisfaction with price of electricity was rated 6.29 out of 10.

To support its spending priorities in terms of reliability and customer service, MH appears to emphasize the portion of the 2019 Perceptions Study that it uses to interpret that customers have indicated that reliability of products and services is more important than lower rates. The questions that customers were asked with respect to these tradeoffs and the responses, are as follows[11]:

- **Q48: In your view, how to you think MH should address the number of customer power outages?** The mean response to this question was 5.28 on a scale of 1 to 10 where 0 was keeping power rates lower and 10 reducing the number of power outages even if it means higher rates; and
- **Q49: In your view, how do you think MH should address the length of time customers are without power?** The mean response to this question was 5.55 on a scale of 1 to 10

[8] Application Tab 10, MFR 12
[9] Application Tab 10, MFR 12, Attachment #1, Page 40
[10] Coalition/MH I-126 b, Attachment 1, Pages 7 and 10
[11] Coalition/MH I-126 q, Pages 7 to 8

where 0 was keeping power rates lower and 10 reducing length of outages even if it means higher rates.

The concerns with respect to MH's interpretation of this customers survey is that they fail to consider the overall findings of the survey and they are based on leading questions. The perceptions and tracking surveys clearly demonstrate customers assess MH's overall service levels and reliability as high, with scores well in excess of 8 out of 10. In contrast, scores with respect to the price of electricity lags in the range of 6 out of 10.

The rates-reliability tradeoff questions appear to ignore these overall findings and specify that there is a problem in terms of number and duration of outages and then prompt respondents on what should be done about them. In this regard, the tradeoff questions appear to be leading, they don't provide the customer with an option that improved reliability is not needed and instead presuppose the need to address reliability. Even with the leading questions, the responses are balanced around the score of 5 and are not overwhelming supportive of additional spending to improve reliability. Caution should be exercised in the interpretation of such questions that there isn't a solution searching for a problem.

Therefore, there is a concern with respect to how much weight that MH should place in these survey findings.

More importantly, a few questions in a particular customer survey, would obviously not be sufficient business justification for the expenditures in the magnitude that would be necessary to significantly improve customer outages for MH.

3.7 Strategy 2040 is a Work in Progress by MH's Own Admission & May Not be Sufficiently Advanced to be Accepted by the PUB for Rate-Setting Purposes

The fifth concern with respect to Strategy 2040 for rate-setting purposes, is that Strategy 2040 is a work in process by MH's own admission and may not be sufficiently advanced to be accepted by the PUB for determining rates and a longer-term rate path.

As was summarized in Section 3.2 of this Evidence, Strategy 2040 is a multi-year journey Involving 21 strategic Initiatives, realignment of the business model, evolution of the corporate culture and a revamp of MH planning & risk management processes – all of which is a work in progress.

As a result of this early stage of development, with many budget place-holders for significant initiatives and associated O&A and capital costs, it is difficult to see how these costs meet regulatory tests of prudency and be accepted by the PUB as part of a long-term rate path for rate-setting purposes.

3.8 Strategy 2040 is Contributing to Upward Pressure on Rates & Self-Imposed Risks on MH's Future Financial Health and Cash Flows as a Result of $2.3 Billion of Increased Spending

The sixth concern with respect to Strategy 2040 for rate-setting purposes, is that Strategy 2040 is contributing to upward pressures in rates as a result of increased levels of spending and resulting in self-imposed risks in terms of MH's future financial outlook and cash flows.

While the financial and cost forecasts of MH that underpin the Application will be examined in more detail in the major sections of the Evidence that follow, the cost implications of Strategy 2040, the changes in policy and attitudes towards risks and ability to control costs – can be demonstrated at a high-level by considering the changes in O&A and BOC since the last MH GRA in 2018/19.

A comparison of the changes in O&A[12] and BOC[13] forecasts between the Integrated Financial Forecast (IFF) that was accepted by the PUB in the 2018/19 MH GRA (MH Exhibit #93, which is referred to as forecast MH16 for shorthand in this Evidence) and the Amended Financial Forecast from the current Application (referred to as MH22 for shorthand in this Evidence), is provided in Figure 1 below:

Figure 1: Operating & Adminstrative Expenses & Business Operations Capital - MH22 vs MH16

1	2	3	4	5	6	7	8	9
			(2 + 3)			(5 + 6)	(4 - 7)	
	O&A	**BOC**	**Total**	**O&A**	**BOC**	**Total**	**Total**	**Cumulative**
Year	**MH22**	**MH22**	**MH22**	**MH16**	**MH16**	**MH16**	**Inc (Dec)**	**Inc (Dec)**
2023	589	495	**1084**	536	549	**1085**	-1	**-1**
2024	657	538	**1195**	548	561	**1109**	86	**85**
2025	687	559	**1246**	559	618	**1177**	69	**154**
2026	683	617	**1300**	571	643	**1214**	86	**240**
2027	697	647	**1344**	583	663	**1246**	98	**338**
2028	711	722	**1433**	595	671	**1266**	167	**505**
2029	724	750	**1474**	607	697	**1304**	170	**675**
2030	736	788	**1524**	620	688	**1308**	216	**891**
2031	739	827	**1566**	633	727	**1360**	206	**1097**
2032	754	866	**1620**	646	734	**1380**	240	**1337**
2033	769	905	**1674**	660	748	**1408**	266	**1603**
2034	785	919	**1704**	674	760	**1434**	270	**1873**
2035	800	933	**1733**	688	835	**1523**	210	**2083**
2036	816	948	**1764**	702	852	**1554**	210	**2293**

[12] Coalition/MH I-67 j

[13] Coalition/MH II-32

As can be seen in Figure 1, MH22 forecasts a total cumulative increase in O&A and BOC spending relative to the 14-year comparable period in MH16 (from the 2018/19 GRA), as follows:

- Increases of $85 million and $154 million for the 2023/24 and 2024/25 Test Years, respectively;
- Increases of approximately $1.3 billion for the first 10-years to 2031/32; and
- Increases of approximately $2.3 billion for the 14-year period to 2035/36, for which a comparison is available.

While MH was not able to quantify the full cost implications of Strategy 2040, indicating that they are integrated into the cost forecasts in MH22, the explanations in the Application, Minimum Filing Requirements, O&A variance analysis and Capital Plan (Appendix 7.7), for the most part refer to the business model transformation, corporate restructuring and spending priorities that are inherently a part of Strategy 2040 and associated initiatives.

Another concerning aspect is that the spending priorities associated with Strategy 2040 appear to be predominately incremental to the levels of spending that were previously forecast by MH at past rate proceedings (incremental to base business). There is very little in the way of identified offsets through prioritizing decreases in other areas of the business that are not as strategically important or attempt to quantify and forecast any benefits that may arise from these strategic expenditures. Here again caution has to be exercised, as the spending associated with strategic imperatives can lead to a situation where they are deemed as justifiable at any cost and not requiring strong business cases.

In addition to O&A and BOC costs, significant amounts have been expended for corporate initiatives and restructuring and are included in forecasts of Other Expenses. On a consolidated basis the corporate initiatives and restructuring costs from 2019/20 to 2024/25 are forecast at $55 million, with $51 million being allocated to electric operations, with another $8 million being projected to 2029/30, for a total allocation to electric operations of $59 million[14].

It is obvious that the strategic initiatives and spending priorities that flow from Strategy 2040 are contributing to upward pressure on rates and contributing to the MH proposed 2% rate path for the next 20-years.

While MH is concerned with respect to its future financial health, its levels of debt and levels of cash flow – the increased spending forecasts in the order of $2.3 billion may be seen as constituting self-imposed risks by MH.

[14] Coalition MH/I-4 h and 4 i

3.9 There are Too Many Concerns & Unknowns for the PUB to Fully Accept Strategy 2040 for Rate-Setting Purposes at This Time

The conclusion of the evaluation of Strategy 2040 for the purposes of this proceeding, is that there are too many concerns and unknowns for the PUB to fully accept Strategy 2040 for rate-setting purposes. Strategy 2040 is a work in progress by MH's own admission and may not be sufficiently advanced to be accepted by the PUB for rate-setting purposes.

Strategy 2040 entails a corporate restructuring of MH, which has been advanced with implementation of the strategy occurring before two foundational pre-cursors in the form the Manitoba Energy Policy and the new MH IRP, and as such appears to be premature. The magnitude of the transformation envisioned in Strategy 2040 may be potentially unnecessary depending on the outcomes of these foundational pre-cursors and as such the strategy appears to be unfocused and not providing sufficient strategic clarity.

There is a weak underpinning with respect to MH's interpretation of customer preferences involving tradeoffs between reliability and lower rates. Strategy 2040 is contributing to upward pressure on rates and self-imposed risks on MH's future financial health and cash flows, as a result of $2.3 billion of increased spending, since the PUB's last comprehensive review of electricity rates at the 2018/19 GRA.

As was outlined by MH in the information request process "Consistent with the current regulatory process, the PUB has the authority to include or exclude costs, revenues, losses or gains in its rate determination"[15]. It is recommended that the PUB weigh the concerns and unknowns and the fact that Strategy 2040 is a work in progress, in making its rate determinations in this regulatory proceeding – and find that it is premature to fully accept Strategy 2040 for rate setting purposes.

[15] Coalition/MH II-20 b

4.0 A Relative Assessment of Risks Since the Last GRA Does Not Support the MH Assessment of Elevated Business & Financial Risks for Rate-Setting Purposes

Risks are assessed in the MH rate-setting process, in order to make judgements on the pace of attainment of financial targets and the level of contributions to financial reserves that will be allowed in rates by the PUB, through net income. This Section of the Evidence contains the evaluation of MH's risk assessment, for rate-setting purposes.

In the current Application, MH provides a high-level risk assessment that its risks are increasing both in amount and the level of risk that it is exposed to, thus supporting its proposed 2% rate path as a means to mitigate these risks.

The conclusion from this Section of the Evidence is that, a relative assessment of risks since the last GRA does not support the MH assessment of elevated business and financial risks for rate-setting purposes, based on the following evaluation:

1. The MH enterprise risk management program is in the early stages of development and its high-level risk assessment is incomplete and not balanced, with many speculative elements;
2. A more objective, balanced and complete assessment of MH's business and financial risks for rate-setting purposes, relative to the last GRA, including the reduced in risk associated with the in-service of the major capital projects, the substantial improvement in MH's financial outlook, MH's own risk quantifications and the value of a hydro-electric system under climate change policy – does not support MH's assessment that its risks are elevated;
3. There are a number of inconsistencies between MH's high-level risk assessment, and its policies, spending priorities (cost increases of $2.3 billion) and enterprise planning priorities (multi-year journeys for ERM Program and asset management initiatives and incomplete IT strategic planning and business case evaluations);
4. MH's decision not to keep its Uncertainty Analysis current, is a step backwards for both its ERM Program and analysis of risks for rate-setting; and
5. The high-level MH risk assessment is not consistent with the PUB rate-setting policy direction from Order 59/18, that rates should not be set to increase financial reserves for all identifiable risks and that the PUB is prepared to consider regulatory action, when and if emerging risks actually materialize.

4.1 Risks Are Assessed in the MH Rate-Setting Process in Order to Make Judgements on Pace of Attainment of Financial Targets and Contributions to Financial Reserves Through Net Income

Risks are assessed in the rate-setting process in order to made judgements and determinations with respect to capital structure (the appropriate mix of debt and equity financing), financial

targets (appropriate levels of interest coverage and other key financial ratios) and the amount of net income to allow in rates up and above the costs of providing utility services that are determined to be prudent for rate-setting purposes. Like many aspects of rate-regulation, the assessment of risks is updated at each rate proceeding and the current assessment builds upon the prior assessments.

In the formulaic Rate Base/Rate of Return (RBROR) rate-setting methodology that is often applied to investor-owned utilities (IOU), the public utilities commission approves an allowed capital structure, rate base (the amount of investment on which the utility is allowed to earn a return) and Return on Equity (ROE) (the percentage that the utility is allowed to earn on the portion of rate base that is financed by equity). Under RBROR, rates are set in a particular test year based on the total revenue requirement for that test year, which includes the costs of providing service (O&A, depreciation, finance expense, taxes etc.) as well as a return on debt (to cover finance costs) and return on equity (essentially the net income that the utility is allowed to include in rates).

The determination of an allowed capital structure and ROE under RBROR is a very complex and time-consuming portion of a rate case. Determinations on cost of capital issues entail considerable professional judgement and often involving a number of ROE experts that conduct comprehensive assessments of business and financial risks to make recommendations on the appropriate capital structure and various ROE estimation methodologies to make recommendations on the appropriate level of ROE.

In contrast, MH has been regulated for decades under what can be referred to as a Modified Cost of Service (MCOS) rate-setting methodology. This methodology has worked well for MH, given its status as a Government Business Enterprise (GBE) and the fact that MH has not traditionally had a policy of earning a return for shareholders, but rather maintain sufficient financial reserves to cover risks.

The MCOS is essentially a judgemental rate-setting methodology, with a focus on rate-smoothing, where rates in the current test year(s) are set by making judgements with respect to the pace of attainment of financial targets (in MH's case, debt to equity ratio, interest coverage ratio and capital coverage ratio) over the financial planning horizon. The attainment of financial targets over time most often results in rates that not only recover the costs of providing service, but also an annual contribution to financial reserves, through the resulting net income.

Under MCOS rate-setting, risk assessments are used to make judgements with respect to the appropriate financial targets and the pace of attainment of these financial targets. Risk assessments also provide valuable insights into the utility's risk tolerance for setting financial policies and strategies (such as financial targets and debt management strategies) and attitudes towards cost control.

4.2 The MH High-Level Risk Assessment is that Its Risks are Increasing Both in Amount and the Level of Risks that it is Exposed To

In the current proceeding, MH's assessment is that its risks are increasing, emphasizing (i) changes in the energy sector are driving greater uncertainty in forecasting both energy demand, as well as energy supply planning, and increasing both the amount and level of risks that it is exposed to and (ii) the current rising interest rate environment presents a significant risk of increased finance costs given its highly debt levered position due to investments made in major capital projects over the past decade and an average of $1.1 billion of annual debt maturities over the next 10-years potentially requiring refinancing at higher interest rates.

In the Application, MH provided the following summary of its Top Enterprise Risks, and in the information request process asserted that all of these risks were increasing and that some of the risks were new risks compared to prior risk assessments provided to the PUB [16]:

1. Drought (low water levels);
2. Interest Rates;
3. Ageing Assets;
4. Cyber Security (IT/OT Assets);
5. Export Price Uncertainty;
6. Disruptive Technology;
7. Self Generation & Stranded Assets;
8. Technology Innovation;
9. Succession Planning; and
10. Talent Acquisition & Retention.

The implications of MH's risk assessment for rate-setting purposes appears to be that it should improve its financial health and reduce levels of net debt, through its proposed 2% rate path.

4.3 The MH Enterprise Risk Management Program is In the Early Stages of Development and Its High-Level Risk Assessment Is Incomplete and Not Balanced

The MH ERM Program is in the early stages of development and the high-level risk assessment provided by MH in the Application is incomplete and not balanced.

MH indicates that it is in the process of a multi-year journey to establish a more formal and comprehensive ERM Program to ensure that its risks are clearly understood, actively monitored and mitigation plans are in place to support the successful execution of Strategy 2040.

[16] Coalition/MH I-1 b and 7 h

Given that the ERM is under development, MH was unable to provide a comprehensive corporate risk management report[17], consistent with the reports that had been filed with the PUB in the past as part of GRA proceedings. As was noted in Section 4.2 of this Evidence, MH was only able to provide a high-level summary of Top Enterprise risks with a sentence or two of commentary, in the current proceeding.

The last comprehensive corporate risk management report developed by MH, was completed in the fall of 2018 and was filed with the PUB as part of the Centra Gas 2019/20 GRA[18]. This report was 52 pages in length, including a risk overview of trends and changes, discussions of risk groups, highest priority risks, other risk areas of concern and high consequence risks, and provided corporate risk profile summaries of 55 corporate risks. The corporate risk profiles included ratings on probability, consequence, tolerance, current status, actions required and a risk heat map. Some of the key risks from this report can be summarized as follows:

- **Highest priority risks**: Interest Rates, Electricity Rates, Completion of Major Capital Projects, Corporate Reputation, Meeting Financial Targets and Concerned Stakeholders;
- **Other Areas of Concern**: Demand Side Management Assumptions, Load Growth Uncertainty, Export Price Uncertainty, Regulatory Environment, Protectionism, Taxation, Transmission System Delays, Electric Distribution System Asset Risk, Union/Employee Issues, Indigenous Relationships & Legal, Cyber Security, Emerging Energy Technologies, Re-licensing of Legacy Facilities and Safety & Health; and
- **High Consequence Risks:** Energy/Fuel Price Volatility, Export Market Access, Infrastructure Risk, Extreme Drought – Shortfall of Energy Supply and Environmental Legislation (Fisheries).

As can be seen from the summary listing of the 2018 Corporate Risk Management Report (which is consistent with the risk assessment information provided at prior GRA's), it is fair to conclude that the information in the current rate proceeding is incomplete and certainly not of the calibre that would be considered appropriate for risk assessments for rate-setting purposes. Moreover, MH's assertions with respect to increases in the number and level of risks, a compared to previous Corporate Risk Management Reports is unfounded.

In addition to the lack of completeness of the risk assessment information for rate-setting purposes, another concern is the lack of balance that is provided in MH's high-level assessment of its Top Enterprise Risks. Risk assessments should be balanced between risks and opportunities, such that a current overall assessment of risk can be made and compared to the overall assessments of risk from prior regulatory proceedings.

There is some other information on the record, which by no means is comprehensive, that can provide a limited degree of a balanced risk assessment for the PUB. In the 2022/23 Enterprise

[17] Application Tab 10, MFR 3

[18] Coalition/MH I-7 a

Plan, MH outlined the implications of decarbonization, decentralization and digitalization (3 D's), in terms of opportunities and challenges:

- **Decarbonization**: Opportunities (strengthen trusted relationship with government, expected increase in electric load through electrification and demand for renewable energy puts MH in an advantageous position); Challenges (energy policy will significantly impact MH, need for sufficient charging infrastructure and need for increased generation capacity);
- **Decentralization**: Opportunities (trusted energy advisors to Manitobans, federal funding to improve capital structure and opportunity to implement innovative solutions); Challenges (stranded assets and decreased revenues from self-generation, higher costs from bi-directional energy flow and peaks in demand in the winter and battery technology development could lead to grid defection); and
- **Digitization**: Opportunities (automation/bundling of services behind the meter, enhance the way MH engages with customers and digital grid operations offsetting capital requirements); Challenges (shifting load resulting in increased investment in distribution grid and need to expand MH digital offerings).

MH also acknowledged that its **hydro-electric system** will become even **more valuable** as the world responds to **climate change**. MH's system a will not be exposed to carbon pricing or future GHG management policies and as a dispatchable resource, has additional value compared to renewables that tend to be intermittent and non-dispatchable. However, MH indicated that it has no ability to assess that portion of its business risks related to the evolving industry trends, that were offset by the opportunities presented by its hydro-electric system[19].

MH also acknowledged that the risk that was previously described as the loss of market access to export power markets has improved as a result of a push to more variable renewable resources which has increased both the need and industry wide support to maximize interconnections and market access[20].

4.4 A Relative Assessment of Risks as Compared to the 2018/19 GRA Does Not Support MH's Assessment that Its Risks are Elevated for Rate-Setting Purposes.

A relative assessment of risks compared to the 2018/19 GRA, does not support MH's assessment that its risks are elevated, for rate-setting purposes.

Typically, assessments of utilities risks for rate-setting purposes, consider the combined business and financial risks, compared to the assessments that were made at prior rate proceedings. As previously mentioned, these assessments are cumulative over time, and build on each other. As

[19] Coalition/MH I-1 c and Coalition/MH II-1 c
[20] AMC/MH I-1

such, a useful approach in this proceeding is to consider the relative business and financial risks of MH as compared to the last comprehensive GRA from 2018/19. It is also useful to review the quantitative risk information on the record to understand how the magnitude of the risks have changed since the last comprehensive assessment of MH's rates.

In the 2018 Corporate Risk Management Report, MH assessed **Completion of Major Capital Projects** as one of its highest priority risks, noting that "further slippage on construction costs and schedule, risk the financial standing of the Corporation in addition to risking the impact to indigenous and customer relationships, reputation and standing with certain stakeholders" and "any significant delays or cancellation would have material financial, reputational and contractual consequences". In that report, MH rated Inadequate Contingency (Risk C1) as a high probability and high consequence risk and Delay to In-Service (Risk C2) as a medium probability and medium consequence risk.

Despite the obvious and material reduction in MH's financial and business (reputational and contractual) risks as a result of the achievement of completion and in-service of the major capital projects, the consideration of this risk category is nowhere to be found in MH's high-level risk assessment. One of the key deficiencies of MH's high-level risk assessment, is that it looks forward, concentrating on the 3 D's that are the cornerstone of Strategy 2040, but neglects to consider the overall risk environment (completion of major capital projects) and relative risk as compared to prior MH GRA's, for rate-setting purposes.

With respect to **Drought Risk** (one of MH's top risks on a consistent basis), the impact of a 5-year drought on retained earnings is currently forecast at a reduction of $1.7 billion in the current GRA, which compares to $1.4 billion from the 2018/19 GRA and $1.7 billion from the 2015/16 GRA[21]. MH's quantification of drought risk appears to be reasonably consistent with the past two GRA's.

MH's concern over elevated **Interest Rate Risks** as a result of the debt associated with the major capital projects and upcoming debt maturities is pervasive throughout its Application, risk analysis and reasons for the proposed 2% rate path. However, information uncovered during the information request process and MH's own interest rate policy guidelines and quantification of forward interest rate risk, places these assessments in doubt. MH concedes in the information request process that[22]:

> "Manitoba Hydro views debt maturities per year of approximately 5% of the total debt portfolio…to be a reasonable level of risk and significantly lower that the upper limited in Manitoba Hydro's current interest rate risk guidelines…Manitoba Hydro's average interest rate risk each year remains at the lower end of its interest rate guidelines…With

[21] MH/Coalition II-19

[22] Coalition/MH I-45 a b

a borrowing program of approximately $10 billion in the next decade…Manitoba Hydro does not anticipate high levels of concentration risk as a result of financing activities."

MH also provides an updated high interest rate sensitivity (+1% increase in interest rates from MH22), which shows a reduction in retained earnings of $462 million. This compares favorably to the high interest rate sensitivities provided at the 2018/19 GRA and 2015/16 GRA, which shows reductions in retained earnings of $747 million and $1.057 billion, respectively[23].

To put this in context, the **high interest rate sensitivity** for the current Application **represents** a **38% reduction** ($462 / $747) from the **2018/19 GRA** and a **56% reduction** ($462 / $1.057) from the **2015/16 GRA**. This quantitative assessment makes sense, as one would expect that as the debt to finance the major capital projects (with interest rates locked in for decades), is progressively issued, then there would be a reduction in MH's forward interest rate risk quantification.

As noted in the above passage, MH confirmed that the debt financings of $1.1 billion, which in terms of magnitude sound daunting, are in fact a reasonable level of risk when you consider the fact that they represent 5% of a debt portfolio with a 19.5 year weighted average term to maturity. The conclusion from MH's own admissions, policies and quantifications, is that its assertion that its forward-looking interest rate risk is elevated, is an overstatement.

The other critical aspect that is absent from MH's high-level risk assessment, is the **substantial improvement** in its **financial outlook**, since the 2018/19 GRA. It has been standard practice in past MH GRA's to provide the PUB with an extensive comparison between the new long-term financial forecast and the financial forecast from the last GRA. Rate proceeding are cumulative over time, with the current GRA, building on the assessments of past GRA's. Despite this standard practice, MH did not provide this comparison in its Application, apparently due to the passage of time and concerns over relevance[24].

The following figures, which compare the current MH financial forecast (MH22) with the forecast available at the last GRA (MH16) in terms of the key financial metrics (net income and net debt) and financial ratios (equity ratio and interest coverage ratio) that have been used by the PUB to set rates at past rate proceedings, demonstrate this fact:

[23] MH/Coalition I-36 f

[24] Coalition/MH I-27 a

Figure 2: Net Income & Net Debt - MH22 vs MH16 - $Millions

1	2	3	4	5	6	7	8
			(2 - 3)				(6 - 7)
Year	Net Income MH22	Net Income MH16	Net Income Inc (Dec)	Net Income Cumulative Inc (Dec)	Net Debt MH22	Net Debt MH16	Net Debt Inc (Dec)
2023	751	**-29**	780	**780**	22963	24666	**-1703**
2024	469	**-111**	580	**1360**	22529	24702	**-2173**
2025	295	**-69**	364	**1724**	22341	24765	**-2424**
2026	149	**-128**	277	**2001**	22371	24891	**-2520**
2027	166	**-68**	234	**2235**	22322	24963	**-2641**
2028	97	**-13**	110	**2345**	22356	24971	**-2615**
2029	92	81	11	**2356**	22401	24899	**-2498**
2030	111	190	-79	**2277**	22451	24713	**-2262**
2031	105	261	-156	**2121**	22471	24476	**-2005**
2032	169	398	-229	**1892**	22424	24091	**-1667**
2033	190	512	-322	**1570**	22372	23592	**-1220**
2034	219	641	-422	**1148**	22270	22950	**-680**
2035	277	793	-516	**632**	22090	22221	**-131**
2036	250	883	-633	**-1**	22030	21403	**627**

Figure 3: Equity Ratio & EBITDA Interest Coverage Ratio - MH22 vs MH16

1	2	3	4	5	6	7
			(2 - 3)			(5 - 6)
Year	Equity Ratio MH22	Equity Ratio MH16	Equity Ratio Inc (Dec)	Interest Coverage Ratio MH22	Interest Coverage Ratio MH16	Interest Coverage Ratio Inc (Dec)
2023	15%	13%	**2%**	2.48	1.58	**0.90**
2024	17%	13%	**4%**	2.21	1.52	**0.69**
2025	18%	12%	**6%**	2.06	1.57	**0.49**
2026	18%	12%	**6%**	1.92	1.53	**0.39**
2027	19%	12%	**7%**	1.95	1.58	**0.37**
2028	19%	12%	**7%**	1.89	1.63	**0.26**
2029	20%	12%	**8%**	1.90	1.72	**0.18**
2030	20%	13%	**7%**	1.95	1.82	**0.13**
2031	21%	14%	**7%**	1.99	1.87	**0.12**
2032	21%	15%	**6%**	2.12	2.01	**0.11**
2033	22%	17%	**5%**	2.17	2.11	**0.06**
2034	23%	19%	**4%**	2.24	2.25	**-0.01**
2035	24%	22%	**2%**	2.33	2.42	**-0.09**
2036	25%	25%	**0%**	2.36	2.56	**-0.20**

The observations with respect to Figures 2 and 3, are as follows:

1. In contrast to MH16 which forecast losses of $418 million in the six-year period between 2022/23 and 2027/28, MH is now forecasting positive contributions to financial reserves (net income) of $1.9 billion in that same period, for a cumulative improvement of $2.3 billion;
2. Net debt is now forecast to be $2.4 billion lower by the end of the of the second Test Year (2024/25), as compared to the prior GRA. This significant improvement holds until the last years of the 14-year period and until the excessive levels of net income in MH16 are projected as a result of the cumulative impact of 3.57% annual rate increases over this period;
3. The Equity ratio is now forecast to recover to 18% by the end of the second Test Year, a remarkable improvement of 6% as compared to the 12% forecast at the last GRA. This is significant in that the Equity ratio is quite "sticky", it requires a significant financial improvement to improve the ratio 1%, let alone 6%; and
4. The EBITBA Interest Coverage Ratio is forecast to be in excess of 2.00 for the Test Years and remain above the former MH target of 1.80 for the next 11-years, as compared to MH16 which projected lower than target interest coverage until 2029/30.

The following figure compares the current MH financial forecast (MH22) with the forecast available at the last GRA (MH16) with respect to the forecast of Export Revenues. Figure 4 demonstrates that there is a significant improvement in forecast Export Revenues since the last MH GRA, with cumulative increases of approximately $1.0 billion by the end of the 2024/25 Test Year and $1.9 billion over the 14-year period of comparability between the two forecasts.

Figure 4: Export Revenues - MH22 vs MH16 - $Millions				
1	2	3	4	5
			(2 - 3)	
Year	MH22	MH16	Export Revenue Inc (Dec)	Export Revenue Cumulative Inc (Dec)
2023	1283	779	504	**504**
2024	1153	788	365	**869**
2025	964	805	159	**1028**
2026	780	667	113	**1141**
2027	778	671	107	**1248**
2028	754	662	92	**1340**
2029	740	677	63	**1403**
2030	748	697	51	**1454**
2031	768	709	59	**1513**
2032	766	705	61	**1574**
2033	754	701	53	**1627**
2034	762	696	66	**1693**
2035	783	694	89	**1782**
2036	707	602	105	**1887**

The above noted financial metrics and ratios are demonstrative of a significantly improved financial outlook and lower levels of financial risk, relative to the last MH GRA. This is the case, despite MH's plans to increase total O&A and BOC spending by $2.3 billion in the next 14 years.

It has already been observed in Section 4.3 of this Evidence that the **substantial value** of the MH **hydro-electric system** could be a **significant offset** to the risks presented by energy industry trends of **decarbonization, decentralization and digitalization**. MH itself, has identified both opportunities and challenges associated with these energy industry trends in its 2022/23 Enterprise Plan. Additional considerations that are on the record in this regard are:

- The MH22 forecast includes increases in future demand and incorporates some of the aspects of increased electrification of transportation and behind the meter solar generation[25]; and
- The current high electricity load forecast scenario (P90) results in an increase in retained earnings of $180 million by 2031/32 (10 years) and $312 million by 2041/42 (20 years). Which compares to the 10-year high electricity forecast scenarios retained earnings

[25] MH/Coalition I-14 b

increases of $484 million and $65 million, at the 2018/19 and 2015/16 GRA, respectively[26]. The 20-year comparisons to past GRA's are not on the record.

In summary, a more objective, balanced and complete assessment of MH's business and financial risks for rate-setting purposes, relative to the last GRA, including consideration of the achievement of in-service of the major capital projects, the substantial improvement in MH's financial outlook MH's own evidence, interest rate risk guidelines and risk quantifications and the value of a hydro-electric system under climate change policy - does not support MH's assessment that its risks are elevated.

4.5 There are a Number of Inconsistencies Between MH's High-Level Risk Assessment and Its Policy, Spending Priorities and Enterprise Planning Priorities

There are number of inconsistencies that can be observed between MH's high-level risk assessment that its risks are increasing and its spending priorities and enterprise planning priorities, including the following:

1. If MH is concerned about its financial outlook, interest rate risk and levels of cash flow, then why has it changed its past policy in terms of cost control and increased its O&A and BOC spending plans by $2.3 billion in the next 14 years. The MH concerns would be expected to result in a policy of tight fiscal constraint, but the evidence on the record is quite the opposite. This situation is assessed as a self-imposed risk by MH;
2. If MH is concerned about elevated levels of risk, then why didn't it make a decision to expedite the implementation of its ERM Program and enhance its risk management analysis with more advanced assessment of risk interconnectivity and risk clock-speed, instead of launching a multi-year journey;
3. If MH is concerned about elevated levels of risk, then why didn't it make a decision to keep the more advanced Uncertainty Analysis that was prepared and presented at prior PUB hearings current, and instead only present one-off risk sensitivities in the current Application (discussed further in Section 4.6 below);
4. If MH is concerned about Ageing Asset risk, then why didn't it decide to expedite the implementation of its asset management framework and associated process improvements, instead of a continuing multi-year journey; and
5. If MH is concerned about Technology Risk, then why doesn't it have a MHEB approved IT Strategy, and why is it seemingly in the initial stages of pre-planning for cloud computing arrangements, without associated business cases.

[26] MH Coalition I- 36 a and d

In summary, it is difficult to reconcile the MH high-level risk assessment with its policies, spending priorities and enterprise planning priorities.

4.6 MH's Decision to Not Keep Its Uncertainty Analysis Current Represents a Step Backwards in Terms of Its ERM Program and Analysis of Risks for Rate-Setting Purposes

It is observed that MH's decision not to keep its Uncertainty Analysis (that was filed with the PUB at the 2014 NFAT proceeding, the 2016/17 Interim Rate Application and 2018/19 GRA) current, represents a significant step backwards in terms of its ERM Program and analysis of risks for rate-setting purposes.

On a high level, MH's Uncertainty Analysis provided over 15,000 discrete financial projections which were based on varying key financial forecast assumptions with respect to water flows, interest rates and export prices, allowing for comparison of corporate financial metrics such as equity ratio, net income and retained earnings across these 15,000 financial projections.

The Uncertainty Analysis is significantly more robust than the one-off risk sensitivities (analysis of changes to one-variable at a time) presented by MH in the current Application, in that it can be used to generate a broad range of possible financial outcomes for a number of combined sensitivities.

More advanced forms of risk management programs are able to analyze the interconnectivity and potential for compounding effects or offsetting effects, of various risks. The MH Uncertainty Analysis is a much more powerful risk management tool than one-off risk sensitivities which can aid in the development of a more advanced risk management program.

MH indicated that the Uncertainty Analysis was not maintained for three reasons (i) priorities redirected towards Strategy 2040 (ii) the development of a new ERM and (iii) the development of a new IRP[27].

Interestingly, MH also indicates that the Uncertainty Analysis will not be updated until after the new IRP has been completed, as MH's understanding of uncertainties of energy industry forces will be influenced to a large degree by the outcome of the new IRP[28]. This admission by MH, further reinforces the concerns with respect to implementing Strategy 2040 in advance of the completion of the IRP (Section 3.3 of this Evidence) and the assessment that MH's high-level risk assessment is incomplete and not balanced (Section 4.3 of this Evidence).

As such, the assessment for this topic area, is that the decision not to update the Uncertainty Analysis for the current Application, represents a step backwards, both for the MH ERM Program

[27] PUB/MH I-21 a b

[28] Coalition/MH II-7c

and for rate-setting purposes. The use of the Uncertainty Analysis as a means of developing rules-based regulation to set rates, is further discussed in Section 5.6 of this Evidence.

4.7 The PUB Policy Established in Order 59/18 is that Rates Should Not be Set to Increase Financial Reserves for all Identifiable Risks & that the PUB is Prepared to Consider Regulatory Action When and If Emerging Risks Actually Materialize

The PUB policy from Order 59/18 is that rates should not be set to increase financial reserves (retained earnings) for all identifiable risks and that the PUB is prepared to consider regulatory action (rate increases) when, and if, emerging risks actually materialize.

The 2018/19 MH GRA was a very comprehensive regulatory proceeding as a result of a significant shift in the Corporations financial policy and plan, that resulted in a proposed 7.9% rate path. There was considerable evidence presented with respect to MH's risks and how these risks should be factored into rate-setting on a go-forward basis.

In its decision (Order 59/18), the PUB rejected the 7.9% rate path and associated financial plan, but set out foundational policy, guidance and findings on how the key risks of MH should be considered and dealt with for rate-setting purposes. The key aspects of this rate-setting policy guidance, can be summarized as follows[29]:

1. The PUB is prepared to take regulatory action (rate increase) as required when emergent situations face MH;
2. Retained earnings should be used to manage drought risk in combination with regulatory action by the PUB;
3. Interest rate and export price risks over the long term should be addressed with rate increases as and when those risks materialize; and
4. Rates should not be set to increase retained earnings to manage these longer-term risks.

The important considerations in this rate-setting policy guidance, is the PUB's focus on setting rates and increasing financial reserves, when risks materialize and the commitment to stakeholders and the financial markets to take the appropriate regulatory action when required. The other important consideration is that financial reserves will not be built through retained earnings for all risks, simply because risks can be identified.

MH appears to be promoting the proposed 2% rate path as the means to deal with all of the potential future risks that it might face. However, the high-level MH risk assessment, which is incomplete and unbalanced, and contains many speculative elements, is not consistent with the PUB rate-setting policy direction from Order 59/18.

[29] PUB Order 59/18, Pages 64 to 65

4.8 A Relative Assessment of Risks Since the Last GRA Does Not Support the MH Assessment of Elevated Business & Financial Risks for Rate-Setting Purposes

The conclusion of the evaluation of MH's risk assessment for the purposes of this proceeding, is that a relative assessment of risks since the 2018/19 GRA does not support the utilities assessment of elevated business and financial risks for rate setting purposes. The MH ERM Program is in the early states of development and the high-level risk assessment that MH provided in the current Application, is incomplete and not balanced.

A more objective, balanced and complete assessment of MH's business and financial risks for rate-setting purposes, relative to the last GRA, including reduced risk as a result of the in-service of the major capital projects, the substantial improvement in MH's financial outlook, MH's own evidence, interest rate risk guidelines and risk quantifications, and the hydro-electric system value for climate change policy - does not support MH's assessment that its risks are elevated.

There are a number of inconsistencies between MH's high-level risk assessment, and its policies, spending priorities (cost increases of $2.3 billion) and enterprise planning priorities (multi-year journeys for ERM Program and asset management initiatives and incomplete IT planning and business case evaluations). MH's decision not to keep its Uncertainty Analysis current, is a step backwards for both its ERM Program and the analysis of risks for rate-setting purposes.

Finally, the PUB policy established in Order 59/18 is that rates should not be set to increase financial reserves for all identifiable risks and that the PUB is prepared to consider regulatory action, when and if, emerging risks actually materialize. The high-level MH risk assessment, which is incomplete and unbalanced, and contains many speculative elements, is not consistent with the PUB rate-setting policy direction from Order 59/18.

5.0 It is Recommended that the PUB Use its Policy Determinations from Order 59/18 & 69/19 and Place Primary Weight on Traditional Financial Metrics & Targets for Rate-Setting Purposes

Under the MCOS rate-setting methodology historically used to set MH rates, judgements with respect to the attainment of financial targets over time are used in order to balance the rate impacts to customers and the financial health of the utility. This Section of the Evidence contains the evaluation of financial targets for rate-setting purposes.

In the current Application, It appears that the MH 2% proposed rate path is determined as a "goal-seek", of the even-annual rate increase that is necessary to obtain the 70% debt ratio (30% equity ratio) by 2039/40, in accordance with the new legislative framework that will not become operative until April 1, 2025.

The conclusion from this Section of the Evidence is the recommendation that the PUB use its policy determinations from Orders 59/18 and 69/19 and place primary weight on traditional financial metrics and targets for rate-setting purposes. These include net income, net debt, interest coverage ratio and capital coverage ratio, with appropriate weight to the debt to equity ratio, credit rating agency reports and cash flow metrics. This recommendation is based on the following evaluation:

1. The PUB found in Order 70/22 that the legislative framework as it read prior to the passing of Bill 36 will continue to apply to the determination of MH rates for 2021/22, 2023/24 and 2024/25, for MH's current GRA. However, it appears that MH's proposed 2% rate path is based on the new legislative framework that will not become operative until April 1, 2025;
2. MH's positioning of the 2% rate path as being a requirement under the new framework is an overstatement and is not appropriately balanced. In the new legislative framework, the Province has prioritized concerns with respect to maximum general rate increases (customer rate impacts) over attainment of MH debt ratio targets (financial health);
3. It does not appear that MH considered if an absolute reduction in net debt levels of $2 billion that is inherent in the proposed 2% rate path, was appropriate from a policy perspective, considering that its assets are projected to increase $5 billion in the next 20-years, instead, accepting the net debt reduction as an outcome of the goal seek;
4. The MH proposed 2% rate path results in a capital structure approaching that of an investor-owned utility and significantly exceeds the debt ratio targets in the new legislative framework by the end of the 20-year financial forecast, casting doubt on whether this rate path represents an appropriate balancing between customers interests and the financial health of MH;
5. It is unfortunate that the MH Uncertainty Analysis was not enhanced for the current GRA to consider a rules-based rate-setting methodology with respect to the appropriate level

of financial reserves, as the increase in financial reserves that flow from the MH proposed 2% rate path is in the order of $5 billion over the 20 year forecast period;

6. The MH proposed 2% rate path, does not align well with the PUB policy determinations in Orders 59/18 and 69/19, with respect to the appropriate financial targets to use for rate-setting purposes, as it places primary reliance on goal seeking to attain a 70:30 debt to equity ratio target by 2039/40 and considerable weight on credit rating agency reports and cash flow concerns; and
7. The use of a number of traditional financial metrics and financial ratios elevates rate-setting to that of policy judgement of an appropriate and balanced rate path and not the false precision of mechanistic goal seeking of one financial ratio (debt to equity ratio).

5.1 Judgements on Pace of Attainment of Financial Targets Are Used in the MH Rate-Setting Process in Order to Balance Rate Impacts to Customers with the Financial Health of the Utility

Under the MCOS rate-setting methodology that was briefly described in Section 4.1 of this Evidence, judgements with respect to the attainment of financial targets over time are used in the MH rate-setting process in order to balance the rate impacts to customers with the financial health of the utility.

Under the MCOS, not only the forecasts of revenues and expenses in the Test Years under review, but also the forecasts in the MH long-term financial forecast are used to make informed judgements on how the proposed rate increase in the test year(s) impact the longer-term financial outlook and rate trajectory for MH. As such, the MCOS approach is essentially a rate-smoothing approach designed to promote rate stability and predictability for customers and balance rate impacts on customers and the financial integrity (financial health) of MH, over the longer-term.

In prior MH GRA's, the PUB have traditionally used financial metrics such as net income, net debt and retained earnings and three long-standing MH financial targets (debt to equity ratio, interest coverage ratio and capital coverage ratio) to assess MH's financial health for rate-setting purposes. The description and purpose behind the three long-standing financial targets, can be summarized as follows:

1. **Debt to equity ratio**: a measure of the proportion of MH's assets that are financed by internally generated funds (equity), as compared to debt. The long-standing MH target was to maintain a minimum equity ratio of 25%;
2. **Interest coverage ratio**: a measure of the ability of MH to meet interest payments with cash flow. The long-standing MH target was to maintain and earnings before interest, taxes, depreciation and amortization (EBITDA) interest coverage ratio with a minimum target of greater than 1.80; and

3. **Capital coverage ratio**: a measure of the ability of MH to fund sustaining capital expenditures through cash flow from operations. The longstanding MH target was to maintain a capital coverage ratio of greater than 1.20.

The three traditional financial targets that have been used by the PUB for rate-setting in the past, incorporate elements of the three primary financial statements. Equity and debt from the statement of financial position, EBITDA from the statement of income and cash flow from operations from the statement of cash flows. In doing so, they provide a robust picture of MH's financial health, for rate-setting purposes.

5.2 The MH 2% Proposed Rate Path is a Goal Seek to Obtain a 70% Debt Ratio by 2039/40

The PUB found in Order 70/22 that the legislative framework as it read prior to the passing of Bill 36 will continue to apply to the determination of MH rates for 2021/22, 2023/24 and 2024/25, for MH's current GRA[30].

However, it appears that MH's proposed 2% rate path is based on a goal seek to meet debt ratio targets in the new legislative framework that will not become operative until April 1, 2025.

Under the new legislative framework, the policy of the Provincial Government is that, subject to maximum general rate increases that must not exceed the less of 5% and the Consumer Price Index (CPI), MH achieve a target debt to equity ratio of (i) 80:20 by March 31, 2035 and (ii) 70:30 by March 31, 2040 and that (iii) any additional financial targets established by regulation be maintained.

MH interpretation of the new legislation is that (i) the 80% target debt ratio is the maximum level of debt in the capital structure on a go-forward basis, with 2034/35 as the latest date for achievement and (ii) the 70% target debt ratio is the new long-term financial target for MH, with 2039/40 as the latest date for achievement.

MH also indicates that (i) until regulations with respect to any additional financial targets is established, it is not formally adopting any additional financial measure or targets and (ii) notwithstanding, it continues to monitor the long-standing financial metrics such as interest coverage and capital coverage ratios, as well as trends in net debt, cash flow surplus/deficits, the self-financing ratio and cash flow to net debt ratio.

While MH provides all of the above noted financial metrics and financial ratios in the Application for the 20-year period of the amended financial forecast (MH22 for shorthand), it appears that the 2% proposed rate path was determined as a "goal-seek" to obtain the 70% debt ratio (30% equity ratio) by 2039/40. That is, the 2% proposed rate path is the even-annual rate increase for

[30] PUB Order 70/22, Page 5

20-years that solves the equation of reaching a 70% debt ratio by 2039/40. The evidence of this circumstance is that the 30% debt ratio is achieved exactly in 2039/40 in MH22 (please see Figure 6 in Section 5.5 of this Evidence).

Despite MH monitoring additional financial ratios, it has not presented these ratios to Credit Rating Agencies in the most current presentations, as they have not been established under regulation and the MHEB has not adopted targets for these measures. In MH's view, the three traditional financial targets, represent all three financial statements, allow for consistent presentation over time and demonstrate similar trends to the additional financial metrics that MH is monitoring[31].

5.3 The MH Proposed 2% Rate Path Does Not Consider that Under the New Legislative Framework Customer Rate Impacts Prevail Over Debt Ratio Target Policy

The first concern with respect to MH's goal-seek to develop the proposed 2% rate path, is that MH does not appear to have considered that the new legislative framework that becomes operating on April 1, 2025, prioritizes the level of customer rate impacts over the attainment of debt ratios.

The new legislative framework states that despite the policy with respect to the attainment of debt ratio targets, the provisions with respect to the maximum general rate increase will prevail. In other words, in the event of a conflict between the rate increases necessary to attain the debt ratios and the maximum rate increases in accordance with what MH refers to as the "rate cap provisions" of the new framework, the rate cap provisions will prevail. In the information request process, it was confirmed that MH agrees with this interpretation of the new legislative framework that it set to become operative on April 1, 2025[32].

The implications of this agreed to interpretation of the new legislative framework are that that the debt ratio targets are policy, with a certain degree of flexibility, but the rate cap provisions will determine the actual rate increases. As such, it appears that the Province has prioritized concerns with respect to maximum general rate increases (customer rate impacts) over attainment of MH debt ratio targets (financial health).

MH's positioning of the proposed 2% rate path as being a requirement under the new legislative framework is an overstatement and it not appropriately balanced, otherwise the priority would have been enacted in the other direction (the debt ratio target policy would have prevailed over the rate cap provisions, in the event of a conflict).

[31] Coalition/MH I-49

[32] Coalition/MH II-10 c

5.4 The MH Proposed 2% Rate Path Results in Reduction of the Absolute Levels of Net Debt by $2 Billion Despite the Forecast that MH's Asset will Grow by $5 Billion

The second concern with respect to MH's goal-seek to develop the proposed 2% rate path, is that this formulaic rate path results in a $2 billion absolute reduction in the net debt of MH by 2041/42, despite MH's own forecasts that its asset base is projected to increase by $5 billion in the next 20-years.

The following figure provides a comparison of the change in total assets and net debt over the 20-year MH22, demonstrating the source of the $5 billion increase in total assets and $2 billion decrease in net debt over the forecast period:

Figure 5: Total Asset & Net Debt Changes - MH22 - $Millions

1	2	3	4	5	6	7
Year	Total Assets MH22	Total Assets Inc (Dec)	Total Assets Cumulative Inc (Dec)	Net Debt MH22	Net Debt Inc (Dec)	Net Debt Cumulative Inc (Dec)
2023	30403	0	**0**	22963	0	**0**
2024	29790	-613	**-613**	22529	-434	**-434**
2025	30038	248	**-365**	22341	-188	**-622**
2026	30251	213	**-152**	22371	30	**-592**
2027	30251	0	**-152**	22322	-49	**-641**
2028	30495	244	**92**	22356	34	**-607**
2029	30770	275	**367**	22401	45	**-562**
2030	30807	37	**404**	22451	50	**-512**
2031	31066	259	**663**	22471	20	**-492**
2032	31419	353	**1016**	22424	-47	**-539**
2033	31879	460	**1476**	22372	-52	**-591**
2034	32604	725	**2201**	22270	-102	**-693**
2035	32994	390	**2591**	22090	-180	**-873**
2036	33200	206	**2797**	22030	-60	**-933**
2037	33820	620	**3417**	22063	33	**-900**
2038	34036	216	**3633**	21983	-80	**-980**
2039	34320	284	**3917**	21798	-185	**-1165**
2040	34860	540	**4457**	21656	-142	**-1307**
2041	35040	180	**4637**	21355	-301	**-1608**
2042	35422	382	**5019**	20930	-425	**-2033**

It is understood that after the investment in the major capital projects was funded primarily through debt financing, that it would be an appropriate objective to improve the relative proportion of debt and equity in MH's capital structure. Prior MH long-term financial forecasts at the 2014 NFAT and thereafter contained projections of MH debt to equity ratio being stuck at around 88:12 for a number of years after the in-service of the major capital projects.

The issue that is raised by the MH proposed 2% rate path, is whether an absolute reduction in the amount of net debt is an appropriate objective, when considering the projected increase in MH's asset base over the 20-year forecast.

As part of the information request process, MH clarified that in order to achieve the debt ratio targets in the new legislative framework, it is required to both (i) increase the level of equity and (ii) decrease the level of net debt.

MH also clarified that it is the 70% debt ratio target in 2039/40 that mathematically results in this requirement and not the 80% debt ratio target in 2034/35 (which could be achieved without an absolute reduction in net debt)[33]. As such, it does not appear that MH considered if an absolute reduction in net debt levels was appropriate from a policy perspective, instead, accepting it as an outcome of the goal seeking exercise to attain the 2039/40 debt ratio target.

If one were to simply accept MH's forecast of the growth in its total assets and the debt ratio target of 70% towards the back-end of the financial forecast period, without critical evaluation for rate-setting purposes – then $35 billion of total assets financed by 70% debt, would result in net debt of around $24.5 billion. This targeted level of net debt would be $3.6 billion higher than the $20.9 billion of net debt that is the result of the MH proposed 2% rate path.

This is the problem with mechanical goal seeking of the MH proposed 2% rate path to produce a desired outcome by a specific timeframe in the 20-year forecast. Under the judgemental MCOS rate-making methodology, with the PUB self-described mandate to balance the interests of customers with the financial health of MH[34], caution must be exercised around mechanical goal-seeking on one metric (in this case the debt to equity ratio) to ensure that there is an appropriate balancing of the interests.

The traditional use of a number of financial metrics and financial ratios to judge an appropriate and balanced rate path (as described in Section 5.1 of this Evidence) is preferable to a mechanistic goal seek on one financial ratio. The use of a number of financial metrics and financial ratios elevates rate setting to that of policy judgement and not the false precision of a mechanistic goal seek.

5.5 The 2% Rate Path Proposed by MH Results in a Capital Structure Approaching that of an Investor Owned Utility & Significantly Exceeds the Debt Ratio Targets in the New Legislative Framework

The third concern with respect to MH's goal-seek to develop the proposed 2% rate path, is that it results in a capital structure approaching that of an investor-owned utility and significantly

[33] Coalition/MH I-11 a b c and II-10 a b

[34] PUB Order 59/18, Section 1.0, Page 4

exceeds the debt ratio targets in the new legislative framework by the end of the 20-year financial forecast.

The following figure provides a summary of equity ratio target achievement and level of retained earnings under the MH proposed 2% rate path in MH22:

Figure 6: Equity Ratio Targets & Retained Earnings - MH22 - $Millions & %

1	2	3	4	5	6
Year	Equity Ratio MH22	Legisative Equity Ratio Target	Retained Earnings MH22	Retained Earnings Inc (Dec)	Retained Earnings Cumulative Inc (Dec)
2023	15%		3575	0	**0**
2024	17%		4044	469	**469**
2025	18%		4339	295	**764**
2026	18%		4488	149	**913**
2027	19%		4654	166	**1079**
2028	19%		4751	97	**1176**
2029	**20%**		4843	92	**1268**
2030	20%		4953	110	**1378**
2031	21%		5058	105	**1483**
2032	21%		5227	169	**1652**
2033	22%		5417	190	**1842**
2034	23%		5635	218	**2060**
2035	24%	**20%**	5912	277	**2337**
2036	25%		6162	250	**2587**
2037	27%		6444	282	**2869**
2038	28%		6753	309	**3178**
2039	29%		7112	359	**3537**
2040	**30%**	**30%**	7551	439	**3976**
2041	32%		8058	507	**4483**
2042	34%		8628	570	**5053**

The observations with respect to Figure 6, under the MH 2% proposed rate path, is as follows:

1. The 80:20 debt to equity ratio target is projected to be achieved in 2028/29, a full six (6) years ahead of the target in the new legislative framework;
2. The 70:30 debt to equity ratio target is projected to be achieved in 2039/40, exactly on the target in the new legislative framework;
3. MH is projected to achieve a 66:34 debt to equity ratio by the end of the 20-year forecast in 2041/42, which is 4% higher than the target in the new legislative framework; and
4. MH's financial reserves (retained earnings) are projected to grow $5.0 billion by the end of 2041/42.

MH is projected to attain a debt to equity ratio which is approaching the allowed range of IOU's of 65:35 to 60:40[35]. IOU's are allowed by their regulators to have this range of a capital structure as they are required to issue debt on a stand-alone basis. This is in contrast to MH's status as a Government Business Enterprise with a provincial guarantee of its debt, which does not borrow debt on the basis of its stand-alone financial metrics. If MH has the debt to equity ratio of an IOU, then one of the customer benefits of MH's status of a GBE of being able to employ more leverage and reduce the cost to customers (debt costs are less costly than equity), is not being achieved.

MH's projection of an equity ratio of 34% by 2041/42 under the proposed 2% rate path, exceeds the new legislative target by 4%. Also, it is observed that the expectation of an improvement in the MH debt to equity ratio of 5%, in the five-year period between 2034/35 and 2039/40, is quite aggressive. This contrasts with the expectation of a 5% projected improvement over the 12-year period between 2022/23 and 2034/35, which is more consistent with a policy objective of rate-smoothing under the MCOS rate-setting methodology.

These observations point to the concerns that the MH 2% proposed rate path exceeds the targets in the new legislative framework, and more importantly, casts doubt on whether this rate path represents an appropriate balancing between customers interests and the financial health of MH.

5.6 The 2% Rate Path Proposed by MH does Not Align with the PUB Policy Determinations in Order 59/18 with respect to Appropriate Financial Targets for Rate-Setting Purposes

The fourth concern with respect to MH's goal-seek to develop the proposed 2% rate path, is that it does not align well with the PUB policy determinations in Order 59/18, with respect to the appropriate financial targets to use for rate-setting purposes.

In the 2018/19 MH GRA, there was considerable evidence presented with respect to the appropriate financial metrics and targets to use for rate-setting purposes, in the context of a revised financial plan that targeted achievement of a 75:25 debt to ratio target in 10-years and resulted in a 7.9% rate path.

In its decision (Order 59/18) on the 2018/19 GRA, the PUB rejected the 7.9% rate path and associated financial plan, but set out foundational policy, guidance and findings on the

[35] BCUC Generic Cost of Capital Proceeding, Concentric Energy Advisors Inc. Cost of Capital Estimation Evidence (January 2022), Figure 64, Page 149 and Figure 65, Page 151, indicates an average approved equity ratio for large Canadian Natural Gas & Electricity IOU's of 37% and 39%, respectively.

appropriate financial targets to use for rate-setting purposes. The key aspects of this rate-setting policy guidance, can be summarized as follows:[36]

1. In finding the right balance between rates increases and the level of debt to fund major capital projects, the PUB will be guided by two considerations. The first consideration is the financial reserves that MH should hold to manage risks (such as drought). The second is to place the amount of debt and retained earnings in a different perspective, by considering cash flow, by using two MH long-standing financial metrics of interest coverage ratio and capital coverage ratio;
2. The PUB found that the debt to equity ratio is a questionable metric for a vertically integrated monopoly crown utility with a debt guarantee from the Provincial government;
3. The 75:25 debt to equity ratio target could remain a long-term objective, but the PUB was not prepared to consider pacing rate increases to obtain a particular equity target level at least until the current phase of major capital construction is complete;
4. The PUB concluded that there was merit to gaining a better understanding of the financial reserves required by MH under various circumstances and directed MH to participate in a technical conference for consideration of a minimum retained earnings test or similar test to provide guidance in the setting of consumer rates for use in rule-based regulation;
5. Care must be taken to avoid placing too much weight on reports by credit rating agencies and credit ratings and capital markets are related, but not the same thing; and
6. The PUB accepted that capital markets would be reassured by a long-term rate plan that acceptably manages risk and regulatory action by the PUB to address circumstances as they arise.

The important considerations in this rate-setting policy guidance, is the PUB's focus on the traditional rate setting metrics/ratios of levels of financial reserves and debt, and interest coverage and capital coverage ratios. The PUB placed the debt to equity ratio and credit rating agency reports in their appropriate context as not being the sole determinates of the pacing of rate increases to balance the interests of customers with the financial health of MH. The PUB also expressed its interest in rule-based regulation through consideration of the appropriate levels of financial reserves to manage risks.

In Order 69/19, with respect to the MH 2019/20 Rate Application, the PUB found the following with respect to financial ratios:[37]

1. The change in presentation by MH of capitalized interest on the Cash Flow statement to be included in cash flow from operating activities, is inconsistent with rate-setting principles and potentially confusing to stakeholders. As such, this change was not to be taken into consideration when considering cash flow sufficiency for rate-setting purposes;

[36] PUB Order 59/18, Pages 61 to 69
[37] PUB Order 69/19, Pages 27 to 30

2. It reiterated its findings from Order 59/18, with respect to financial metrics, uses of financial reserves, the weight to be afforded credit rating agency reports and consideration of rule-based regulation through a technical conference.

Cash Flow Reclassifications by MH for Financial Reporting Purposes

Despite MH’s concerns with respect to the levels of cash flow and the PUB findings from Order 69/19, it chose to make a series of changes to the presentation of its cash flow statement for financial reporting purposes in its 2021/22 financial statements. These changes include reclassifying cash flows related to regulatory deferrals such as Demand Side Management (DSM) expenditures, ineligible overhead and regulatory costs as well as costs associated with the perpetual obligation related to the purchase of Winnipeg Hydro from the City of Winnipeg - from Investing Activities to Operating Activities.

The result of these reclassifications are to significantly reduce the Cash Flow from Operating activities and associated cash flow metrics (capital coverage ratio, cash flow to net debt ratio and self-financing ratio) that have been presented in the current GRA for rate-setting purposes, for both actual results and the long-term forecast (MH22).

The following figure provides the EBITDA Interest Coverage Ratios for MH22, and shows the reduction in the Capital Coverage Ratio as a result of change in the cash flow presentation that was made by MH for financial reporting purposes in 2022:

Figure 7: EBITDA Interest Coverage & Capital Coverage Ratios - MH22

1	2	3	4	5
				(3 - 4)
Year	Interest Coverage Ratio MH22	Capital Coverage Ratio MH22	Capital Coverage Ratio Prior Cash Flow Presentation MH22	Capital Coverage Ratio Inc (Dec)
2023	2.48	2.26	2.50	-0.24
2024	2.21	2.23	2.45	-0.22
2025	2.06	1.61	1.83	-0.22
2026	1.92	1.20	1.41	-0.21
2027	1.95	1.21	1.42	-0.21
2028	1.89	**1.08**	1.27	-0.19
2029	1.90	**1.06**	1.25	-0.19
2030	1.95	**1.06**	1.24	-0.18
2031	1.99	**1.08**	1.23	-0.15
2032	2.12	**1.16**	1.29	-0.13
2033	2.17	**1.16**	1.30	-0.14
2034	2.24	1.21	1.35	-0.14
2035	2.33	1.29	1.43	-0.14
2036	2.36	1.27	1.41	-0.14
2037	2.44	1.32	1.46	-0.14
2038	2.53	1.37	1.51	-0.14
2039	2.64	1.43	1.57	-0.14
2040	2.79	1.52	1.67	-0.15
2041	2.92	1.59	1.73	-0.14
2042	3.07	1.66	1.80	-0.14

The observations from Figure 7, are as follows:

1. Even with the $2.3 billion of higher O&A and BOC expenditures in MH22, the EBITDA Interest Coverage Ratio is higher than the historic 1.80 target in all years of the 20-year forecast;
2. In most of the years of MH22, the Interest Coverage Ratio is well in excess of 2.00 and by the end of the forecast period is in excess of 3.00;
3. Even with the same higher levels of O&A and BOC expenditures and the cash flow presentation changes for financial reporting purposes (which reduces the ratio by 0.13 to 0.24), the Capital Coverage ratio in MH16 meets or exceeds the historic 1.20 target in all but six years of the forecast; and
4. With the prior cash flow presentation for rate-setting purposes, the restated Capital Coverage ratio in MH22 exceeds the target in all years of the 20-year forecast, and by the end of the forecast period is around 1.80.

While MH is in control of the presentation of cash flows for financial reporting purposes, the issue for this proceeding is the presentation to be used for rate-setting purposes. As was noted above, when MH made previous changes for financial reporting purposes such that interest capitalized was reclassified from investing to operating activities, the PUB determined in Order 69/19, that this change should not to be taken into consideration when considering cash flow sufficiency for rate-setting purposes.

The current cash flow presentation changes with respect to regulatory deferrals and the perpetual City of Winnipeg obligation for financial reporting purposes, appear to be a follow on to the prior change to interest capitalized.

The net result of the application of regulatory accounting principles to MH's income statement is that the costs associated with regulatory deferrals are deferred and amortized for rate-setting purposes, not dissimilar to the treatment of property, plant and equipment for rate-setting purposes. For instance, for rate-setting purpose, MH considers DSM expenditures to be system resource (an alternative to additional generation resources) and as such has historically deferred and amortized DSM expenditures over a 10-year period. In addition, the City of Winnipeg perpetual obligation is a result of the purchase of the assets of Winnipeg Hydro by Manitoba Hydro from the City of Winnipeg.

As such, it would appear that the cash flow treatment for both the regulatory deferrals and the City of Winnipeg perpetual obligation for rate-setting purposes, would most appropriately be considered as an investing activity, consistent with rate-setting principles. It would also be appropriate that the PUB make the same determination as Order 69/19 and maintain the presentation of these costs as investing activities when considering cash flow sufficiency for rate-setting purposes in the current GRA.

Technical Conference for Rule-Based Regulation & MH Uncertainty Analysis

In Order 70/22 (at page 5), the PUB found that the technical conference that was envisioned to consider rule-based regulation is no longer achievable in advance of the filing of the current GRA, and as such did not set aside this directive, but varied it to allow for consideration of alternative rate scenarios and impacts on financial metrics as part of this GRA.

In the Consumers Coalition evidence from the 2019/20 MH Rate Application[38], it was recommended that MH's Uncertainty Analysis could be enhanced for the next GRA to provide a quantitative tool to further guide the incorporation of risks considerations and the appropriate level of financial reserves, into rate-setting. Potential enhancements that were identified, included applying probabilistic thresholds, building in routine management responses (policy changes and cost control by MH) and regulatory responses (rate increases by the PUB), and

[38] Consumers Coalition & Winnipeg Harvest Exhibit # 7-1, Section 9.3, Pages 96 to 99

assessing the residual risk and sufficiency of financial reserves, after these management actions and regulatory actions were built into the analysis.

It was also observed that this was best achieved through a technical conference or generic hearing which would set these rules – such that these rules could be used to determine the capital and financial reserve requirements in subsequent specific rate application hearings.

The conclusions and recommendations from the 2019/20 MH Rate Application with respect to the use of the Uncertainty Analysis to consider rule-based regulation, are as applicable now as they were in the prior MH rate proceeding. The absence of the MH Uncertainty Analysis in the current GRA, did not allow for further detailed consideration of rule-based regulation in this proceeding as the financial forecast and one-off risk sensitivities do not allow for effective and efficient consideration of such a rate-setting methodology.

It is unfortunate that the MH Uncertainty Analysis was not enhanced for the current GRA to consider rules-based rate-setting methodology as to the appropriate level of financial reserves, as the increase in financial reserves that flow from the MH proposed 2% rate path are literally a "$5 billion issue" (Please see Figure 6 from Section 5.5 of this Evidence).

However, the concepts of setting-rates by considering management actions and regulatory action and residual risk associated with financial reserve levels can be applied as part of making judgements and recommending alternate rate paths for consideration by the PUB.

MH's proposed 2% rate path, does not align well with the PUB policy determinations in Order 59/18, with respect to the appropriate financial targets to use for rate-setting purposes. The proposed 2% rate path places primary reliance on goal seeking to attain a 70:30 debt to equity ratio target by 2039/40 and considerable weight on credit rating agency reports and cash flow concerns. The presentation in the GRA of the more traditional financial ratios used for rate-setting by MH, appear to be more of a by-product of the primary reliance on the debt to equity ratio and credit rating/cash flow concerns, rather than receiving the weight in accordance with the PUB policy guidance.

5.7 It is Recommended that the PUB Use its Policy Determinations from Orders 59/18 & 69/19 and Place Primary Weight on Traditional Financial Targets for Rate-Setting Purposes

The conclusion of the evaluation of MH's financial targets for the purposes of this proceeding, is the recommendation that the PUB use its policy determinations from Orders 59/18 and 69/19 and place primary weight on the traditional financial targets for rate-setting purposes in this GRA.

The PUB found in Order 70/22, that the legislative framework as it read prior to the passing of Bill 36 will continue to apply to the determination of MH rates for 2021/22, 2023/24 and 2024/25, for MH's current GRA.

However, it appears that the MH 2% proposed rate path is determined as a “goal-seek” as the even-annual rate increase that is necessary to obtain the 70% debt ratio (30% equity ratio) by 2039/40 in accordance with the new legislative framework to become operative on April 1, 2025. MH’s positioning of the proposed 2% rate path as being a requirement under the new framework is an overstatement and is not appropriately balanced. An appropriate interpretation of the new framework is that the Province has prioritized concerns with respect to maximum general rate increases (customer rate impacts) over attainment of MH debt ratio targets (financial health).

The MH proposed 2% rate path results in a number of concerns for rate-setting purposes:

1. A reduction of the absolute levels of net debt by $2 billion despite the forecast that MH’s assets will grow by $5 billion over the 20-year financial forecast period;
2. Achievement the 80:20 debt to equity target under the new legislative framework, a full six years ahead of the target timeframe;
3. The expectation of an improvement in the MH debt to equity ratio of 5%, in the five-year period between 2034/35 and 2039/40, which is quite aggressive;
4. The projected attainment a debt to equity ratio of 66:34 by 2041/42, which is a full 4% higher than the debt ratio target; and
5. A debt to equity ratio which is approaching the allowed range of IOU’s of 65:35 to 60:40. Thus negating one of the customer benefits of MH’s status of a GBE, with a provincial debt guarantee, of being able to employ more leverage and reducing the cost to customers.

These observations cast doubt on whether the 2% rate path represents an appropriate balancing between customers interests and the financial health of MH.

It is unfortunate that the MH Uncertainty Analysis was not enhanced for the current GRA to consider rules-based rate-setting methodology for the appropriate level of financial reserves, as the increase in financial reserves that flow from the MH proposed 2% rate path are literally a “$5 billion issue”.

Finally, MH’s proposed 2% rate path, does not align well with the PUB policy determinations in Orders 59/18 and 69/19, with respect to the appropriate financial targets to use for rate-setting purposes, as it places primary reliance on goal seeking to attain a 70:30 debt to equity ratio target by 2039/40 and considerable weight on credit rating agency reports and cash flow concerns. The presentation by MH in the GRA of the more traditional financial ratios used for rate-setting appear to be more of a by-product of the primary reliance on the debt to equity ratio and credit rating/cash flow concerns, rather than receiving the weight in accordance with the PUB policy guidance.

The traditional use of a number of financial metrics and financial ratios to judge an appropriate and balanced rate path is preferable to a mechanistic goal seek on one financial ratio. The use of a number of financial metrics and financial ratios elevates rate setting to that of policy judgement and not the false precision of a mechanistic goal seek.

6.0 The $2.3 Billion Increase in O&A and BOC Since the Last GRA is Significantly Related to Strategy 2040 and Associated Initiatives and is Inconsistent With/Unresponsive To Prior PUB Findings and Regulatory Signaling to Control & Prioritize Controllable Costs

Under the MCOS rate-setting methodology historically used to set MH rates, judgements on the necessary and prudent levels of O&A and BOC spending to include in rates are part of the MH rate-setting process. O&A is forecast in the order of $700 million and Depreciation & Amortization expense is forecast in the order of $650 million, in the Test Years. This Section of the Evidence contains the evaluation of MH's O&A and BOC forecasts, for rate-setting purposes.

The conclusion from this Section of the Evidence is that the $2.3 billion increase in O&A and BOC in the current financial forecast is significantly related to Strategy 2040 and associated initiatives and is inconsistent with and unresponsive to, prior PUB findings and regulatory signaling to MH to control and prioritize its controllable O&A and BOC costs. This conclusion is based on the following evaluation:

1. MH has shifted its policy orientation from prior regulatory proceedings to pursue cost savings and instead has taken a position that it has little influence over O&A and BOC expenditures;
2. Successfully controlling costs requires a long-term strategic approach, but the vacancy management approach currently used by MH is not a strategy or a plan, but rather, a short-term tactical response, that does not effectively manage O&A costs;
3. The projected $175 Million or 34% increase in O&A costs between 2019/20 and 2024/25 represents an average annual growth rate of 6.1% and does not demonstrate a commitment to O&A cost control;
4. An evaluation of O&A cost increases between 2019/20 and 2024/25 demonstrates that there is a $72 million increase in O&A costs and 116 increase in FTE's in the MH Governance & Services business units. These increases are primarily due to Strategy 2040 and related strategic initiatives, including significant expenditures on technology, without an accompanying IT Strategic plan or associated business cases;
5. Extrapolating these near-term O&A increased into the forecast period results in a projected cumulative increase in O&A costs of $1.5 billion compared to the last GRA;
6. There is a policy concern that a 15-year time frame for MH to achieve a reasonable maturity level on asset management does not demonstrate a commitment to prioritizing BOC spending. In addition, the MH capital expenditure plan has limitations for rate setting purposes;
7. An evaluation of the projected $0.8 billion cumulative increase in BOC spending compared to the last GRA demonstrates that incremental expenditures of $480 million related to Strategy 2040 appear to be prioritized over sustaining capital expenditures. This is the situation despite the fact that there are no business cases for these initiatives and MH's stated concerns with respect to aging infrastructure; and

8. MH's forecasts of O&A and BOC spending are inconsistent with, not responsive to and essentially ignore the sustained and consistent regulatory decisions and signaling from the PUB to MH at prior regulatory proceedings in the past five years, with respect to the on-going need to control O&A costs and BOC spending after the in-service of Keeyask and the need to develop a mature asset management process to justify proposed levels of BOC spending.

6.1 Judgements on the Necessary and Prudent Levels of O&A and BOC Spending to Include in Rates Are Part of the MH Rate-Setting Process.

Under the MCOS rate-setting methodology that has been traditionally used to set MH rates, the PUB makes judgements with respect to the necessary and prudent levels of O&A and BOC (through Depreciation Expense) as part of the process of determining rate increases[39]. In making these judgements for rate-setting purposes, the PUB considers MH's approach and efforts to prioritize and control O&A and BOC expenditures.

The levels of MH's Operating & Administrative (O&A) expense and Business Operations Capital (BOC) are important for rate-setting as O&A and BOC constitute significant expenditures for MH. As outlined in Section 3.8 of this Evidence, the total O&A and BOC spending in the 2023/24 and 2024/25 Test Years are in the Order of $1.2 billion per year (O&A in the order of $700 million and BOC in the order of $500 million).

O&A expense is part of the MH revenue requirements on a 1:1 basis. In MH22, O&A is forecast to increase from the level of around $690 million in 2024/25 to approximately $940 million by 2041/42.

It is also noted that the last detailed review of MH's O&A costs for rate-setting purposes was conducted during the 2015/16 GRA, with follow up review in the 2016/17 Interim Rate Application. As such, this significant portion of the MH revenue requirements has not been reviewed in detail for rate-setting purposes for seven to eight years. The PUB did make findings with respect to high-level O&A targets and BOC levels for rate-setting purposes in the 2018/19 GRA, 2019/20 Rate Application and 2021/22 Interim Application, which are discussed in Section 6.9, below.

BOC spending becomes part of the revenue requirements through depreciation expense on these expenditures, once the underlying projects or programs enter service. MH's assets tend to have relatively long service lives, so the impact of BOC is somewhat muted in any particular test year. However, years of successive BOC spending accumulate in increased Depreciation Expense over time and as such can result in significant pressure on MH's revenue requirement and rates.

[39] PUB Order 5/12, Pages 25 to 27

In MH22, Depreciation & Amortization expense is forecast to increase from the level of around $640 million in 2024/25 to approximately $1.1 million by 2041/42. In addition, BOC spending is a significant use of cash for MH, and as such consideration of cash flow sufficiency for rate-setting purposes inherently needs to consider the projected levels of BOC spending.

The rate-setting approach applied to MH contrasts with the more formulaic RBROR rate-setting methodology that focuses only on the test years and where a regulator will make specific determinations of the levels of O&A and BOC to include in rates, as well as any specific disallowances of O&A and BOC, that will not be included in rates.

6.2 MH Asserts that it is Committed to Cost Control but Has Shifted its Policy Orientation Away from Cost Savings to Continuous Improvement & Taken a Position that It Has Little Influence Over O&A and BOC Expenditures

MH asserts that it is committed to cost control but has shifted its policy orientation away from cost savings to continuous improvement and changed its position from prior regulatory proceedings to one in which it has little influence over O&A and BOC expenditures.

MH position that it has limited influence over its O&A costs, asserting that there are certain expenditures that management has little to no control over and that it has been in a cost savings mode for several years and it is not sustainable to continue in a cost savings mode indefinitely.[40] MH also asserts that it is committed to effectively managing O&A costs but there has been a shift from cost savings to continuous evaluation of process improvement to encourage the containment of costs and make improvements to the way that it works.

MH also takes the position that it currently has limited influence over depreciation and amortization expense as the current level of Depreciation expense is based on assets already in service. It also asserts there is limited ability to minimize or reduce future depreciation and amortization expense as MH needs to make sustaining capital expenditures (BOC) to ensure system reliability and performance are maintained[41].

MH’s policy orientation at prior GRA proceedings was that it was committed to controlling and reducing its controllable costs of O&A and BOC and balancing cost control and rate increases. At the 2014 NFAT proceeding, MH emphasized its commitment to controlling O&A costs and BOC expenditures and subsequent strategies were developed in the 2015/16 GRA and 2018/19 GRA to demonstrate this commitment.

At the 2015/16 GRA, a committed position reduction (attrition) strategy was developed to maintain O&A increases to below inflationary levels at 1% through a reduction of 330 operational positions over the 3-year period of 2014/15 to 2016/17. In the 2018/19 GRA, a Voluntary

[40] Coalition/MH I-6 h and II-6 b
[41] Coalition/MH I-6 i and II-6 c

Departure Program (VDP) strategy was developed to accelerate cost decreases through eliminating 900 full-time equivalent employees between 2016/17 and 2018/19.

The following Figure provides the results of these strategies and demonstrate the MH commitment to O&A cost control, through a flat or decreasing O&A costs over that period of time. Over the 5-year period between 2014/15 and 2019/20, O&A expenditures decreased by $26 million or 4.8% (cumulative inflation during that period was approximately 9.4%[42]):

Figure 8: Actual O&A Exenditures - 2015 to 2020 - $Millions						
	1	**2**	**3**	**4**	**5**	**6**
	2015	**2016**	**2017**	**2018**	**2019**	**2020**
	Actual	**Actual**	**Actual**	**Actual**	**Actual**	**Actual**
O&A Expenditures	538	543	536	517	507	512
$ Change from Prior Year		5	-7	-19	-10	5
% Change from Prior Year		**0.9%**	**-1.3%**	**-3.5%**	**-1.9%**	**1.0%**
$ Cumulative Change - 5 Years						**-26**
% Cumulative Change - 5 Years						**-4.8%**

It is also clear through the O&A forecasts that were provided by MH at the 2018/19 GRA, that the objectives in accelerating the O&A reductions was not simply temporary in nature, to be subsequently reversed through subsequent higher than inflationary increases, but rather to be sustained into the future to manage financial and rate pressures in a era of major capital projects.

MH's policy shift to continuous improvement and attitudinal shift to having little influence over costs is both not clear and concerning. The policy shift is not clear in terms of what performance metric is guiding MH's top-down budgeting process in terms of desired outcome and assessing the degree of success or alternatively, the need for corrective action.

The attitude shift is concerning and a red flag for rate-setting purposes, as a public utility's O&A and BOC costs are considered to be their most controllable costs and the financial levers that can be used to improve financial results and smooth rate increases over time.

In this regard it is noted that in a year of major drought, MH was overbudget $22 million on O&A costs and took no corrective action in 2021/22 to attempt to reduce O&A cost to or below budget. This is despite the fact that the worsening water conditions were apparent as early as its first quarter of 2021/22.[43]

[42] Coalition/MH I-13 b
[43] Coalition/MH I-19 a c and II-13a

These concerns will be further highlighted in Section 6.4 of this Evidence, where the analysis shows that MH's O&A costs are forecast to increase $175 million or 34.2% in the 5-year period between 2019/20 and 2024/25.

6.3 O&A Cost Control Requires a Long-Term Strategic Approach but MH's Vacancy Management Approach is a Short-Term Tactical Response that does Not Effectively Manage Costs

O&A Cost control requires a long-term strategic approach as compared to MH's approach of vacancy management, which is a short-term tactical response.

Successful O&A cost containment requires a strategic and long-term approach with a number of elements:

a) A strategy and plan, as was the approach used by MH in the 2015/16 GRA and 2018/19 GRA;
b) A commitment to actively manage O&A, find efficiencies, productivity enhancements and activities that the organization can stop doing - to help offset general wage increases, merit increases and fund the cost of strategic initiatives;
c) Multi-year O&A plans to manage on-going cost pressures, communicate a cost containment focus to departmental management and provides a commitment to funding levels for several years into the future. This also allows departmental management to take a longer-term view to develop efficiency initiatives, rather than short-term vacancy management which is reconsidered on an annual basis;
d) Setting stretch targets for the business units at the executive level through the top-down target setting process (strategic portion of the budgeting process) that considers the general strategic landscape, overall financial outlook, revenue requirements and rate pressures for a number of years into the future;
e) Communicating expectations to management and staff through the issuance of up-front budget guidelines before the bottom-up detailed departmental budgeting process commences;
f) A bottom-up detailed departmental budgeting exercise (the tactical portion of the budgeting process) that considers departmental operating plans and risk tolerances and identifies cost pressures;
g) Reconciliation of top-down stretch targets and bottom-up detailed budgets through assessment of key priorities and risks, and reallocating targets to higher priority and higher risk areas and away from lower priority and lower risk areas or imposing negative contingencies until specific cost reduction or efficiency initiatives can be identified at the departmental level;

h) Measurement of performance against budget targets that have been set down to the departmental or section level and reporting to senior management at regular intervals; and
i) Taking corrective action when necessary and on-going reinforcement by senior management during execution of the plan and into the next budgeting cycle.

MH asserts that it took a top-down approach to budgeting where O&A targets were set and bottom-up budgets were balanced to targets through vacancy rates, which were set at 552 FTE's (including enterprise wide vacancy factor of 66 FTE's) or 10% for 2022/23, 856 FTE's or 14% for 2023/24 and 767 FTE's or 13% for 2024/25.[44] MH did not provide any other details on how O&A targets were set[45] and confirmed that no other top-down adjustments were made for these fiscal years[46]. MH did not provide an indication if it planned to move to multi-year budgeting in the future, simply indicating that future budget processes will evolve to meet business needs[47].

The vacancy management approach used by MH in the Test Years is not a strategy or a plan. Rather, it is a short-term tactical response to be able to manage through to the next budget cycle.

The vacancy management approach used by MH does not result in longer-term cost containment through strategic and efficiency initiatives that reduce costs. Rather, it results in the need for a higher vacancy factor in subsequent budget cycles to offset the costs of rising wages and salaries and other cost pressures. The vacancy levels in MH's O&A budgets were increased from 10% in 2022/23 to 13% to 14% in the Test Years. Even at those levels of vacancies, the MH O&A forecast is increasing in the order of 8% per year in each of the Test Years, and 6% per year in the last 5 years.

In reviewing Tab 6 of the Application it is apparent that there is no plan for O&A cost containment. Tab 6 consists of 47 pages of material, with a few up-front pages describing the budget process and a few examples of continuous improvement initiatives and then 38 pages of details of O&A cost pressures.

This cost pressure approach is common in public utility rate applications in order to justify higher levels of O&A in rates. The concern is that management at public utilities become very good at identifying cost pressures in GRA's - but are not as skilled at identifying cost containment strategies or productivity initiatives, that are designed to reduce costs.

Also common in public utilities is the use of incremental budgeting approaches. In this type of budgeting approach, budgets for the next year are set using the prior year as a base year. The

[44] GSS/GSM/MH I-5 b
[45] Coalition/MH II-29 b
[46] Coalition/MH II-29 d
[47] Coalition/MH I-6 e

base year is then adjusted upward for (i) general wage increases (ii) merit and promotional increases (iii) other inflationary pressures and (iv) strategic initiatives.

While public utilities attempt to position this incremental budgeting approach as being consistent with active cost management and top-down budgeting, it is not. Rather, this budgeting approach is a passive form of cost management at best and guarantees higher operating costs as the utility is simply following the cost curve on its upward trajectory, instead of actively managing costs.

With the rising costs associated with Strategy 2040 and related strategic initiatives, it may warrant MH considering the implementation of a priority-based budgeting approach. Under such an approach, the O&A budget would be set by identifying and ranking services or programs, instead of the current approach of providing budgets targets to organizational units. O&A budgets targets could then be better linked with strategic objectives, with target O&A spending being moved to services/programs of greater priority and risk and away from services/programs of lower priority and risk.

A necessary first step for in developing a priority-based budget for MH would involve identifying electric services and programs and then developing a program view of MH's electricity O&A costs (as it currently does not have an electric program view).[48] MH currently has a program view of O&A for gas operations, but this is more of an outcome of budgeting based on organizational units and then taking the resulting resource allocations into a program view, rather than using the gas program view as a driver of O&A budgeting.

6.4 The $175 Million Increase in O&A Between 2019/20 and 2024/25 Represents an Average Annual Growth Rate of 6.1% and Does not Demonstrate a Commitment to O&A Cost Control

The $175 million increase in O&A for the 5-years between 2019/20 and 2024/25 represents a cumulative average growth rate of over 6% and does not demonstrate that MH has a commitment to O&A cost control.

The Figure below, provides a summary analysis of MH's O&A by cost category for three distinct time-frames (i) the 3-year period between 2019/20 Actual and 2022/23 Forecast (ii) the 2-year period between the 2022/23 Forecast and the 2024/25 Forecast and (iii) the entire 5-year time period from 2019/20 to 2024/25. The 5-year period was selected as the analysis period as the 2019/20 MH Rate Application was the last time that the high-level O&A targets of MH were reviewed by the PUB for rate setting purposes:

[48] GSS-GSM/MH 4 e

Figure 9: O&A Cost Category View - 2020 to 2025 - $ Millions									
	1	2	3	4	5	6	7	8	9
	2020 Actual	*2023 vs. 2020 $ Change*	*2023 vs. 2020 % Change*	2023 Forecast	*2025 vs. 2023 $ Change*	*2025 vs. 2023 % Change*	2025 Forecast	*2025 vs. 2020 $ Change*	*2025 vs. 2020 % Change*
Wages & Salaries	458	*1*	*0.2%*	459	*46*	*10.0%*	505	*47*	*10.3%*
Employee Benefits	124	*29*	*23.4%*	153	*13*	*8.5%*	166	*42*	*33.9%*
Overtime & Other	146	*-11*	*-7.5%*	135	*17*	*12.6%*	152	*6*	*4.1%*
Total Employee Related	**728**	***19***	***2.6%***	**747**	***76***	***10.2%***	**823**	***95***	***13.1%***
Less: Capitalized Costs	-287	*39*	*-13.6%*	-248	*-19*	*7.7%*	-267	*20*	*-7.0%*
Operational Employee Related	**441**	***58***	***13.2%***	**499**	***57***	***11.4%***	**556**	***115***	***26.1%***
Consulting & Professional	13	*12*	*92.3%*	25	*26*	*104.0%*	51	*38*	*292.3%*
Construction & Maintenance	23	*7*	*30.4%*	30	*5*	*16.7%*	35	*12*	*52.2%*
Building & Property Costs	29	*5*	*17.2%*	34	*5*	*14.7%*	39	*10*	*34.5%*
Computer Services	2	*6*	*300.0%*	8	*7*	*87.5%*	15	*13*	*650.0%*
Other External Srvces/Material	68	*7*	*10.3%*	75	*6*	*8.0%*	81	*13*	*19.1%*
External Srvces/Materials	**135**	***37***	***27.4%***	**172**	***49***	***28.5%***	**221**	***86***	***63.7%***
Other Costs/Recoveries	**-64**	***-18***	***28.1%***	**-82**	***-8***	***9.8%***	**-90**	***-26***	***40.6%***
Operational Non-Employee	**71**	***19***	***26.8%***	**90**	***41***	***45.6%***	**131**	***60***	***84.5%***
Total O&A	**512**	***77***	***15.0%***	**589**	***98***	***16.6%***	**687**	***175***	***34.2%***

The observations from the cost category O&A analysis in Figure 9 and the variance analysis provided by MH, are as follows:

1. Total O&A is forecast to increase $77 million or 15.0% from the **3-year period** from **2019/20 actual** to the **2022/23 forecast**, a cumulative average growth rate of 5.9% per year.[49] The main components of this increase are (i) an increase in employee benefits of $29 million (ii) a decrease in capitalized costs of $39 million and (iii) an increase in consulting & professional costs of $12 million;
2. **Wages & Salaries** increased by $1 million[50] over the 3-year period, as a result of general wage increases and merit increases of $28 million, mainly offset by other decreases that net to $27 million (which would include a decrease in FTE's of 94 as outlined in Section 6.5 of this Evidence);
3. The $29 million increase in **employee benefits** is primarily due to actuarial impacts (+$16 million), a forecast decrease in the discount rate (+$6 million) and other unspecified increases (+$6 million);[51]

[49] Coalition/MH I-67 g
[50] Coalition/MH II-33
[51] Coalition MH I-81 c and II-34 b

4. The $39 million decrease in **capitalized costs** is primarily due to the reduction in capitalized labour related to the wind down of the Keeyask Project, a shift from capital to operating activities and a decrease in capital activities due to the IBEW strike;[52]
5. The $12 million increase in **consulting & professional costs** is primarily due to work on strategic initiatives, costs related to Keeyask environmental monitoring and partnership commitments[53] and the change in accounting treatments for cloud computing arrangements;[54]
6. Total O&A is forecast to increase $98 million or 16.6% from the **2-year period** from **2022/23 forecast** to the **2024/25 forecast**, a cumulative average growth rate of 8.0% per year.[55] The main components of this increase are (i) an increase in Wages & Salaries of $46 million (ii) an increase in employee benefits of $13 million (iii) an increase in consulting & professional costs of $26 million and (iv) an increase in computer services of $7 million;
7. The increase in **wages & salaries** of $46 million[56] is primarily a result of general wage increases and merit increases totaling $26 million, and other increases that net to $20 million (which would include the increase in FTE's of 191 as outlined in Section 6.5 of this Evidence);
8. The $13 million increase in **employee benefits** is primarily due to increased wages & salaries and workforce changes (+$9 million) and phase 2 of the CPP enhancement which will begin in 2024 (+$5 million);[57]
9. The $26 million increase in **consulting & professional costs** is primarily due to the change in accounting treatment for cloud computing arrangements, an increase in cloud bases services and Keeyask terrestrial effects monitoring;[58] and
10. The $7 million increase in **computer services** is primarily due to SAP S/4HANA license costs due to the change in accounting treatment for cloud computing arrangements and an increase in cloud-based services.[59]

In summary, total O&A is forecast to increase $175 million or 34.2% over the **5-year period** from **2019/20 actual** to the **2024/25 forecast**, a cumulative average growth rate of 6.1% per year.[60] The main components of this increase are:

1. An increase in **wages & salaries** of **$47 million** or 10.3%, primarily related to general wage and merit increases and an increase in FTE's of 97;

[52] Application, Appendix 3.3, Section 1.2.5 and PUB/MH I-67, Figure 2
[53] PUB/MH I-76 c, Figure 4
[54] PUB/MH I-67, Figure 2
[55] Coalition/MH I 67 g
[56] Coalition/MH II-33
[57] Coalition MH I-81 c and II-34 b
[58] PUB/MH I-62 c, Figure 3 and Coalition/MH I-82 c, Figure 14
[59] PUB/MH I-62 c, Figure 3 and Coalition/MH I-82 c, Figure 14
[60] Coalition/MH I-67 g

2. An increase in **employee benefits** of **$42 million** or 33.9%, primarily related to actuarial impacts of $16 million, increased wages & salaries and workforce changes of $9 million, CPP changes of $5 million, discount rate changes of $5 million and other unspecified changes of $7 million;
3. A decrease in **capitalized costs** of **$20 million** or 7.0%, as a result of the wind down of the major capital projects. MH indicates that of the 517 employees working on the Bipole III and Keeyask projects, approximately 264 or 51% remain with MH. MH also provided an analysis on the number of FTE that were capitalized to capital projects over time, which indicated that the number has decreased by 253 FTE's (1,763 – 1,510) between 2019/20 and 2024/25; [61] and
4. An increase in **consulting & professional** and **computer services** costs of **$51 million** or 340.0% primarily due the change in accounting treatment for cloud computing arrangements, an increase in cloud-based services and SAP licensing costs and Keeyask monitoring and partnership commitments.

It is also noted that MH has assumed pension and benefit discount rates that range between 3.11% and 3.32% for 2022/23 and 3.75% to 4.00% for 2023/24 and 2024/25, respectively. The discount rate curve that MH uses to set its pension and benefit discount rates has ranged from 5.00% to 5.43% on December 31, 2022 and 4.53% to 5.25% on January 31, 2023, which is significantly higher than the assumed discount rates in MH22.

MH has also provided a calculation indicating that the reduction in pension and benefit costs from a 1% increase in the discount count rate could be in the order of $37 million, including remeasurement gains/losses.[62] As such, based on the most current information of pension and discount rates in the range of 5.00%, it would appear that the forecast pension and benefit expense for the three years could be overstated in a range of $37 million to $74 million. There is an inverse relationship such that increases in the pension discount rate result in a decrease in pension and benefit costs.

Finally, with the $175 million or 34.2% projected O&A increases in the 5-year period, which represents a cumulative average annual growth rate of 6.1%, it is not possible to conclude that MH is committed to controlling O&A costs.

While cumulative inflation over the last 5-year period is forecast by MH to total approximately 12.9%[63], the majority of MH's O&A costs relate to wages and salaries that are escalating at much lower annual rates that other types of cost that make up Manitoba CPI. The majority of the

[61] Coalition/MH I-78 d and PUB/MH I-70 b
[62] Coalition/MH I-81 b and II-34 c d
[63] Application, MFR 10, Page 5

general wage increases in that timeframe have been in the range of 0.5% to 1.5% based on the available unredacted information provided by MH.[64]

In addition, it does not appear that MH had a sound plan to reduce the number of FTE's returning to operational positions after the in-service of the major capital projects and was unable to take advantage of this potential opportunity to use attrition to reduce O&A cost pressures.

6.5 The FTE Increase Between 2019/20 and 2024/25 is Entirely in the Governance & Services Business Units and is Primarily Due to Strategy 2040 and Related Strategic Initiatives

The overall corporate FTE increase in the five-year period between 2019/20 and 2024/25 is entirely within the Governance and Services business units of MH and are primarily due to Strategy 2040 and related strategic initiatives.

For the purposes of this Evidence, **Governance & Services business units** is used as a collective shorthand for the following business units (i) President & CEO (ii) Digital & Technology (iii) HR, Safety, Health & Environment (iv) Chief Financial Officer and (v) External, Indigenous Relations and Communications – and **Operational business units** is used as a collective shorthand for the following business units (vi) Customer Solutions & Experience (vii) Asset Planning & Delivery and (viii) Operations.

The following figure summarizes the changes in FTE's by MH business unit for the same three timeframes as the analysis provided in Section 6.4 of this Evidence:

[64] Coalition/MH I-74

Figure 10: Business Unit FTE's - 2020 to 2025

	1	2	3	4	5	6	7	8	9
		2023 vs.	*2023 vs.*		*2025 vs.*	*2025 vs.*		*2025 vs.*	*2025 vs.*
	2020	*2020*	*2020*	2023	*2023*	*2023*	2025	*2020*	*2020*
	Actual	*Change*	*% Change*	Forecast	*Change*	*% Change*	Forecast	*Change*	*% Change*
President & CEO	8	*11*	*137.5%*	19	*2*	*10.5%*	21	*13*	*162.5%*
Digital & Technology	249	*-3*	*-1.2%*	246	*27*	*11.0%*	273	*24*	*9.6%*
HR, Safety, Health & Environ.	159	*9*	*5.7%*	168	*41*	*24.4%*	209	*50*	*31.5%*
Chief Financial Officer	352	*12*	*3.4%*	364	*8*	*2.2%*	372	*20*	*5.7%*
Exteral, IR. & Comm.	116	*6*	*5.2%*	122	*3*	*2.5%*	125	*9*	*7.8%*
Governance & Service BU's	**884**	***35***	***4.0%***	**919**	***81***	***8.8%***	**1000**	***116***	***13.1%***
Customer Solutions & Exper.	373	*-18*	*-4.8%*	355	*10*	*2.8%*	365	*-8*	*-2.1%*
Asset Planning & Delivery	1509	*-237*	*-15.7%*	1272	*35*	*2.8%*	1307	*-202*	*-13.4%*
Operations	2407	*126*	*5.2%*	2533	*65*	*2.6%*	2598	*191*	*7.9%*
Operational BU's	**4289**	**-129**	***-3.0%***	**4160**	**110**	***2.6%***	**4270**	**-19**	***-0.4%***
Total Business Units	**5173**	***-94***	***-1.8%***	**5079**	***191***	***3.8%***	**5270**	***97***	***1.9%***

The observations from the business unit FTE analysis in Figure 10 and the variance analysis provided by MH, are as follows:

1. For the **3-year period** between **2019/20 actual** and the **2022/23 forecast**, total FTE's decreased by 94, primarily as a result of a 129 FTE decrease in the Operational Business Units and partially offset by a 35 FTE increase in the Governance & Services Business Units;
2. For the **2-year period** between the **2022/23 forecast** and the **2024/25 forecast**, total FTE's are forecast to increase by 191, as a result of an 81 FTE increase in the Governance & Services Business Units and a 110 FTE increase in the Operational Business Units;
3. For the **5-year period** between the **2019/20 actual** and the **2024/25 forecast**, total FTE's are forecast to increase by 97, as a result of an overall 116 FTE increase in the Governance & Services Business Units and partially offset by an overall 19 FTE decrease in the Operational Business Units;
4. The overall 13 FTE increase in the **President & CEO** business unit is primarily in the Enterprise Excellence division and is due to initiatives associated with Strategy 2040, such as embedding change management, continuous evaluation and improvement and alignment to strategy[65];
5. The overall 24 FTE increase in the **Digital & Technology** business unit is primarily due to building out the business unit to support Strategy 2040 and execution of the D&T roadmap and filling of certain vacancies[66];

[65] Coalition/MH II-35 a

[66] Coalition/MH II-35 b

6. The overall 50 FTE increase in the **HR, Safety, Health & Environment** business unit is primarily due to supporting strategic initiatives associated with the business model review and alignment and filling vacancies;[67]
7. The overall 20 FTE increase in the **Chief Financial Officer** business unit is primarily due to strategic initiatives associated with Strategy 2040, filling vacancies in the Strategy & Enterprise Planning and Enterprise Risk Management divisions and moving MHI staff into the business unit as part of the business model review;[68]
8. The overall 8 FTE decrease in the **Customer Service & Experience** business unit is primarily due to the transfer of staff to Efficiency Manitoba and mostly offset by increases as a result of initiatives with respect to customer experience and journey;[69] and
9. The overall 11 net FTE decrease in the **Asset Planning & Delivery** and **Operations** business units is primarily due to the in-service of major capital projects and filling vacancies, mainly offset by the increase in Trade Trainees that have been consolidated in the Operations business unit;[70] and
10. There has been an **FTE increase in executive and senior management** since the last GRA, from 36 to 39 in total (3 additional directors) and an increase 21 of **managers positions** since 2021/22 that are primarily (19) in the Governance & Services business units and as a result of Strategy 2040, related strategic initiatives and the business model review.[71]

It is also noted that MH's actual FTE complement is under forecast by 86 FTE's to February of 2023.[72] As such, there is a potential for a positive variance in wages and salaries and other employee related costs in 2022/23.

In summary, the overall increase in FTE's between 2019/20 actual and 2024/25 forecast, results from a 116 FTE increase in the Governance & Services business units and based on MH's variance explanations is primarily due to Strategy 2040, the business model realignment and associated strategic initiatives such as the D&T roadmap. This FTE increase includes an additional 22 directors and managers primarily related to Strategy 2040 and related initiatives.

While MH has asserted that it is concerned about service reliability and customer experience, more than the entire increase in FTE's in the last 5-years analysis period are in the Governance & Services business units and there is an actual decrease in FTE's in the Operational business units. The variance explanations for the increases primarily relate to Strategy 2040 and related strategic initiatives.

[67] Coalition/MH II-35 c
[68] Coalition/MH II-35 d
[69] Coalition/MH II-35 f
[70] Coalition/MH II-35 g
[71] Coalition/MH I-4 c and II-35 i
[72] PUB/MH II-27 a

6.6 The Forecast O&A Increase of $175 Million Between 2019/20 and 2024/25 Includes $72 Million of Increases in Governance & Services Business Units which is Primarily Due to Strategy 2040 and Related Strategic Initiatives

The forecast O&A increase of $175 million in the five years between 2019/20 and 2024/25 includes $72 million of increases in Governance & Services business unit costs, which are primarily due to strategy 2020 and related strategic initiatives.

The following figure summarizes the changes in MH's O&A by business unit in the same three timeframes as Section 6.4 of this Evidence:

Figure 11: O&A Business Unit View - 2020 to 2025 - $Millions

	1	2	3	4	5	6	7	8	9
	2020 Actual	*2023 vs. 2020 $ Change*	*2023 vs. 2020 % Change*	2023 Forecast	*2025 vs. 2023 $ Change*	*2025 vs. 2023 % Change*	2025 Forecast	*2025 vs. 2020 $ Change*	*2025 vs. 2020 % Change*
President & CEO	3	*2*	*66.7%*	5	*1*	*20.0%*	6	*3*	*100.0%*
Digital & Technology	42	*10*	*23.8%*	52	*36*	*69.2%*	88	*46*	*109.5%*
HR, Safety, Health & Environ.	18	*1*	*5.6%*	19	*5*	*26.3%*	24	*6*	*33.3%*
Chief Financial Officer	54	*6*	*11.1%*	60	*6*	*10.0%*	66	*12*	*22.2%*
Exteral, IR. & Comm.	16	*4*	*25.0%*	20	*1*	*5.0%*	21	*5*	*31.3%*
Governance & Service BU's	**133**	***23***	***17.3%***	**156**	***49***	***31.4%***	**205**	***72***	***54.1%***
Customer Solutions & Exper.	51	*3*	*5.9%*	54	*2*	*3.7%*	56	*5*	*9.8%*
Asset Planning & Delivery	200	*-21*	*-10.5%*	179	*16*	*8.9%*	195	*-5*	*-2.5%*
Operations	319	*25*	*7.8%*	344	*33*	*9.6%*	377	*58*	*18.2%*
Operational BU's	**570**	**7**	***1.2%***	**577**	**51**	***8.8%***	**628**	***58***	***10.2%***
Total Business Units	**703**	***30***	**4.3%**	**733**	***100***	***13.6%***	**833**	***130***	***18.5%***
Non-BU Adjustments	**-191**	***47***	***-24.6%***	**-144**	***-2***	***1.4%***	**-146**	***45***	***-23.6%***
Total O&A	**512**	**77**	***15.0%***	**589**	**98**	***16.6%***	**687**	***175***	***34.2%***

The observations from the business O&A analysis in Figure 11 and MH variance explanations, are as follows[73]:

1. For the **three-year period** between **2019/20 actual** and the **2022/23 forecast**, O&A is forecast to increase $77 million, primarily as a result of a $47 million increase in non-business unit adjustments such as increases in employee benefits and capitalized costs and a $23 million increase in the Governance & Service business units,

[73] Coalition/MH I-83 c

2. The increase in the **Governance & Service business units** relates to (i) additional cloud software service contracts and higher software maintenance to support the foundational D&T Strategy 2040 roadmap, in the VP Digital & Technology division (ii) increased insurance premiums and coverage for Keeyask in the Enterprise Risk Management division, increased snow clearing and security costs and a return to pre-pandemic levels of spending in the Supply Chain division and (iii) higher professional & consulting costs related to partnership commitments for Keeyask operations, in the Indigenous & Community Relations Division;
3. For the **two-year period** between the **2022/23 forecast** and **2024/25 forecast**, O&A is forecast to increase $98 million, primarily as a result of a $51 million increase in the Operational business units and a $49 million increase in the Governance & Service business units;
4. The increase in the **Operational business units** relates to (i) a business unit vacancy factor as a result of labour market challenges while the business unit realignment is still underway in the VP Asset Planning & Delivery business unit (ii) higher wages & salaries from filing vacancies and higher building and property maintenance costs and other cost pressures in the System Operations and Generation Operations & Maintenance divisions (iii) and higher costs associated with additional trades trainees in the Operations Business Solutions & Services division;
5. The increase in the **Governance & Services business units** relates to (i) additional cloud software service contracts, higher software maintenance to support the foundational D&T Strategy 2040 roadmap and higher consulting costs for cloud based services, in the VP Digital & Technology and Information Technology Services divisions, (ii) higher wages & salaries for implementing of business model organizational changes and external recruitment services in the Human Resources and Safety, Health & Environment divisions and (iii) the integration of MHI staff, work on Strategy 2040 and higher insurance premiums in the Corporate Controller, Strategy & Enterprise Planning and Enterprise Risk Management divisions.

In summary, total O&A is forecast to increase $175 million or 34.2% over the **5-year period** from **2019/20 actual** to the **2024/25 forecast**, with the main contributors from the business unit O&A view being:

1. An increase in the **Governance & Service business unit** costs of $72 million or 54.1%, an increase in the **Operational business unit** costs of $58 million or 10.2% and a change in **non-business unit adjustments** of $45 million or 23.6%;
2. The increase in the **Governance & Service business units** costs, primarily relates to (i) a $46 million increase in Digital & Technology business unit for additional cloud software service contracts, higher software maintenance to support the foundational D&T Strategy 2040 roadmap and higher consulting costs for cloud based services (ii) a $12 million increase in the Chief Financial Officer business unit for higher insurance costs, the

integration of MHI staff and work on Strategy 2040 and (iii) a $6 million increase in the HR, Safety & Environment business unit related to higher wages & salaries for implementing of business model organizational changes and external recruitment services;

3. The increase in the **Operational business units** costs, primarily relates to (i) a $29 million increase in the Operations Business Solutions & Services division[74] related to the consolidation of the trades trainees (ii) a $17 million increase in the Generations Operations & Maintenance division[75] related to wage increases and filling vacancies and other cost pressures such as additional work on aging assets and inflationary pressures related to supply chain challenges and new requirements for zebra mussel mitigation and (iii) a $7 million increase in the Systems Operations division related to higher wages & salaries from filing vacancies and higher building and property maintenance costs and other cost pressures in the System Operations division; and
4. The change in the **non-business unit adjustments** primarily relates to (i) a $42 million increase in employee benefits and (ii) a $20 million decrease in capitalized costs - as described in Section 6.4 of this Evidence, partially offset by a $23 million increase in O&A costs charged to Centra Gas.

Similar to the conclusion in Section 6.5 of this Evidence, the largest increase in business unit O&A costs over the last five years, is found in the Governance & Services business units ($72 million). The average increase in these business unit costs is in the order of 10% per year, compared to the average increase in the operational business units which is in the order of 2% per year.

The variance explanations for the increases in the Governance & Services business primarily relate to Strategy 2040 and related strategic initiatives. The most significant portion of this increase relates to spending associated with IT initiatives such as SAP and other cloud-based computing arrangements. MH has not yet developed an IT Strategic Plan or the business cases that are necessary to support these initiatives for either business purposes or rate-setting purposes.

6.7 A 15 Year Time Frame to Achieve a Reasonable Maturity Level on Asset Management Does Not Demonstrate a Policy Commitment to Prioritizing BOC Spending

As was outlined in the 2018/19 GRA, MH launched a Corporate Asset Management initiative in 2016 in order to foster mature and consistent asset management practices across the various business units of the corporation. The initiative involved centralizing asset management

[74] Coalition/MH II-36 a
[75] Coalition/MH II 36 b

governance and developing a corporate asset management framework, including assessment of asset management practices, development of asset management policies and strategies and development of a detailed roadmap for the implementation of the framework.

The detailed technical assessment of MH's efforts towards the development of the asset management framework in the past eight years since 2016, is part of the scope of Midguard Consulting, and as such is not within the scope of this Evidence.

However, it is noted at a high-level that MH's most recent assessment is that it will take another seven years to implement this asset management framework to achieve a maturity level of 2.45 at MH.[76] From an overall policy, enterprise risk management and rate-setting perspective, this delay in implementation of the asset management framework is concerning.

MH assesses aging infrastructure as a top 10 enterprise risk that is increasing over time and describes investing in sustainment of aging assets as one of the reasons for the proposed 2% rate path. From a policy perspective, the asset management framework and underlying tools such as the Corporate Value Framework were intended to provide a means to prioritize capital spending, both from a business and rate-setting perspective. Prior findings of the PUB are that a mature asset management framework would be necessary in order for MH to justify levels of BOC that would be included in rates at subsequent GRAs.

Despite these circumstances, MH's asset management journey is expected to have taken a full 15 years since the launch in 2016. With this lack of urgency, it is not possible to conclude on a policy basis that MH has demonstrated a commitment to prioritizing BOC, for rate-setting purposes.

6.8 The MH Capital Expenditure Plan Has Limitations for Rate-Setting Purposes and Includes Incremental Expenditures of $480 Million that Relate to Strategy 2040 Initiatives

The MH capital expenditure plan has limitations for rate-setting purposes and includes incremental expenditures of $480 million that relate to Strategy 2040 initiatives.

MH provided what it refers to as its most current Capital Expenditure Plan (CEP)(CEP22 for shorthand in this Evidence) as Appendix 7.7 to the Application, noting that it has not prepared a Capital Expenditure Forecast (CEF) as previously known as a result of on-going work on Strategy 2040.

CEP22 differs from CEF's that have been filed in past MH GRA's, such as CEF16 from the 2018/19 GRA. Unlike these past CEF's, CEP22 did not provided project descriptions, project justifications, in-service dates, reasons for revisions to project cost estimates and 20-years of capital project

[76] PUB/MH II-34 a

expenditures, project descriptions for capital projects over $1 million, as was previously directed by the PUB[77] and commentary as to the reasons for changes in the CEF since the last GRA.

CEP22 only provided project details for 3-years (2022/23 to 2024/25) and 10-year and 20-year sub-totals. MH confirmed in the information request process that project details were not available beyond year 10 of the forecast (2032/33).[78] No project descriptions were provided for capital projects over $1 million. No commentary was provided on the overall reasons for changes in the CEP since the last GRA.

The above-noted limitations with respect to CEP22 make it difficult to provide meaningful analysis for rate-setting purposes on an overall basis. The information that is available is not complete and it is confusing in terms of how MH has built in placeholder budgets for significant capital expenditures into the details of CEP22. These placeholder budgets are associated with Proxy Dispatchable Capacity Resources ($1.4 billion), Bipole I and II HVDC Refurbishments ($1.0 to $1.8 billion), Long Spruce Generating Station Unit Overhauls ($265 million), Kettle Generating Station Unit Overhauls ($314 million), Advanced Metering Infrastructure (AMI) ($300 million) and Grid Modernization ($180 million).

The following figure provides a comparison of CEP22 with the last full CEF that was reviewed by the PUB in the 2018/19 GRA (CEF16 for shorthand), based on the limited information on the record of this proceeding:

Figure 12: Business Operations Capital - CEP22 vs CEF16 - $Millions

	1	2	3	4	5
	2023 Forecast	2024 Forecast	2025 Forecast	2023 to 2032 10 Years	2023 to 2036 14 Years
CEP22:					
Sustainment	286	313	354	4305	NA
Capacity & Growth	122	140	117	1551	NA
Business Op. Support	87	85	88	952	NA
Total	**495**	**538**	**559**	**6808**	**10514**
CEF16:					
Sustainment	353	374	423	4438	6654
Capacity & Growth	102	104	125	1315	1912
Business Op. Support	93	83	70	798	1179
Total	**548**	**561**	**618**	**6551**	**9745**
Difference CEP22 vs. CEF16:					
Sustainment	-67	-61	-69	-133	NA
Capacity & Growth	20	36	-8	236	NA
Business Op. Support	-6	2	18	154	NA
Total Difference Inc (Dec)	**-53**	**-23**	**-59**	**257**	**769**

[77] PUB Order 73/15, Directive #15

[78] MIPUG/MH I-80

The observations from the BOC analysis from Figure 12, are as follows:[79]

1. Total BOC expenditures in CEP22 are expected to decrease by $53 million, $23 million and $59 million, in the 2022/23, 2023/24 and 2024/25 forecasts, respectively – as compared to CEF16;
2. The BOC decreases in the early years of CEP22, primarily relate to reductions in the sustainment investment category. The sustainment investment category involves investments to sustain the current and future performance capabilities of MH's generation, transmission, HVDC and distribution assets, and include expenditures for system renewal, system efficiency, mandated compliance and for decommissioning;
3. The BOC decreases in the early years of CEP22 are partially offset by increases in capacity and growth and business operations support capital expenditures. The capacity and growth investment category involve investments for the expansion of MH's generation, transmission, HVDC and distribution assets, and includes expenditures for new generation capacity, grid interconnections, increasing system load capacity and new customer connections. The business operations support investment category involves investments that are shared or common throughout the corporation and includes expenditures for fleet, corporate facilities, information technology, townsite infrastructure and tools and equipment;
4. For the **10-year period** from 2022/23 to 2031/32, BOC in CEP22 is projected to increase by $257 million, in comparison to CEF16 from the last GRA. This increase is primarily related to increased expenditures in the capacity and growth and business operations support investment categories that total $389 million, partially offset by decreases in the sustainment category of $133 million; and
5. The details by investment category for the entire **14-year common period** between CEP22 and CEF16 are not available, but on an overall basis, BOC expenditures are projected to increase by $769 million over that timeframe.

In summary, with respect to CEP22:

1. While the details are not available, It appears from the information requests that the primary reason for the 10-year and 14-year increase in BOC relative to CEF16, is the addition of placeholders for the AMI and Grid Modernization Project, that total $480 million in the first 10-years of CEP22;[80]
2. The AMI and Grid Modernization Project are simply placeholders in CEP22 as their feasibility and business cases are currently being evaluated with the assistance of external consultants, and no firm timeline or milestones for decision making have been provided by MH.[81] Both of these capital projects are closely associated with Strategy 2040 and

[79] Coalition/MH I-14 a, 78 a and II-32
[80] Coalition/MH II-139
[81] Coalition/MH I-89 c and 90 d

related strategic initiatives and are incremental and not prioritized against other BOC expenditures; and

3. While MH is concerned with respect to aging assets and the reliability of its electrical infrastructure as a top 10 enterprise risk, expenditures in the sustainment category are down $133 million in the first 10-years of CEP22. It is understood from qualitative commentary by MH, that capital expenditures for reliability have been increased in the later years of CEP22.

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

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

The projected O&A and BOC increases of $1.5 billion and $0.8 billion, respectively, since the last GRA are not consistent with or responsive to, the PUB findings and regulatory signalling from Orders 59/18, 69/19 and 9/22.

MH was unable to provide detailed O&A budgets for either the 2018/19 GRA or 2019/20 Rate Application as a result of the VDP and subsequent corporate restructuring and relied on high-lever O&A targets for rate-setting for those two regulatory proceedings.

MH did provide a full CEF for the 2018/19 GRA, as well as significant information with respect to it Asset Management initiative and provided a CEF as part of the 2019/20 Rate Application. As a result of the limited scope of the 2021/22 Interim Rate Application, only high-level information was provided with respect to O&A and BOC, and only for the short-term financial forecast period of 2021/22 and 2022/23.

The PUB made a number of consistent rate-setting findings in the successive decisions related to O&A and BOC in these three regulatory proceedings, through Orders 59/18, 69/19 and 9/22, respectively.

The key aspects of the PUB O&A and BOC findings in Order 59/18, can be summarized as follows:[82]

1. MH's review of its operations, at a time of restructuring and transition, presents an opportunity to find further areas to reduce O&A costs and it was recommended that MH

[82] PUB Order 59/18, Pages 110 to 113, 141 to 142 and 264

continue these efforts, both in terms of staff reductions and supply chain management, after the VDP concludes;

2. In a period of major capital spending, MH should find savings in BOC. The PUB did not accept the BOC spending in CEF16 for rate-setting purposes and found that BOC spending in the test year could be safely decreased by $160 million;
3. MH did not demonstrate the proposed BOC spending is necessary or has been optimized to any extent. The cost pressures from the major capital projects mean that MH can no longer continue to fund BOC at historic levels unless and until is can demonstrate through mature asset management processes that those investments are necessary; and
4. It was recommended that MH continue to find reductions in BOC spending during the period of record spending on major capital projects.

The key aspects of the PUB O&A findings in Order 69/19, can be summarized as follows:[83]

1. MH's 2019/20 O&A target is not acceptable for rate-setting purposes should be reduced from $511 million to $489 million, which was the equivalent of a 1.3% rate decrease to ratepayers and will have enduring benefits for ratepayers over time;
2. An escalation factor of 1% above the 2018/19 O&A outlook should be used for rate-setting purposes. The 1% escalation factor was consistent with MH's prior commitment dating back to 2013 to limit operating cost increases to 1% per year;
3. MH's evidence did not establish that a 2% escalation factor should be used and the PUB was concerned that the use of such an escalation factor would erode all of the O&A savings that resulted from the VDP and supply chain initiatives, within the early years Keeyask entering service; and
4. The PUB expected MH to continue its efforts to reduce O&A costs, both in terms of staff reductions and supply chain management and that cost control should be on-going and continue in the post-VDP program years.

The key aspects of the PUB O&A and BOC findings in Order 9/22, can be summarized as follows:[84]

1. The position of MH previously expressed at the NFAT proceeding has changed with respect to addressing the financial impacts of drought and MH should seek savings in its O&A expenses in order to confront liquidity concerns related to drought;
2. As major capital projects wound down and were completed, MH should have planned for the fact that the related employee salaries would move from being capitalized to expensed in O&A;

[83] PUB Order 69/19, Pages 23 to 24

[84] PUB Order 9/22, Pages 30 to 31, Pages 33 to 34

3. MH is to seek O&A savings regardless of whether the water conditions recover and the drought ends. The PUB will consider MH's steps to reduce its O&A expenses at the next GRA;
4. With respect to the concerns expressed by MH over its cash flow shortfall in 2021/22, it appears that MH missed an opportunity to preserve some cash flow early in the year by postponing or reducing its BOC spending; and
5. If drought continues, MH shall seek savings in BOC, just as it committed to do at the NFAT proceeding. The PUB will consider MH steps to reduce BOC and control costs at the next GRA. MH is to seek BOC savings regardless of whether the water conditions recover and the drought ends.

Through the above noted decisions reaching back to the last GRA five years ago, the PUB has provided sustained and consistent regulatory decisions, findings and regulatory signalling to MH with respect to the need to control O&A costs and BOC spending.

The important policy aspects of this regulatory signalling by the PUB include:

- The need to reduce O&A and BOC spending as a result of the cost and rate pressures after the in-service of the major capital projects, consistent with MH's commitment dating back to the NFAT proceeding;
- The on-going need to further reduce staffing levels and O&A costs after the VDP is completed;
- The concerns that escalation in O&A costs would erode the VDP savings and the view that these savings should be enduring well past the in-service of Keeyask;
- The view that it was MH's responsibility to be able to anticipate and plan for the fact that the in-service of the major capital projects had the potential to shift costs into O&A costs;
- The view that MH's proposed level of BOC spending had not been demonstrated to be necessary or optimized and that it was MH's responsibility to remedy this situation through the development of a mature asset management process; and
- The view that in times of financial challenges such as drought and lower cash flow, MH has the ability to control the levels of O&A and BOC.

Despite this clear and persistent regulatory signalling, MH has ignored these findings of the PUB.

As demonstrated through the following figures, which compare forecasts available now and at the last MH GRA, MH's O&A costs are forecast to be $1.5 billion and BOC expenditures are forecast to be $0.8 billion higher, than at the time of the last GRA.

Figure 13: Operating & Administrative Expenses - MH22 vs MH16 - Millions					
1	2	3	4	5	
			(2 - 3)		
			MH22 vs. MH16	Cumulative Inc (Dec)	
Year	MH22	MH16			
2023	589	536	53	**53**	
2024	657	548	109	**162**	
2025	687	559	128	**290**	
2026	683	571	112	**402**	
2027	697	583	114	**516**	
2028	711	595	116	**632**	
2029	724	607	117	**749**	
2030	736	620	116	**865**	
2031	739	633	106	**971**	
2032	754	646	108	**1079**	
2033	769	660	109	**1188**	
2034	785	674	111	**1299**	
2035	800	688	112	**1411**	
2036	816	702	114	**1525**	

Figure 14: Business Operations Capital - MH22 vs MH16 - $Millions				
1	2	3	4	5
			(2 - 3)	
			MH22 vs. MH16	Cumulative Inc (Dec)
Year	MH22	MH16		
2023	495	549	-54	**-54**
2024	538	561	-23	**-77**
2025	559	618	-59	**-136**
2026	617	643	-26	**-162**
2027	647	663	-16	**-178**
2028	722	671	51	**-127**
2029	750	697	53	**-74**
2030	788	688	100	**26**
2031	827	727	100	**126**
2032	866	734	132	**258**
2033	905	748	157	**415**
2034	919	760	159	**574**
2035	933	835	98	**672**
2036	948	852	96	**768**

Additionally, a comparison of the PUB determination of O&A for rate-setting purposes for 2019/20 of $489 million, with 1% escalation to the actual and forecast MH O&A, is provided in the following figure, and demonstrates that the MH forecast of O&A in the 2024/25 Test Year is $173 million higher than the rate-setting signaling provided by the PUB in Order 69/19:

Figure 15: O&A Exenditures vs Order 69/19 - 2020 to 2025 - $Millions						
	1	**2**	**3**	**4**	**5**	**6**
	2020	**2021**	**2022**	**2023**	**2024**	**2025**
MH Actual/Forecast	512	534	579	589	657	687
Order 69/19 plus 1% Escalation	489	494	499	504	509	514
Difference - Higher (Lower)	**23**	**40**	**80**	**85**	**148**	**173**

It is clear that the projected O&A & BOC increases of $1.5 billion and $0.8 billion, respectively, are not consistent with or responsive to PUB findings and regulatory signalling from Orders 59/18, 69/19 and 9/22.

6.10 The Projected O&A & BOC Increases of $1.5 Billion & $0.8 Billion Are Significantly Related to Strategy 2040 and Associated Initiatives and are Not Consistent With/Responsive To PUB Findings and Regulatory Signalling from Orders 59/18, 69/19 and 9/22

The conclusion of the evaluation of MH's O&A and BOC forecasts for the purposes of this proceeding, is that the $2.3 billion increase in O&A and BOC in the current financial forecast is significantly related to Strategy 2040 and associated initiatives and is inconsistent with and unresponsive to, prior PUB findings and regulatory signaling to MH to control and prioritize its controllable O&A and BOC costs.

While MH asserts that it is committed to cost control, in reality it has shifted its policy orientation away from the position at prior regulatory proceedings to pursue cost savings – and instead has developed a position that it has little influence over O&A and BOC expenditures. Successfully controlling costs requires a long-term strategic approach, but the vacancy management approach currently used by MH is not a strategy or a plan, but rather, a short-term tactical response, that does not effectively manage costs.

An evaluation of the projected increase in O&A spending compared to the last GRA and projected increases in O&A costs between 2019/20 and 2024/25 demonstrates that (i) the $175 Million or 34% increase in O&A represents an average annual growth rate of 6.1% and does not demonstrate a commitment to O&A cost control (ii) the corporate FTE increase entirely relates to the 116 FTE increase in the MH Governance & Services business units and are primarily due to Strategy 2040 and related strategic initiatives and (iii) there is a $72 million increase in the O&A costs of the MH Governance & Services business units which is primarily due to Strategy 2040

and related strategic initiatives. This includes significant expenditures on technology, without an accompanying IT Strategic plan or associated business cases.

Extrapolating these near-term O&A increased into the forecast period results in a projected cumulative increase in O&A costs of $1.5 billion compared to the last GRA.

There is a policy concern that a 15-year time frame for MH to achieve a reasonable maturity level on asset management does not demonstrate a commitment to prioritizing BOC spending and that the MH capital expenditure plan has limitations for rate setting purposes.

An evaluation of the projected $0.8 billion cumulative increase in BOC spending compared to the last GRA demonstrates that incremental expenditures of $480 million related to Strategy 2040 initiatives of AMI and Grid Modernization appear to be prioritized over sustaining capital expenditures. This is despite the fact that there are no business cases for these initiatives and MH's stated concerns with respect to aging infrastructure.

Finally, MH's forecasts of O&A and BOC spending are inconsistent with, not responsive to and essentially ignore the sustained and consistent regulatory decisions and signaling from the PUB to MH at prior regulatory proceedings in the past five years, with respect to the on-going need to control O&A costs and BOC spending after the in-service of Keeyask and the need to develop a mature asset management process to justify proposed levels of BOC spending.

7.0 MH's Revised Debt Management Strategy and Reduced Tolerances to Treasury Risks are Unnecessarily Increasing the Finance Expenses in MH22 for Rate-Setting Purposes

Under the MCOS rate-setting methodology historically used to set MH rates, judgements on the necessary and prudent levels of Finance expense to include in rates are part of the MH rate-setting process. Finance expense is forecast in the order of $900 million in the Test Years. This Section of the Evidence contains the evaluation of MH's revised Debt Management Strategy (DMS) and resulting impacts to Finance expense, for rate-setting purposes.

The conclusion from this Section of the Evidence is that MH's revised Debt Management Strategy and reduced tolerances to treasury risks are unnecessarily increasing the Finance expenses in MH22, based on the following evaluation:

1. The MH DMS and treasury risk tolerances are heavily influenced by the $23 billion level of net debt and the $1.1 billion annual projected refinancing requirements over the next decade, prompting policy changes to reduce tolerances for interest rate risk and levels of floating rate debt and future plans to maintain multiple layers of liquidity protection;
2. However, MH's own assessment is that this level of debt maturities represents a reasonable level of risk, are well within interest rate risk guidelines and do not result in high levels of debt concentration risk. As such, the emphasis placed on these treasury risks as it relates to support for the MH proposed 2% rate path, appears to be overstated;
3. MH's floating rate debt assumptions of 1.3% to 7.0% in MH22 are materially lower than updated independent analysis (8% to 15%) and peer group comparisons (6% to 16%), resulting in finance costs that are overstated, for rate setting purposes. Floating rate debt is forecast to have a lower cost than fixed rate debt by the independent consensus forecasters that MH uses to forecast interest rates in MH22; and
4. MH is planning multiple layers of liquidity protection (cash, sinking funds, short and long-term debt) and has not forecast any significant use ($50 million or 3%) of the larger $1.5 billion short term debt facility in MH22, resulting in finance costs that are overstated, for rate-setting purposes. Each of these layers of protection has an associated cost for ratepayers.

7.1 Judgements on the MH Debt Management Strategy and the Necessary and Prudent Levels of Finance Expense to Include in Rates Are Part of the MH Rate-Setting Process

Judgements on the MH Debt Management Strategy and the necessary and prudent levels of Finance Expense to include in rates are part of the MH rate-setting process.

MH's Debt Management Strategy (DMS) is important for rate-setting as Finance expense is now the largest expense in MHs revenue requirement, following the borrowing associated with the

in-service of the major capital projects. Finance expense is in the order of $900 million for the 2023/24 and 2024/25 Test Years and is relatively constant in the 20-year forecast period, despite the assumption of rising interest rates in MH22.

While financing requirements and cash flow may appear to be an outcome of the financial forecast model, based on the confluence of all of the other forecasts and assumptions with respect to revenues and expenses, the MH debt portfolio and liquidity, interest rate and foreign exchange risks are actively managed through the DMS, to balance cost and risks. As such, judgements with respect to the DMS and necessary and prudent levels of finance expense to include in rates, form an important component of the rate-setting process for MH.

7.2 The MH Revised Debt Management Strategy and Treasury Risk Tolerance is Heavily Influenced by the Levels of Net Debt from the Investment in Major Capital Projects & Refinancing Requirements Over the Next Decade

The MH revised DMS and treasury risk tolerances are heavily influenced by the $23 billion level of net debt and the $1.1 billion annual projected refinancing requirements over the next decade, prompting policy changes to reduce tolerances for interest rate risk and levels of floating rate debt and to maintain multiple layers of liquidity protection.

MH indicates that its fundamental debt management objectives are low-cost and stable funding, while maintaining risk at prudent levels and reserving sufficient flexibility to adapt to changing circumstances.

MH explains that its DMS following the era of investment in major capital projects, includes the following strategies and policies (with comparisons to the former policy[85]):

1. Maintaining floating rate debt to below 10% of the debt portfolio to minimize overall interest rate exposure (formerly 15% to 25%);
2. The revised interest rate risk policy is to limit the aggregate of (i) floating-rate debt (ii) short-term debt and (iii) fixed rate long-term debt to be refinanced in the next 12 months to a maximum of 25% of the total debt portfolio (formerly 35%);
3. The revised debt management guidelines are to (i) maintain an aggregate of short-term and floating rate debt within 0% to 20% of the total debt portfolio (formerly 15% to 25%) and (ii) having net long-term debt to be refinanced in the next 12 months being less than 10% of the debt portfolio (formerly less than 15%);
4. Continuing to smooth the debt maturity schedule by targeting debt issuance with terms to maturity of 10 to 14 years into the portion of the maturity schedule that is currently lacking debt maturities;

[85] Coalition/MH I-44 c

5. Replenishing the sinking fund reserve with internally generated funds to make annual debt retirements and eliminate refinancing risk,
6. Maintaining positive cash balances to mitigate liquidity risk and ensure financing flexibility; and
7. Use the larger $1.5 billion (up from $0.5 billion) short-term borrowing program (once fully guaranteed by the Province of Manitoba) as a tool to adjust the level of floating-rate debt.

The key risks that are managed through the DMS include:

- **Liquidity risk**: the risks that MH will not have sufficient cash to meeting financing obligations as they come due, either as a result of issues associated with the availability of internally generated cash flow or debt financing from the financial markets,
- **Interest rate risk**: risk that MH future cash flows will fluctuate due to changes in interest rates; and
- **Foreign currency exchange risk**: potential for financial gain or loss due to foreign exchange movements.

While the development of the policies, strategies and guidelines in the DMS is a complex undertaking, involving a number of policy and technical considerations, it appears that the changes in the DMS are influenced by two key concerns of MH. The first MH concern is the increase in MH's net debt to historically high levels, which are forecast to be around $23 billion at the end of 2022/23 as a result of borrowing to finance the investment in the major capital projects. The second MH concern is annual debt maturities that average around $1.1 billion that potentially require refinancing over the next decade, which are projected to be refinanced at higher rates than originally obtained in the past.

It appears that these two concerns have prompted policy changes to the DMS to reduce its tolerance for interest rate risk and levels of floating rate debt, and both replenish the sinking fund reserve and maintain positive cash balances. These concerns figure prominently in MH's justification for the MH 2% rate path proposal.

7.3 MH Assesses Debt Maturities of $1.1 Billion or 5% on an Annual Basis to be Well Within Its Interest Rate Risk Guidelines & Not Represent Concerns Over Debt Concentration Risk

Despite the concerns raised in the Application, MH's own assessment is that debt maturities per year of $1.1 billion or 5% of the total debt portfolio are a reasonable level of risk and significantly lower than the upper limit in the interest rate risk guidelines and that it does not anticipate high levels of debt concentration risk as a result of refinancing activities.

While $1.1 billion in annual expected debt maturities over the next decade can sound daunting, this level of maturities must be put in proper context.

In a debt portfolio with a 19.5 weighted average term to maturity (WATM), debt maturities in the level of approximately 5% per year is to be expected (1/19.5 = 5%). In a $23 billion debt portfolio and with a 19.5 WATM, an annual $1.1 billion of debt maturities is to be expected ($23 billion / 19.5 = $1.1 billion).

When asked in information requests, if this level of annual debt maturities was unusual or represented an elevated risk situation, MH conceded that:

"…Manitoba Hydro views debt maturities per year of approximately 5% of the total debt portfolio of $24.5 billion to be a **reasonable level of risk** and significantly lower than the 10% upper limit in Manitoba Hydro's current interest rate risk guidelines…Manitoba Hydro's average interest rate risk each year remains at the lower end of its interest rate risk guidelines".[86]

When asked in information requests, if it targets debt issuance with terms to maturity of 10 to 14 years into the portion of its maturity schedule that is currently lacking maturities, that MH would expect annual debt maturities in years 11 to 20 of the forecast to be at or near the 5% level per year, MH indicated that:

"…Manitoba Hydro does **not anticipate high levels of concentration risk** as a result of refinancing activities…The issuance of predominately Province of Manitoba 10 and 30 year benchmarks will naturally fill the void of debt maturities that exist in the years 2033-2042 and 2053-2062 and will relocate 10 years of debt refinancing into approximately 20 years of debt maturities, reducing concentration risk".[87]

The following figure, summarized from information provided by MH,[88] demonstrates the basis of its assessment that the projections in MH22 are well within its debt and interest rate guidelines as outlined in Section 7.3 of this Evidence. Over the first 10-years of the forecast period the average of floating rate debt and debt to be refinanced is 7.6% compared to the new guideline of 25% and the debt to be refinanced is 4.4% as compared to the new guideline of 10%:

[86] Coalition/MH I-45 a
[87] Coalition/MH I-45 b
[88] Coalition/MH I-44 d

Figure 16: Interest Rate Risk Profile % - MH22

1	2	3	4	5	6
			(1 + 2)		(4 + 5)
Year	Floating Rate Debt	Debt To Be Refinanced	Sub-total	New Debt	Total Interest Rate Profile
2023	1%	6%	7%	0%	7%
2024	1%	4%	5%	0%	5%
2025	2%	4%	6%	0%	6%
2026	2%	5%	7%	0%	7%
2027	2%	6%	8%	1%	9%
2028	3%	7%	10%	1%	11%
2029	4%	4%	8%	0%	8%
2030	5%	5%	10%	0%	10%
2031	6%	3%	9%	1%	10%
2032	6%	0%	6%	1%	7%
2033	6%	0%	6%	2%	8%
2034	7%	0%	7%	0%	7%
2035	7%	1%	8%	0%	8%
2036	7%	0%	7%	0%	7%
2037	6%	2%	8%	0%	8%
2038	6%	2%	8%	0%	8%
2039	6%	2%	8%	0%	8%
2040	7%	2%	9%	0%	9%
2041	7%	2%	9%	0%	9%
2042	7%	3%	10%	0%	10%
Averages:					
1 - 10 Years	**3.2%**	**4.4%**	**7.6%**	**0.4%**	**8.0%**
11-20 Years	**6.6%**	**1.4%**	**8.0%**	**0.2%**	**8.2%**
1-20 Years	**4.9%**	**2.9%**	**7.8%**	**0.3%**	**8.1%**

As noted earlier in Section 5.4 of this Evidence, with forecast total assets of $30 billion currently and $35 billion by the end of the 20-year forecast period, and assuming a 70% debt ratio, net debt in the range of $21 billion to $24 billion is to be expected and not represent an elevated level of risk, when placed in proper context.

MH is concerned that maturing debt will be projected to be refinanced at higher rates than the interest rates initially obtained for the original debt. It is noted that from a perspective of risk relative to the last GRA, that long-term fixed rate debt interest rates for 2023/24 and forward, including the Provincial Guarantee Fee (PGF), have decreased since the MH16 forecast, as follows[89]:

- MH16: 4.45% plus 1.00% PGF = 5.45%;
- MH22: 3.80% to 4.05% plus 0.50% PGF = 4.30% to 4.55%; and
- The **decrease** in **long-term fixed rates MH22 relative** to **MH16** = **0.40% to 0.65%** before PGF and **0.90% to 1.15%** including the PGF.

[89] Coalition/MH II-25 f

MH was asked to provide its views on the outlook for interest rates as compared to the pre-financial crisis period before 2008, and if the current outlook for interest rates represented a return to more normal levels of interest rates. MH indicated that outlook interest rates are lower than the pre-financial crisis period and that consensus forecasts indicate that interest rates will stay within the higher end of the range experienced in the post-financial crisis period[90].

In summary, based on MH's own assessments that debt maturities per year of $1.1 billion or 5% of the total debt portfolio are a reasonable level of risk and significantly lower than the upper limit in the interest rate risk guidelines and that it does not anticipate high levels of debt concentration risk as a result of refinancing activities, the emphasis placed on these treasury risks as it relates to support for the MH proposed 2% rate path, appear to be overstated. It appears that there is a disconnect between the concerns in the Application to justify the proposed 2% rate path and the treasury analysis provided in the information request process.

7.4 MH's Floating Rate Debt Assumptions of 1.3% to 7.0% are Materially Lower than Updated Independent Analysis and Peer Group Comparisons Resulting in Higher Finance Costs in MH22

MH's floating rate debt assumptions in MH22 (1.3% in the early years, building to 7.0% at the end of the forecast) are materially lower than updated independent analysis (8% to 15%) and peer group analysis (6% to 16%) would suggest. This results in higher Finance expense costs in MH22 than necessary, using the independent consensus forecasts that forecast floating interest rates are projected to be lower than fixed rate interest rates.

Prior to the era before the investment in the major capital projects, MH's long-standing policy was to maintain an aggregate of short-term and floating rate debt within 15% to 25% of the total debt portfolio, with a midpoint of 20%.

As a result of a directive of the PUB (Order 150/08), MH engaged National Bank Financial (NBF) to undertake an independent assessment of the appropriate level of floating rate debt for MH. The NBF report[91] was filed with the PUB in July of 2009, and the conclusion was that the optimal range of floating rate debt for MH was between 14% and 27% - which closely matched MH's long-term floating rate debt policy target range.

NBF concluded at Page 5 of its report that its analysis implied that risk could be lowered by increasing the floating rate debt mix while making positive gains in net income, since floating interest rates tend to be lower than fixed interest rates. NBF also concluded at Page 33 of its report that having a portion of floating rate debt can lead to lower overall risk levels as short-

[90] Coalition/MH II-27

[91] Coalition/MH I-44 a

term interest rates and spot export prices are positively correlated and can offset each other. There has been no subsequent independent assessment of this policy, but NBF provided MH with a working model to use for future analysis in making on-going policy assessments[92].

Recognizing the period of significant investment in major capital projects, MH's policy was adjusted to allow for aggregate floating rate debt of less that 15% of the debt portfolio during years in which there are high refinancings or new borrowings.[93] At March 21, 2022, MH actual level of floating rate debt fell to 1.5% of the total debt portfolio[94] from levels of around 19% at the time the NFB report was completed in 2007/08.

Given the broadness of the new policy range of 0% to 20% floating rate debt, MH was asked if this provides clear policy guidance and for it to provide its intent with respect to the level of floating rate debt that it intended to maintain in its capital structure, as well as the level of floating rate debt held by the Province of Manitoba.

Unfortunately, MH did not directly respond to the question on its intent with respect to floating rate debt but did indicate that the Province of Manitoba held floating rate debt of 11% at March 31, 2022[95]. MH did indicate that the assumptions in MH22 were that all new long-term debt was issued in Canadian dollars, with an 85%/15% fixed/floating split, and a 20-year term to maturity.[96]

MH did provide the assumptions on the composition of its debt structure in MH22, including the total of short-term debt, long-term floating rate debt and long-term fixed rate debt and the total floating rate debt % (including short-term debt), which is summarized in the following figure:

[92] Coalition/MH I-44 a b
[93] Coalition/MH I-44 c
[94] Coalition/MH I-44 d
[95] Coalition/MH I-44 e f g
[96] Coalition/MH I-44 h

Figure 17: MH Debt Portfolio Structure - MH22 - $Millions & Average %						
1	2	3	4	5	6	7
				(2 + 3 +4)		
Year	Short Term Debt $	Floating Rate Debt $	Fixed Rate Debt $	Total Debt $	Average Floating Rate Debt %	Average Fixed Rate Debt %
2023	50	230	24193	24473	1.3%	98.7%
2024	50	290	23114	23454	1.3%	98.7%
2025	50	410	22905	23365	1.8%	98.2%
2026	50	410	22980	23440	2.0%	98.0%
2027	50	560	22642	23252	2.4%	97.6%
2028	50	749	22570	23369	3.1%	96.9%
2029	50	989	22460	23499	3.9%	96.1%
2030	50	1079	22259	23388	4.6%	95.4%
2031	50	1409	22035	23494	5.2%	94.8%
2032	50	1479	22103	23632	6.4%	93.6%
2033	50	1508	22246	23804	6.5%	93.5%
2034	50	1569	22588	24207	6.6%	93.4%
2035	50	1569	22511	24130	6.7%	93.3%
2036	50	1569	22239	23858	6.7%	93.3%
2037	50	1449	22362	23861	6.8%	93.2%
2038	50	1479	22168	23697	6.4%	93.6%
2039	50	1509	21892	23451	6.5%	93.5%
2040	50	1539	21696	23285	6.7%	93.3%
2041	50	1539	21273	22862	6.8%	93.2%
2042	50	1569	20958	22577	7.0%	93.0%
Averages:						
1 - 10 Years	**50**	**761**	**22726**	**23537**	**3.2%**	**96.8%**
11-20 Years	**50**	**1530**	**21993**	**23573**	**6.7%**	**93.3%**
1-20 Years	**50**	**1145**	**22360**	**23555**	**4.9%**	**95.1%**

Observations with respect to Figure 17, are as follows:

1. MH has assumed **$50 million of outstanding debt** from its **short-term borrowing facility**, throughout the MH22 forecast period to 2041/42, representing about 0.2% of its debt portfolio over the forecast period;
2. In the **first 10-years** of the forecast period, MH has assumed long-term floating rate debt of between $230 million and $1.5 billion or approximately 1.1% to 6.2% of its debt portfolio. The total floating rate debt in the first 10-years ranges from 1.3% to 6.4%, with an **average of 3.2%** of the total debt portfolio;
3. In the **second 10-years** of the forecast period, MH has assumed long-term floating rate debt of around $1.5 billion and or approximately 6.3% to 6.8% of its debt portfolio. The total floating rate debt in the second 10-years ranges from 6.5% to 7.0%, with an **average of 6.7%**; and
4. Over the **20-year forecast period** of MH22, floating rate debt **averages 4.9%** and fixed rate debt averages 95.1%.

MH was also asked to provide the interest rate cost differentials between Canadian short-term debt, long-term floating rate debt and long-term fixed rate debt assumptions used in MH22. These interest rate assumptions are based on independent consensus forecasts from 11 Canadian primary financial institutions and other respected independent sources,[97] which can be summarized as follows for 2023/24 and onward in the 20-year forecast period:[98]

- Lower forecast cost of short-term debt - compared to long-term floating rate debt = **0.90%** to **1.35%**;
- Lower forecast cost of short-term debt - compared to long-term fixed rate debt = **1.10%** to **1.80%**; and
- Lower cost of long-term floating rate debt - compared long-term fixed rate debt = **0.15%** to **0.90%**.

MH also provided the sensitivity of each 1% increase in short-term debt and 1% increase in floating rate long-term debt which demonstrated a **decrease** to **finance expense** in the **$5** to **$6 million range.**[99]

MH provided an updated policy range of floating rate debt levels based on the NBF working model indicating an optimal range of 8% to 15%, updated for current data, the level of the MH debt portfolio and normal US opportunity sales volumes.[100] This updated range was provided in the second round of information requests and as such was not tested further.

MH provided an updated peer group analysis from the NBF report demonstrating a range of 6% to 16% floating rate debt, with BC Hydro at 11% and Quebec Hydro at 6% in 2021/22.[101] This compares to MH current floating rate debt levels of around 1%.

In summary, MH's current level of floating rate debt of 1.3% and the projected range in MH22 of 1.3% to 7.0% over the 20-year forecast period, are materially lower than updated independent analysis (8% to 15%) and peer group analysis (6% to 16%). MH's appetite for exposure and policy guidelines related to floating rate debt appear to be more risk adverse than necessary.

MH now has very low levels of floating-rate debt (around 1%) such that the MH22 modelling assumption of 85% fixed rate and 15% floating rate and little in the way of new debt issuances in the forecast period does not result in any significant levels of floating rate debt until later in the 20 year forecast period. The implications for rate-setting purposes are that the levels of Finance expense included in MH22 are overstated using the lower cost of floating-rate debt, provided in the independent consensus forecasts used by MH in MH22.

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[97] Application, MFR 65
[98] Coalition/MH I-44 i
[99] Coalition/MH I-44 j
[100] Coalition/MH II-25 b
[101] Coalition/MH II-25 a

It is also recommended that MH undertake an updated independent evaluation of the appropriate level of floating rate debt, as and independent review would provide valuable insights into this significant policy issue and validate the optimal range of floating rate debt for MH, based on current circumstances.

7.5 MH is Planning Multiple Layers of Liquidity Protection & Has Not Forecast Any Significant Use of the Larger $1.5 Billion Short Term Debt Facility Resulting in Higher Finance Costs in MH22

Through its DMS, MH is planning multiple layers of liquidity protection and has not forecast any significant use of the larger $1.5 billion short-term debt facility in MH22. A number of the associated financial modelling assumptions appear to unnecessarily increase the level of Finance expense included in MH22.

As noted in Section 7.2 of this Evidence, one of MH's debt management strategies is to replenish the sinking fund reserve with internally generated funds to make annual debt retirements and eliminate refinancing risk. Despite this objective, MH clarified in the information requests that MH22 assumes that sinking fund contributions and withdrawals occur on the same day and as a result there is no cost to carry these sinking fund balances in MH22.[102] The cost to carry is the difference between the cost to borrow to fund the sinking fund less the investment income received on the sinking fund assets.

MH indicates that as part of its revised DMS that it plans to maintain average unencumbered cash balances of approximately $400 to 500 million in the first decade of MH22 and approximately $200 million in the second decade of the forecast, to mitigate liquidity risk and ensure financing flexibility.[103]

However, MH22 includes cash balances that are as high as $1.2 billion in the last decade of MH22, which MH explains is as a result of a financial planning assumption. MH22 includes cash calls related to the WPLP and KHLP.[104] The following Figure summarizes the cost to carry (borrowing cost less investment income) related to the average cash balances forecast in MH22:[105]:

[102] Coalition/MH I- 46 a f
[103] Coalition/MH I-46 b
[104] Coalition/MH II-26 a
[105] Coalition/MH II-26 b

Figure 18: Cost to Carry Cash - MH22 - $Millions

1	2	3	4	5	6
				(3 - 4)	
	Average Cash Balance	Borrowing Cost	Investment Income	Cost to Carry	Cumulative Cost to Carry
Year	$	$	$	$	$
2023	933	38	30	8	8
2024	308	12	12	0	8
2025	357	14	11	3	11
2026	357	14	8	6	17
2027	188	8	4	4	21
2028	241	10	6	4	25
2029	315	13	7	6	31
2030	135	6	3	3	34
2031	210	9	5	4	38
2032	376	16	9	7	45
2033	590	25	14	11	56
2034	1085	46	25	21	77
2035	1178	50	28	22	99
2036	956	41	22	19	118
2037	926	39	22	17	135
2038	832	35	20	15	150
2039	771	33	18	15	165
2040	747	32	18	14	179
2041	625	27	15	12	191
2042	765	33	18	15	206
Averages:					
1 - 10 Years	**342**	**14**	**10**	**5**	**24**
11-20 Years	**848**	**36**	**20**	**16**	**138**
1-20 Years	**595**	**25**	**15**	**10**	**81**

It is not clear from the information requests if this level of cash for the partnership cash calls is simply a modelling assumption in MH22 or if MH would plan to actually hold this level of cash. From Figure 18, The negative cost to carry results in an average cost to carry of $10 million and a cumulative reduction in retained earnings of around $200 million by the end of the 20-year forecast period.

MH historically has had a short-term borrowing facility under the MH Act of $500 million. In April of 2020, the MH Act was amended to provide for an increase in the short-term borrowing facility to $1.5 billion. MH provided an update that it is currently in discussions with the Province of Manitoba with respect to the next steps to allow it to operationalize the increased authority, including the provincial guarantee[106].

MH outlined the benefits of the larger short-term borrowing facility to $1.5 billion, as follows:[107]

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[106] Coalition/MH I-46 c

[107] Coalition/MH I-46 d e

- Mitigate interest rate risk by providing bridge financing to avoid locking in long term rates at less than opportune times and may reduce financing costs by saving the cost to carry associated with pre-funding long-term debt;
- Mitigate liquidity risk by improving access to financial resources in the event of unanticipated cash requirements and provide bridge financing;
- Provide an additional tool to reduce net income volatility through an opportunity to potentially reduce exposure to opportunity exports price risk through short-term and floating rate debt; and
- Mitigate provincial credit risk as the increased short-term liquidity will be viewed positively by credit rating agencies.

Despite its own assessment of the benefits of the larger $1.5 billion short-term borrowing facility, MH22 only assumes that there is $50 million or 3% of this facility outstanding in each of the 20-years of the financial forecast. When questioned on this apparent disconnect in information requests, MH indicated that it will not change planned levels of short-term borrowing until the facility is fully guaranteed by the Province of Manitoba.[108] As such, it appears that the $50 million level of short-term borrowing in MH22 is another modelling assumption that was made because the increased short-term borrowing facility is not yet fully guaranteed, resulting in increased levels of Finance expense than otherwise would be the case.

There are a few implications of MH's DMS for rate-setting purposes, as it relates to sinking funds, unencumbered cash and use of the larger $1.5 billion short-term debt facility (when operationalized).

First, it appears that MH has multiple liquidity tools in place, and this will be improved in the short run when the $larger 1.5 billion short-term debt facility is operationalized. However, MH is planning to layer on sinking fund balances, on top of unencumbered cash, the short-term facility and access to long-term debt through the Province of Manitoba. This appears to be another area of where MH is overly risk adverse and the MH concerns with respect to liquidity risk and cash flow in the Application are overstated.

Second, each of these liquidity tools has a cost and there is an issue for ratepayers in terms of how many layers of liquidity protection and cost, should be prudently included in rates. It should be remembered, that even with the decrease in the PGF from 1.0% to 0.5%, MH is still projecting to pay $110 to $115 million per year for access to long-term debt through the Province of Manitoba (which is recovered through rates), a sovereign body, with a very high credit rating.[109] A number of financial modelling assumptions appear to unnecessarily increase the level of Finance expense included in MH22.

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[108] Coalition/MH II-26 c

[109] Application, MFR 62

7.6 MH's Revised Debt Management Strategy and Reduced Tolerances to Treasury Risks are Unnecessarily Increasing the Finance Expenses in MH22 for Rate-Setting Purposes

The conclusion of the evaluation of MH's DMS for the purposes of this proceeding, is that MH's revised Debt Management Strategy and reduced tolerances to treasury risks are unnecessarily increasing the Finance expenses in MH22.

The MH revised DMS and risk tolerance are heavily influenced by the $23 billion level of net debt from the investment in major capital projects and the $1.1 billion annual level of projected refinancing requirements over the next decade, prompting policy changes to reduce tolerances for interest rate risk and levels of floating rate debt and future plans to maintain multiple layers of liquidity protection.

However, MH's own assessment is that debt maturities of $1.1 billion or 5% per year represent a reasonable level of risk, are well within interest rate risk guidelines and do not result in high levels of debt concentration risk. As such, the emphasis placed on these treasury risks in the Application as it relates to support for the MH proposed 2% rate path, appears to be overstated and there appears to be a disconnect with the treasury risk analysis.

MH's floating rate debt assumptions of 1.3% to 7.0% in MH22 are materially lower than updated independent analysis (8% to 15%) and peer group comparisons (6% to 16%) and more risk adverse than necessary. This results in Finance costs that are overstated, for rate setting purposes, as floating rate debt is forecast to be lower cost than fixed rate debt by independent consensus forecasters.

MH is planning multiple layers of liquidity protection (cash, sinking funds, short and long-term debt) and has not forecast any significant use ($50 million or 3%) of the larger $1.5 billion short term debt facility in MH22. This results in Finance costs that are overstated, for rate-setting purposes, as each of these layers of protection has an associated cost for ratepayers.

The overall conclusion is that MH's revised Debt Management Strategy and reduced tolerances to treasury risks are unnecessarily increasing the Finance expenses in MH22, for rate-setting purposes.

8.0 It is Recommended that Considerations of Rate Stability & Intergenerational Equity Be Afforded the Most Weight by the PUB in Approving Regulatory Deferral Accounts for Rate Setting Purposes

Use of regulatory deferral accounts (RDA's) are an important and common feature of the rate-setting process and represent the timing differences between recognition of revenues and expenses for rate-setting purposes and financial reporting purposes. In the 2023/24 and 2024/25 Test Years, the timing differences through the Net Movement in Regulatory Deferrals are a $106 million and $77 million reduction to revenue requirements. This Section of the Evidence contains the evaluation of MH's RDA proposals, for rate-setting purposes.

The conclusion from this Section of the Evidence is that it is recommended that considerations of rate stability and intergenerational equity be afforded the most weight by the PUB in approving RDA's for rate-setting purposes, based on the following evaluation:

1. RDA's are a means to achieve the foundational and generally accepted rate-setting objectives of rate stability and predictability and intergenerational equity;
2. MH's objective to reduce the growth and reliance on RDA's should be afforded less weight by the PUB. The level of RDA's as percentage of MH total assets (currently less than 5%) would not suggest an over-reliance on RDA's by the PUB or MH;
3. In the event that a final determination on depreciation methods is not reached in this proceeding, there are pragmatic options available to the PUB, such as continuing the deferral of depreciation differences and amortizing them over a reasonable time period. The levels of RDA's would slightly increase to 6.4% of total assets under these options;
4. Given the lack of justification (no business case) with respect to the proposed SAP CCA RDA, it is recommended that the PUB leave the establishment of such an RDA to MH's decisioning making and interpretation of IFRS14, as was the case with the Keeyask In-Service RDA;
5. As the objectives of rate stability and intergenerational equity appear to be met through the Keeyask In-Service RDA, it is recommended that the PUB endorse this RDA and approve the proposed 106-year amortization period.
6. The PUB could consider increasing the Major Capital Projects (MCP) RDA to include any rate relief granted in the current Application and windfall reductions in payments to government and an amortization period of 10-years, to further aid in rate smoothing beyond the 2023/24 and 2024/25 Test Years; and
7. In the event the PUB decides not to increase the MCP RDA, it is recommended that the amortization period for the current MCP RDA be approved at 5-years, consistent with its purpose and the amortization period of the Bipole III RDA.

8.1 Regulatory Deferral Accounts are Commonly Used in Rate-Setting to Promote Rate Stability & Intergenerational Equity for Ratepayers

Use of regulatory deferral accounts (both assets/debits and liabilities/credits) are an important and somewhat unique feature of the rate-setting process. Regulatory deferral accounts (RDA) represent the timing differences between recognition of items of revenues and expenses for rate-setting purposes and the recognition of those items for financial reporting purposes.

The use of RDA's in cost of service rate-regulation is quite common and has existed for decades. RDA's are a means to achieve several foundational and generally accepted rate-setting objectives, rate stability and predictability and intergenerational equity. RDA's are used to smooth large changes in costs or revenues into rates over time and thus aid in promoting rate stability and predictability for ratepayers. RDA's are also used in situations where application of financial reporting standards requirements for rate-setting would result in a mismatch of the timing of benefits received by customers with the timing of the recognition of the costs.

The timing difference for rate-setting purposes is recognized through the Net Movement in Regulatory Deferrals line in the statement of income. Under the current presentation for IFRS14, revenues and expenses follow financial reporting standards above this line item in the MH income statement and the timing difference is incorporated through a separate line called Net Movement in Regulatory Deferrals.

Net Movement in Regulatory Deferrals includes two components: (i) the reversal of the financial reporting treatment and (ii) the amortization of the RDA as approved by the regulator for rate-setting purposes.

DSM expenditures are the easiest example of how this timing difference is accomplished. For example, in the 2024/25 Test Year, $56 million of DSM expenditures are expensed in the Other Income line item. This $56 million is then added back to income as a regulatory deferral and amortization of prior periods DSM expenditures of $49 million is taken as a reduction to income based on the PUB approved 10-year amortization period – for a net reduction of $7 million in Net Movement in Regulatory Deferrals.

The net impact for rate-setting purposes is inclusion of the $49 million (+$56 million Other Expense less $7 million Net Movement) of amortization in the allowed revenue requirement and rates. Under interim standard IFRS14, MH is allowed to recognize the RDA's for financial reporting purposes (through Net Movement in Regulatory Deferrals) and would recognise a net expense of $46 million in its financial statements. As such, there is alignment for rate-setting and financial reporting purposes, with respect to RDA's, and no need for "two sets of books" for MH.

In the 2023/24 and 2024/25 Test Years, the timing differences through the Net Movement in Regulatory Deferrals are $106 million and $77 million reduction to revenue requirements, respectively, related mostly to RDA's associated with Depreciation, Ineligible Overhead, the Bipole III revenue deferral and a new proposed RDA associated with SAP Cloud Computing Costs.

8.2 It is Recommended that Considerations of Rate Stability & Intergenerational Equity Be Afforded the Most Weight by the PUB in Approving Regulatory Deferral Accounts for Rate Setting Purposes

It is recommended that considerations of rate stability and intergenerational equity should be afforded the most weight by the PUB in approving RDA's for rate setting purposes.

MH is requesting PUB endorsement or approval of several new RDA's related to Keeyask In-Service, SAP cloud computing arrangements and Depreciation related matters. In the Application, MH outlines its three criteria for proposing the establishment of RDA's and associated amortization periods, for approval by the PUB:

1. Costs and benefits are fairly apportioned to customers in order to promote intergenerational equity and rate stability;
2. Amortization periods are established to ensure that MH recovers its costs and revenues over appropriate periods of time to promote intergenerational equity and consider stability in customer rates; and
3. Progress towards applying IFRS for both financial reporting and rate regulation purposes to reduce the growth in RDA balances and to reduce the reliance on RDA's for rate-setting purposes.

The first two criteria are reasonable and consistent with the regulatory objectives associated with RDA's and long-standing use of RDA's by the PUB and MH. The third criteria has two parts (i) progress towards applying IFRS for both financial reporting and rate-setting purposes and (ii) reducing growth and reliance on RDA's.

It is generally desirable to have a consistency between rate-setting and financial reporting as this can improve the understandability and transparency of using forecasts generated using financial reporting policies - for rate-setting purposes. However, if MH is allowed through financial reporting standards to recognize regulatory timing differences and RDA's in its financial statements, this is not a crucial requirement.

MH's analysis presented in this GRA is that it will continue to be able to recognize RDA's for financial reporting purposes both under IFRS14 and a proposed new IFRS standard based on a recent exposure draft of the IASB[110]. It is also observed that a significant alignment of rate-setting and financial reporting requirements under IFRS has been achieved, since MH transitioned to IFRS in 2015/16.

The criteria to reduce growth and reliance on RDA's is more questionable. For the 2024/25 forecast, MH is projecting net RDA's of $1.405 billion ($1.503 billion debits less $98 million credits) on a total asset base of $30.038 billion. As such, RDA's represent about 4.7% of MH's

[110] Coalition/MH I-37 a b c and II-20 a b

projected total assets. Put in the proper context, this would not suggest an over-reliance on RDA's by the PUB or MH.

When MH was challenged in information requests, with respect to the apparent contradiction of reducing RDA's and its proposals to the PUB to endorse or establish several new and material RDA's in this Application, MH clarified that its proposals result from balancing its three criteria.[111]

It is agreed that rate-setting requires a significant degree of balancing of principles, criteria and interests of various parties. However, with respect to the three MH criteria for RDA's, it is appropriate that the first two criteria receive the most weighting by the PUB, considering the purpose of this GRA is for setting rates and ensuring rate stability and intergenerational equity for ratepayers.

8.3 There are Pragmatic Options Available to the PUB on Depreciation Related Regulatory Deferral Accounts in the Event a Final Decision on Depreciation Methods Is Not Reached

In the event that a final determination on depreciation methods and depreciation RDA's in not reached in this proceeding, the PUB has pragmatic options available to it that balance the various viewpoints of MH and interest parties to the hearing.

Perhaps the most complex issue in this GRA as it relates to RDA's is MH's proposals with respect to the Depreciation related RDA's, which are summarized as follows:

1. Approval to use ELG as the depreciation methodology for rate-setting purposes;
2. Approval of a new RDA to transition to ELG effective September 1, 2023 (phasing out the difference between ELG and ASL depreciation over 15 years) and amortization of this new RDA over 30 years commencing October 1, 2023;
3. Approval to cease additions to the Change in Depreciation Method and Losses on Disposal of Assets RDAs, effective September 1, 2023;
4. Approval for the establishment of an amortization period for the Change in Depreciation Method RDA (30 years for MH, 42 years for WPLP and 62 years for KHLP), commencing October 1, 2023; and
5. Approval for the establishment of an amortization period for the Losses on Disposal of Assets RDA (26 years for MH, 27 years for WPLP and 58 years for KHLP), commencing October 1, 2023.

The issues surrounding the appropriate depreciation methodology for rate-setting purposes has a long history before the PUB, going back 10 years or more as MH was preparing for the transition to IFRS for financial reporting purposes. This history is well known to the PUB, MH and other

[111] Coalition/MH I-38 c

intervenors and will not be repeated here. Independent experts engaged by other intervenors to this proceeding are leading the evaluation of the appropriate depreciation methodology for rate-setting purposes. The scope of this Evidence is limited to the consideration of options related to Depreciation related RDA's.

The complexity and the level of disagreement between MH and intervenors with respect to ELG and ASL depreciation methodologies are such, that there is a possibility that the PUB may not be able to make a definitive decision on this matter in this proceeding.

MH has expressed significant concerns that without an amortization period for the Depreciation related RDAs it will not be able to recover these costs in rates, the deferral balance will grow significantly and there may be external audit issues with respect to continue recognition of the RDA as an asset.

In recognition of the possibility that a definitive decision is not reached, a number of pragmatic alternative scenarios were canvassed in the information request process to provide options and comparisons for the PUB for rate-setting purposes. The options include:[112]

1. A status quo option, where MH would be directed by the PUB to continue to defer amounts into the Change in Depreciation Method and Losses on Disposal of Assets RDA's, without any amortization (as was directed in Order 59/18);
2. An option with the continued deferral of amounts but with amortization over the amortization periods proposed by MH (MH, WPLP and KHLP) as noted above;
3. An option with the continued deferral of amounts but with amortization over the average remaining service life of MH's assets of 49 years; and
4. An option assuming approval of all MH depreciation proposals, as noted above and contained in MH22.

The interplay of all of the variables associated with these options (various amounts of deferrals, amortization and resulting RDA balances for four options) is difficult to compare and keep track of, so a comparison of net income impacts and resulting balances of the RDA's is used to simplify the analysis.

Figure 19 provides a comparison of Option #4 (MH12) where all of MH's proposals are approved by the PUB and the Status Quo Option (Option #1). This essentially provides the outer bounds of the impacts on net income of the options and MH's proposals:

[112] Coalition/MH I-41 c d e f

Figure 19: Net Income Depreciation Options - $Millions

1	2	3	4	5
			(2 - 3)	
Year	Net Income MH22	Net Income Status Quo	Net Income Difference	Cumulative Net Income Difference
2023	751	751	0	**0**
2024	469	471	-2	**-2**
2025	295	306	-11	**-13**
2026	149	169	-20	**-33**
2027	166	193	-27	**-60**
2028	97	132	-35	**-95**
2029	92	136	-44	**-139**
2030	111	162	-51	**-190**
2031	105	164	-59	**-249**
2032	169	237	-68	**-317**
2033	190	265	-75	**-392**
2034	219	301	-82	**-474**
2035	277	367	-90	**-564**
2036	250	347	-97	**-661**
2037	282	387	-105	**-766**
2038	309	419	-110	**-876**
2039	358	470	-112	**-988**
2040	439	554	-115	**-1103**
2041	507	624	-117	**-1220**
2042	569	686	-117	**-1337**
Averages:				
1 - 10 Years	240	272	-32	**-110**
11-20 Years	340	442	-102	**-838**
1-20 Years	290	357	-67	**-474**

Figure 20 provides a comparison of Option #2 (continued deferral with amortization based on MH amortization proposals) with Option #4 (MH22), which is essentially an option between the two extremes of MH22 (including MH's Depreciation RDA proposals) and the status quo scenario:

Figure 20: Net Income Depreciation Options - $Millions

1	2	3	4	5
			(2 - 3)	
Year	Net Income MH Amortization Periods	Net Income Status Quo	Net Income Difference	Cumulative Net Income Difference
2023	751	751	0	**0**
2024	462	471	-9	**-9**
2025	289	306	-17	**-26**
2026	151	169	-18	**-44**
2027	173	193	-20	**-64**
2028	111	132	-21	**-85**
2029	112	136	-24	**-109**
2030	137	162	-25	**-134**
2031	137	164	-27	**-161**
2032	207	237	-30	**-191**
2033	235	265	-30	**-221**
2034	268	301	-33	**-254**
2035	331	367	-36	**-290**
2036	309	347	-38	**-328**
2037	346	387	-41	**-369**
2038	376	419	-43	**-412**
2039	426	470	-44	**-456**
2040	506	554	-48	**-504**
2041	574	624	-50	**-554**
2042	634	686	-52	**-606**
Averages:				
1 - 10 Years	253	272	-19	**-82**
11-20 Years	401	442	-42	**-399**
1-20 Years	327	357	-30	**-241**

Observations with respect to Figures 19 and 20, are as follows:

1. The impact of MH's Depreciation related proposals (MH22) relative to the status quo is to decrease MH's projected cumulative net income by $317 million in the 10-year period to 2031/22 and by $1.3 billion in the 20-year period to 2041/42;
2. The impact of Option #2 (continued deferral and amortization over MH proposed amortization periods) relative to the status quo is to decrease MH's projected cumulative net income by $191 million in the 10-year period to 2031/22 and by $606 million in the 20-year period to 2041/42;
3. Option #2 would reduce the cumulative net income impact of MH's proposals by $126 million in the first 10-years and $730 million in the 20-year period; and
4. It is noted that Option #3 (continued deferral with amortization of 49 years), has net income impacts that are reasonably similar to Option #2.

In addition, the following Figure provides a comparison of the level of the Depreciation related RDA's[113] and their relationship with respect to the size of MH's total asset base, for years 10 and 20 of the forecast (comparing MH22, Option #2 and the Status Quo Options):

Figure 21: Regulatory Deferral Account (RDA) Balances - $Millions & % of Total Assets - 2032 & 2042

	1	2	3	4	5	6
	MH22 2032 Forecast	MH Amortization Periods 2032 Forecast	Status Quo 2032 Forecast	MH22 2042 Forecast	MH Amortization Periods 2042 Forecast	Status Quo 2042 Forecast
DSM Programs RDA	396	396	396	550	550	550
Conawapa & Keeyask RDAs	298	298	298	162	162	162
Ineligible Overhead RDA	270	270	270	335	335	335
Other RDAs	169	169	169	18	18	18
Sub-Total	1133	1133	1133	1065	1065	1065
Depreciation Related RDAs	**665**	**793**	**988**	**434**	**1194**	**1830**
Total RDAs	**1798**	**1926**	**2121**	**1499**	**2259**	**2895**
Total Assets	**31419**	**31419**	**31419**	**35422**	**35422**	**35422**
% of Total Assets:						
Depreciation Related RDAs	**2.1%**	**2.5%**	**3.1%**	**1.2%**	**3.4%**	**5.2%**
Total RDAs	**5.7%**	**6.1%**	**6.8%**	**4.2%**	**6.4%**	**8.2%**

Observations with respect to Figure 21, are as follows:

1. Under **Option #1 (Status Quo)**, Depreciation related RDA's would represent 3.1% of total assets in Year 10 and 5.2% of total assets in Year 20 of the forecast, and total RDA's would represent 6.8% of total assets in Year 10 and 8.2% of total assets in Year 20 of the forecast;
2. Under **Option #2** (continued deferral with MH proposed amortization periods), Depreciation related RDA's would represent 2.5% of total assets in Year 10 and 3.4% of total assets in Year 20 of the forecast, and total RDA's would represent 6.1% of total assets in Year 10 and 6.4% of total assets in Year 20 of the forecast; and
3. Under **Option #4 (MH proposals)**, Depreciation related RDA's would represent 2.1% of total assets in Year 10 and 1.2% of total assets in Year 20 of the forecast, and total RDA's would represent 5.7% of total assets in Year 10 and 4.2% of total assets in Year 20 of the forecast.

[113] Coalition/MH I-32 a and I-41 d

In summary, in the event that a final determination on depreciation methods and depreciation RDA's in not reached in this proceeding, the PUB has pragmatic options available to it that balance the various viewpoints of MH and interest parties to the hearing.

An option of continuing the deferral of depreciation differences and amortizing them over MH's proposed amortization periods (or the remaining average service life of MH's assets), would allow for amortization of these RDA's, while managing the total level of RDA's to within a reasonable proportion of MH's total assets (Total RDA's of around 6.4% of total assets by year 20 of the forecast).

8.4 It is Recommended that the Establishment of an SAP Regulatory Deferral Account be Left to MH's Interpretation of IFRS14 Until Justification for the Associated Expenditures Has Been Developed

Considering the lack of justification on the record with respect to the proposed SAP RDA, it is recommended that the PUB leave the establishment of such an RDA to MH's decisioning making, based on its interpretation of IFRS14. MH can make application to the PUB for endorsement and an approved amortization period, once its business case associated with SAP has been developed or alternatively at the next GRA.

MH is requesting PUB approval of the establishment of the SAP S/4HANA Cloud Computing Arrangements (SAP CCA) RDA to defer costs over a seven-year period between 2023/24 and 2029/30 and an amortization period of 10 years subsequent to the actual in-service dates. It is assumed in MH22 that the amortization will commence in 2030/31.[114]

MH asserts that its current version of SAP will not be supported beyond 2027. MH is requesting the SAP CCA RDA to smooth the impact of a significant one-time investment in an SAP CCA, which is projected to be $156 million, into rates.

MH has reviewed the accounting treatment for CCA's and concluded that they must now be expensed through O&A, compared to the prior treatment to capitalize in-house IT systems as BOC. The MH proposed amortization period of 10 years is based on the estimated service life of SAP S/4HANA. MH asserts that this amortization period promotes fairness to customers by matching expense recognition with the period of benefit to customers.

MH indicates that while utilities have generally lagged broader industry in adopting cloud-based services, the shift is now well underway. MH also asserts that Strategy 2040 and its information technology plan are inseparable, with information technology debt being a major constraint for progress on Strategy 2040 pillars and initiatives.

[114] Coalition/MH I-40 b

However, in information requests, MH was forced to concede that it does not have yet have a Digital & Technology strategic plan that is reviewed and approved by the MHEB, as this plan is still under development.[115] As such, further details on its Digital and IT initiatives are not available at this time and for this GRA.

Despite requesting PUB approval of the SAP CCA RDA and an amortization period of 10-years, MH appears to be in the early stages of its review of its options and justification of the associated expenditures.

MH is in what it describes as Phase 0 (pre-planning) and when requested in the information request process was unable to provide the business case for this investment or provide any information with respect to alternatives being evaluated, risks and NPV of the alternatives. MH simply stated that it has engaged a consultant to assist with the business case for this platform. MH asserts that it will also evaluate extended support options for its current version of SAP that are available from third party providers. The final decision with respect to SAP S/4HANA will not be made until after the completion of the business case and readiness assessment[116].

MH is also forecasting $13 million in 2023/24 and $9 million in 2024/25 and forward related to CCA's for the implementation of small software systems, which will be expensed as incurred. MH indicates that the average service life of these systems is six years and since the costs are regular and recurring, it is not proposing to defer these costs in an RDA. MH also confirmed that it was in the planning phase for these small software systems and that business cases have not yet been prepared to justify the expenditures.

The following Figure provides a summary of the net income impacts related to SAP CCA and small systems CCA costs, and MH's SAP CCA RDA proposal[117]. Figure 22 demonstrates that all but $1 million of the SAP CCA costs (column 7) are deferred until amortization is projected to begin in 2030/31 and that the total CCA costs (column 8) recognized in revenue requirement from 2023/24 to 2029/30 are in the $10 million to $14 million range. From 2030/31 to 2039/40, the total CCA costs (column 8) in revenue requirement increase to $34 million, including the on-going costs of SAP and small software systems and the $16 million amortization related to the SAP CCA RDA.

[115] Coalition/MH I-75 (updated)
[116] Coalition/MH I-76 a, PUB/MH II-11 a and GSS-GSM/MH I-6 e f g
[117] Coalition/MH I-40 d

Figure 22: Net Income Impact CCA Deferrals - $Millions							
1	2	3	4	5	6	7	8
			(2 + 3)			(2 - 5 + 6)	(4 - 5 + 6)
Year	Total SAP CCA Costs	Small System CCA Costs	Total CCA Costs	Defferal SAP CCA Costs	Amortization SAP CCA Costs	SAP CCA Net Income Impact	Total CCA Net Income Impact
2023	0	5	5	0	0	0	5
2024	14	13	27	13	0	1	14
2025	24	9	33	23	0	1	10
2026	25	9	34	24	0	1	10
2027	25	9	34	24	0	1	10
2028	26	9	35	25	0	1	10
2029	26	9	35	25	0	1	10
2030	24	9	33	23	0	1	10
2031	9	9	18	0	16	25	34
2032	9	9	18	0	16	25	34
2033	9	9	18	0	16	25	34
2034	9	9	18	0	16	25	34
2035	9	9	18	0	16	25	34
2036	9	9	18	0	16	25	34
2037	9	9	18	0	16	25	34
2038	9	9	18	0	16	25	34
2039	9	9	18	0	16	25	34
2040	9	9	18	0	16	25	34
2041	9	9	18	0	0	9	18
2042	9	9	18	0	0	9	18
Averages:							
1 - 10 Years	18	9	27	16	3	6	15
11-20 Years	9	9	18	0	13	22	31
1-20 Years	14	9	23	8	8	14	23

While this uneven cost profile does not appear to be consistent with rate smoothing, it does recognize that the assumption that SAP S/4HANNA system is not expected to be in-service until 2029/30. As such, deferring and amortizing these costs are consistent with intergenerational equity and matching of costs and benefits for customers. It also supports MH's position that the small systems CCA costs should not be deferred and amortized.

However, the fact that MH is in the initial pre-planning phase with respect to SAP S/4HANNA, with no business case, is problematic from a rate-setting perspective. MH is forecasting significant expenditures in the near-term Test Years but does not have appropriate information to justify the prudence of these expenditures to the PUB for inclusion in revenue requirements and rates.

MH is in effect requesting the PUB to approve the expenditures into rates, and approve an RDA and associated amortization period, based on a planning assumption, before these expenditures are formally approved by MH's senior management and the MHEB. The state of MH's planning related to SAP S/4HANA would not meet an acceptable regulatory test for approval of an RDA and amortization period, and such approval by the PUB would be premature based upon the information on the record of this proceeding.

MH was able to establish RDA's on transition to IFRS and an RDA for Keeyask In-Service costs under IFRS14, without prior PUB endorsement on the basis of an expectation of approval by the PUB.[118] In the case of the IFRS transitional RDA's, PUB endorsement and approval of amortization periods occurred at the 2018/19 GRA, through Order 59/18. MH is requesting endorsement and approval of an amortization period for the Keeyask In-Service RDA in this proceeding.

MH has noted a concern that failure of the PUB to approve an SAP CCA RDA may lead to sub-optimal decision making on its part of a less desirable option as a result of the regulatory or financial reporting treatment. This circular reasoning and this argument should not be accepted by the PUB as justification for establishing an SAP CCA RDA. It is the responsibility of MH to ensure that appropriate information and justification is developed and available, before bringing RDA proposals to the PUB for approval. MH is also responsible to make prudent investment and business decisions, regardless of the regulatory or financial reporting treatment of costs.

On balance and considering the lack of justification on the record with respect to the proposed SAP CCA RDA, it is recommended that the PUB leave the establishment of such an RDA to MH's own decisioning making. If MH decides that the SAP CCA RDA meets the criteria of IFRS14 based on past precedent of the endorsement of RDA's by the PUB, then once the appropriate business cases are available, it has the options of either (i) filing a separate application with the PUB requesting endorsement of the establishment and an appropriate amortization period or (ii) waiting until its next scheduled GRA to make such an application.

8.5 It is Recommended that the PUB Endorse the Keeyask In-Service Deferral Account & Approve the Proposed 106-Year Amortization Period

The PUB should endorse the Keeyask In-Service RDA and approve the proposed 106-year amortization period, considering they are consistent with the regulatory objectives of rate stability and intergenerational equity.

MH is requesting PUB endorsement of the Keeyask In-Service RDA and approval of an amortization period of 106 years, effective September 1, 2023. MH indicates that the 106-year amortization period represents the weighted average service life of the Keeyask assets.

The Keeyask In-Service RDA was established by MH without prior approval of the PUB, based on its interpretation of IFRS14 and an expectation of approval by the PUB. This RDA arises as a result of the different accounting treatment between IFRS and CGAAP with respect to the in-service of multi-unit generating stations that come into service over a period of years.

[118] Coalition/MH I-39 a

Under CGAAP, the carrying costs (depreciation and finance expense) of the total value of all the generating assets were recognized into income (and revenue requirements) on a per unit of output basis (for example for Keeyask 1/7 as each of the 7 units coming into service).

Under IFRS, the assets are placed in service when they first become used and useful, significantly increasing the asset (powerhouse, dams, spillway etc.) carrying costs that are recognized into income when the 1st unit of Keeyask went into service.

The Keeyask In-Service RDA currently has a balance of $104 million. This RDA is a debit balance, and as such its amortization would increase the revenue requirements and rate increases to customers. The proposed long amortization period results in a relatively immaterial amount of $1 million of amortization per year over the MH22 forecast period.

MH was also requested to consider the merits of writing off the balance in the Keeyask In-Service RDA in 2022/23 and respond by indicating that such a write-off would negatively impact the debt ratio by increasing it 0.5%[119].

Considering the objectives of rate stability and intergenerational equity appear to be met through the Keeyask In-Service RDA and that a write-off of this RDA against the expected record net income in 2022/23 would not materially impact the revenue requirements (and rates) on a go-forward basis – it is recommended that the PUB endorse this RDA and approve the proposed 106-year amortization period.

8.6 Absent Other Options It is Recommended that the PUB Approve a Five-Year Amortization Period for the Major Capital Projects Deferral Account Consistent with Its Purpose of Rate Smoothing

Absent other options, it is recommended that the PUB approve a 5-year amortization period for the Major Capital Projects (MCP) RDA, consistent with its purpose to smooth in the rate impacts of the major capital projects and consistent with the amortization of the Bipole III RDA, which had a similar purpose.

In the Application, MH is requesting the approval of a two-year amortization period (2025/26 and 2026/27), effective April 1, 2025, with respect to the MCP RDA, with the reasoning that this amortization period is consistent with the period over which the revenue was collected[120]. The MCP RDA currently has a balance of $98 million. This RDA is a credit balance, and as such its amortization would reduce the revenue requirements and rate increases to customers. MH is proposing an amortization credit of $49 million over each of the two years.

[119] PUB/MH I-33 a
[120] Coalition/MH I-42 c

In the information requests, it was confirmed by MH that the purpose of the MCP RDA was to smooth in the revenue requirement impacts of the Keeyask generating station and other major capital projects, which was consistent with the purpose of the Bipole III RDA, for which the PUB approved a 5-year amortization period.[121] Amortizing the MCP RDA over 5-years would result in amortization credit of $20 million per year.

The following Figure summarizes the impact on MH's projected net income[122] if the MCP RDA was amortized over a 5-year period consistent with the Bipole III RDA. Figure 23 demonstrates that a 5-year amortization period would smooth out MH's net income from 2025/26 to 2029/30, decreasing net income by $30 million in 2025/26 and 2026/27 and increasing net income by $20 million from 2027/28 to 2029/30.

Figure 23: Major Capital Deferral Options - $Millions

1	2	3	4 (2 - 3)	5
Year	Net Income MH22	Net Income 5 Year Amortization	Net Income Difference	Cumulative Net Income Difference
2023	751	751	0	0
2024	469	469	0	0
2025	295	295	0	0
2026	149	119	**30**	**30**
2027	166	136	**30**	**60**
2028	97	117	**-20**	**40**
2029	92	112	**-20**	**20**
2030	111	131	**-20**	**0**
2031	105	105	0	0
2032	169	169	0	0
2033	190	190	0	0
2034	219	219	0	0
2035	277	277	0	0
2036	250	250	0	0
2037	282	282	0	0
2038	309	309	0	0
2039	358	358	0	0
2040	439	439	0	0
2041	507	507	0	0
2042	569	569	0	0
Averages:				
1 - 10 Years	240	240	0	15
11-20 Years	340	340	0	0
1-20 Years	290	290	0	8

There maybe other options with respect to the use of the MCP RDA to smooth in rate impacts of the major capital projects (explored in Section 8.7 below). In the event the PUB does not want to pursue these options, it is recommended that the amortization period for the current MCP

[121] Coalition/MH I-42 a b
[122] Coalition/MH I-42 d

RDA be approved by the PUB at 5-years, consistent with its purpose and the amortization period of the Bipole III RDA.

8.7 The PUB Could Consider Increasing the Major Capital Projects Deferral Account for Any Rate Relief Granted & Windfall Reductions in Payments to Government to Further Aid Rate Smoothing Beyond the Test Years

The PUB could consider increasing the MCP RDA to include any rate relief granted in the current Application and windfall reductions in payments to government (guarantee fees & water rentals) in the order of $180 million per year, to further aid in rate smoothing beyond the 2023/24 and 2024/25 Test Years.

It is observed that the $98 million amount in the MCP RDA is not an overly significant amount with respect to its stated purpose of smoothing in rate increases of the major capital projects. Accordingly, other options for the use of the MCP RDA to smooth out future revenue requirements were explored in the information request process, recognizing:

- The record levels of export revenues and net income projected for 2022/23;
- The windfall reductions in the payments to government in the order of $180 million per year; and
- MH's concerns with respect to the lower levels of net income in the first 10-years of the forecast period.

These other options included:[123]

1. **MCP RDA Scenario #1**: deferring the $98 million requested rate increases in 2023/24 and 2024/25 and 50% of the reductions in the payments to government from 2022/23 to 2024/25 into the MCP RDA – and amortizing the resulting total balance ($369 million) over the 10-year period from 2025/26 to 2034/35; and
2. **MCP RDA Scenario #2**: deferring the $98 million requested rate increases in 2023/24 and 2024/25 and 100% of the reductions in the payments to government from 2022/23 to 2024/25 into the MCP RDA – and amortizing the resulting total balance ($641 million) over the 10-year period from 2025/26 to 2034/35.

The following Figure provides a comparison of net income in MH22 to the MCP RDA Scenario #1 and Scenario #2, as described above. Figure 24 demonstrates that the larger balances of the MCP RDA under these two scenarios would serve to smooth out MH's net income in the 10-year period after the Test Years, and from 2027/28 to 20234/35, would increase net income levels in excess of $30 million under Scenario #1 and in excess of $60 million under Scenario #2.

[123] Coalition/MH I-42 f g

Figure 24: Major Capital Deferral - Additional Options - $Millions					
1	2	3	4	5	6
				(2 - 3)	(2 - 4)
Year	Net Income MH22	Net Income 50% Deferral	Net Income 100% Deferral	Net Income 50% vs MH22 Difference	Net Income 100% vs MH22 Difference
2023	751	659	567	**92**	**184**
2024	469	380	291	**89**	**178**
2025	295	207	119	**88**	**176**
2026	149	139	167	**10**	**-18**
2027	166	155	183	**11**	**-17**
2028	97	135	164	**-38**	**-67**
2029	92	130	158	**-38**	**-66**
2030	111	149	177	**-38**	**-66**
2031	105	143	170	**-38**	**-65**
2032	169	209	236	**-40**	**-67**
2033	190	229	256	**-39**	**-66**
2034	219	257	285	**-38**	**-66**
2035	277	314	341	**-37**	**-64**
2036	250	250	251	**0**	**-1**
2037	282	283	283	**-1**	**-1**
2038	309	310	310	**-1**	**-1**
2039	358	359	360	**-1**	**-2**
2040	439	440	441	**-1**	**-2**
2041	507	508	508	**-1**	**-1**
2042	569	572	572	**-3**	**-3**
Averages:					
1 - 10 Years	240	231	223	**10**	**17**
11-20 Years	340	352	361	**-12**	**-21**
1-20 Years	290	291	292	**-1**	**-2**

In summary, the above analysis demonstrates that the PUB could consider increasing the MCP RDA to include any rate relief granted in the current Application and windfall reductions in payments to government in the order of $180 million per year, and consider a longer amortization period of 10-years, to further aid in rate smoothing beyond the 2023/24 and 2024/25 Test Years.

8.8 It is Recommended that Considerations of Rate Stability & Intergenerational Equity Be Afforded the Most Weight by the PUB in Approving Regulatory Deferral Accounts for Rate Setting Purposes

The conclusion of the evaluation of MH's RDA proposals for the purposes of this proceeding, is that it is recommended that considerations of rate stability and intergenerational equity be afforded the most weight by the PUB in approving RDA's for rate-setting purposes.

MH's objective to reduce the growth and reliance on RDA's should be afforded less weight, as an analysis of the level of RDA's as percentage of MH total assets (currently less than 5%) would not suggest an over-reliance on RDA's by the PUB or MH.

In the event that a final determination on depreciation methods and depreciation RDA's in not reached in this proceeding, the PUB has pragmatic options available to it that balance the various viewpoints of MH and interest parties to the hearing. These options include continuing the deferral of depreciation differences and amortizing them over MH's proposed amortization periods or the remaining average service life of MH's assets (RDA's would slightly increase to 6.4% of total assets under these options).

Considering the objectives of rate stability and intergenerational equity appear to be met through the Keeyask In-Service RDA, it is recommended that the PUB endorse this RDA and approve the proposed 106-year amortization period.

As a result of the lack of justification (no business case) on the record with respect to the proposed SAP CCA RDA, it is recommended that the PUB leave the establishment of such a RDA to MH's decisioning making and interpretation of IFRS14, as was the case with the Keeyask In-Service RDA.

The PUB could consider increasing the MCP RDA to include any rate relief granted in the current Application and windfall reductions in payments to government and consider a longer amortization period of 10-years, to further aid in rate smoothing beyond the 2023/24 and 2024/25 Test Years. In the event the PUB decides not to pursue this option, it is recommended that the amortization period for the current MCP RDA be approved at 5-years, consistent with its purpose and the amortization period of the Bipole III RDA.

9.0 It is Recommended that the PUB Approve a Single Overall Rate Increase of 1.3% Effective April 1, 2024 & Confirm the 3.6% Interim Rate Increase that Was Effective January 1, 2022 as Final

The PUB describes its rate-setting mandate as setting electricity rates for MH customers that balance two concerns (i) the interests of MH ratepayers and (ii) the financial health of MH. The net present value of the three rate increases to customers that MH is seeking final approval in this Application is approximately $2.8 billion in perpetuity and as such is important to the finances of ratepayers and the economy of Manitoba.

This Section of the Evidence provides recommendations to the PUB with respect to MH's rate increase proposals, considering the six conclusions and recommendations from Sections 3.0 to 8.0 of this Evidence and an analysis of financial information on the record of the proceeding from three distinct analytical perspectives.

The conclusion from this Section of the Evidence is that it is recommended that the PUB approve a single overall rate increase of 1.3% effective April 1, 2024 and confirm the 3.6% rate increase that was effective January 1, 2022, as final, based on the following evaluation:

1. The results from **analytical perspective #1 (Test Year Only Analysis)** is that there is no Justification for 2% Rate Increases in 2023/24 & 2024/25 Test Years themselves, based on traditional rate-setting metrics, as these metrics are all above long-standing targets or showing progress towards the attainment of longer-term targets;
2. The results from **analytical perspective #2 (20 Year Rate Smoothing Analysis)** is that a single 1.2% to 1.5% rate increase on April 1, 2024 and similar indicative annual rate increases in the forecast period, together with active cost containment on the part of MH - represent a more appropriate balancing of the interests of customers with the financial health of MH. This range of rate increases is most consistent with MH's status as a GBE with a Provincial debt guarantee and the preliminary nature of significant expenditures on Strategy 2040 and related initiatives. This range is more aligned with prior policy directives and regulatory signalling from the PUB with respect to risks, appropriate financial metrics and need for cost containment and considerations of public acceptance of rate increases in a year when MH expects to post a record level of net income;
3. The results from **analytical perspective #3 (Longer Term Intergenerational Equity Analysis)** is that there is potential for a mid-term course correction in the form of a rate pause for current customers in the forward Test Years (2023/24 and 2024/25) for a more even distribution of funding the costs of the major capital projects. This analysis points to the potential intergenerational inequity between ratepayer over the last 12 years who have paid average annul rate increases of 3% and ratepayers for the next 19 years that are projected to pay average annual rate increases of 2% or less; and
4. These analytical perspectives provide a **continuum of between 0% and 1.5% rate increases** as a recommendation to the PUB to more appropriately balance the interests

of ratepayers with the financial health of MH. Providing some weight to each of the three perspectives but the most weight to the PUB's policy of rate smoothing, results in a recommendation of a single 1.3% overall rate increase on April 1, 2024 and final confirmation of the 3.6% interim rate increase that was effective January 1, 2022. This recommendation considers more active cost containment on the part of MH.

9.1 The PUB's Mandate is to Balance the Interest of Ratepayers & the Financial Health of MH for Rate Increases with an NPV of $2.8 Billion

The PUB describes its rate-setting mandate as setting electricity rates for MH customers that are just and reasonable and in doing so, it must balance two concerns (i) the interests of MH ratepayers and (ii) the financial health of MH[124].

As described in Sections 3.0 to 8.0 of this Evidence, under the MCOS rate-setting methodology, balancing the interests of ratepayers with MH's financial health involves judgement and considerations of risks and financial targets, prudence of MH's cost control (particularly of the three largest cost categories of finance expense, O&A and depreciation & amortization expense), rate stability and predictability for customers and intergeneration equity.

Rate-setting decisions inherently build on the decisions and regulatory policies that have been determined in prior proceedings and consider the current economic environment as context for the setting of rates.

The rate increases that are approved by the PUB do not only generate additional revenues in the Test Year(s) or the 20-year forecast period, but rather form part of MH revenues in perpetuity. There is also a compounding effect of each subsequent rate increase.

The MH rate increase proposals of a 2% rate increase on September 1, 2023 and a 2% rate increase represent a cumulative rate increase of 4.04% or approximately $74 million on an annualized basis. The net present value (NPV) of these two rate increases to customers in perpetuity is approximately $1.5 billion,[125] assuming a social discount rate of 5%.

The rate increases that are proposed to be confirmed or awarded for the four test years under review in this Application (2021/22, 2022/23, 2023/24 and 2024/25) represent a cumulative rate increase of 7.79%[126] or approximately $139 million on an annualized basis. The NPV of these three rate increases to customers in perpetuity is approximately $2.8 billion,[127] assuming a social discount rate of 5%.

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[124] PUB Order 59/18, Section 1.0, Page 4
[125] $74 million / .05 = $1.480 billion
[126] Coalition/MH I-9 b
[127] $139 million / .05 = $2.780 billion

While the additional revenues sought in the rate application are important to MH's maintaining MH's financial health over time, they are also important to the finances of ratepayers and the economy of Manitoba, over time.

9.2 Recommendations on MH Rate Proposals are Based on Conclusions in Sections 3.0 to 8.0 & Three Analytical Perspectives on the Financial Information in this Proceeding

The recommendation on MH's rate proposals are based on the conclusions reached in Sections 3.0 to 8.0 of this Evidence and three analytical perspectives on the financial information in this proceeding.

Sections 3.0 to 8.0 of this Evidence provide observations, conclusions and recommendations related to the PUB's balancing of the interests and assessment of the prudency of MH's expense estimates for rate-setting purposes. These conclusions can be summarized as follows:

1. There are too many concerns and unknowns for the PUB to fully accept strategy 2040 for rate-setting purposes at this time (Section 3.0);
2. A relative assessment of risks since the last GRA does not support the MH assessment of elevated business and financial risks for rate-setting purposes (Section 4.0);
3. It is recommended that the PUB's policy determinations from Orders 59/18 and 69/19 and traditional financial targets and metric be provided primary weight for rate-setting purposes (Section 5.0);
4. The $2.3 billion increase in O&A and BOC in the current financial forecast is significantly related to Strategy 2040 and associated initiatives and is inconsistent with and unresponsive to, prior PUB findings and regulatory signaling to MH to control and prioritize its controllable costs (Section 6.0);
5. MH's revised Debt Management Strategy and reduced tolerance to treasury risks are unnecessarily increasing the finance expenses in MH22 (Section 7.0); and
6. It is recommended that considerations of rate stability and intergenerational equity be afforded the most weight by the PUB in approving RDA's for rate-setting purposes (Section 8.0).

In order to provide recommendations to the PUB with respect to MH's rate increase proposals, these six conclusions and the financial information on the record of the proceeding are examined from three distinct analytical perspectives:

1. The forecast financial metrics in the 2023/24 and 2024/25 Test Years (Test Year Only Analysis);
2. Rate-smoothing in the 20-year financial forecast period to 2041/42 (20 Year Rate Smoothing Analysis); and

3. Longer-term intergenerational equity considerations for the 30-year period between 2011/12 and 2041/42 (Longer Term Intergenerational Equity Analysis).

9.3 Analytical Perspective #1: There is No Justification for 2% Proposed Rate Increases in 2023/24 & 2024/25 Based on Traditional Rate-Setting Metrics Solely in the Test Years Themselves

The first analytical perspective evaluates if there is sufficient justification for the two 2% rate increases based on the forecast financial metrics in the 2023/24 and 2024/25 Test Years themselves. The conclusion is that there is no justification for the 2% proposed rate increases based on traditional rate-setting metrics solely in the Test Year themselves.

Figure 25 summarizes the traditional financial metrics used for rate-setting in the Test Years:

Figure 25: Test Year Key Financial Metrics MH22 - $Millions				
	1	2	3	4
	2022 Actual	2023 Forecast	2024 Forecast	2025 Forecast
Net Income:				
Net Income - with rate increases	-249	751	469	295
Less: 2% Rate Increases			-24	-74
Net Income - without rate increases	**-249**	**751**	**445**	**221**
Cumulative - with rate increases	-249	502	971	1266
Cumulative - without rate increases	**-249**	**502**	**947**	**1168**
Other Financial Metrics:				
Net Debt - with increases	23293	22963	22529	22341
Net Debt - without increases	**23293**	**22963**	**22552**	**22442**
Retained Earnings - with increases	2825	3575	4044	4339
Retained Earnings - without increase	**2825**	**3575**	**4021**	**4238**
Equity Ratio - with increases	13%	15%	17%	18%
Equity Ratio - without increases	**13%**	**15%**	**17%**	**18%**
EBITDA Interest Coverage - with	1.31	2.48	2.21	2.06
EBITDA Interest Coverage - without	**1.31**	**2.48**	**2.18**	**1.98**
Capital Coverage Ratio - with	0.56	2.26	2.23	1.61
Capital Coverage Ratio - without	**0.56**	**2.26**	**2.18**	**1.48**

Observations with respect to Figure 25, are as follows:

1. After a net loss of $249 million in 2021/22 due to drought, MH's expected financial results for 2022/23 have rebounded significantly as a result of improved water conditions and

high export prices, to result in a forecast record net income for MH of $751 million in 2022/23;

2. In absence of the further rate increases in the forward Test Years, MH forecast net income for the 2023/24 and 2024/25 are $445 and $221, respectively, an average of $333 million. This is well above net income levels in the prior 5 to 10 years.
3. For the four test years that are the subject of this Application (2021/22 to 2024/25), net income without any further rate increases is projected to be $1.168 billion, or an average of $292 million per year, which is a healthy level of net income for MH;
4. In the absence of further rate increases, retained earnings are forecast to grow from $3.1 billion (2020/21) to $4.2 billion and net debt reduce from $22.6 billion (2020/21) to $22.4 billion, over the forecast of these four test years;
5. In the absence of further rate increases, the Equity ratio is expected to recover from 14% (2020/21) to 18%. While this is lower than the lost-standing MH target of 25%, it is a significant improvement from the prior long-term forecast that demonstrated a persistent stickiness at the 12% to 13% level until 2029/30; and
6. In the absence of further rate increases, the EBITDA Interest Coverage Ratio is forecast in the Test Years to range from 1.98 to 2.18 and the Capital Coverage Ratio is forecast to range from 1.48 to 2.18, well above the long-standing MH targets of 1.80 and 1.20, respectively.

In summary, the traditional rate-setting metrics in the 2023/24 and 2024/25 Test Years are all above long-standing targets or showing progress towards the attainment of longer-term targets, without any further rate increases.

The conclusion from this analysis is that there is no justification for 2% rate increases in 2023/24 and 2024/25, based upon traditional rate setting metrics used by the PUB to guide its judgements with respect to rate increases, solely in the Test Years themselves.

9.4 Analytical Perspective #2: A 1.2% to 1.5% Rate Path Commencing in 2024/25 is Indicated Using Traditional Rate-Setting Metrics & Rate Smoothing Over the 20-Year Financial Forecast Period

The second analytical perspective evaluates if there is sufficient justification for the two 2% rate increases in the 2023/24 and 2024/25 Test Years, considering rate smoothing over the full 20-year forecast period. The conclusion is that a 1.2% to 1.5% rate path commencing on April 1, 2024 - combined with cost containment on the part of MH - represents a more appropriate balancing of the impacts on customers and the financial health of MH.

Rate Smoothing Evaluation Framework

The evaluation of rate smoothing over the full 20-year forecast period, is based on the following considerations:

1. The implications of the six conclusions from Sections 3.0 to 8.0 of this Evidence;
2. The traditional rate setting metrics that have been used by the PUB to make judgements with respect to rate increases; and
3. Alternate rate scenarios requested through the Consumers Coalition information requests that are used to examine various balancing points of the level of rate increases to customers with the financial health of MH and assuming cost containment on the part of MH.

As part of the process of evaluating alternatives to the MH proposed 2% rate path, 11 alternative rate scenarios were requested through the Consumers Coalition information requests.[128] These alternate rate scenarios are referred to as CC1 through CC11 for shorthand in this Evidence and for the Figures in this Section of the Evidence.

MH was requested in information requests to explain why it was requesting two rate increases that were less than 12 months apart (September 1 2023 and April 1, 2024 are only 7 months apart), and how this approach balanced rate impacts on customers with the financial health of MH, considering the current economic environment. MH's response was essentially process oriented, considering the timing of preparation of the GRA and potential decision by the PUB on September 1, 2023 and an objective to implement subsequent rate increases on the beginning of the fiscal year of April 1st.[129]

No consideration was provided by MH with respect to rate stability and predictability for customers, and the difficulties many customers face with decades high rates of inflation and rising interest rates.

One of the generally accepted ratemaking principles is the practical-related attribute of public acceptability. Under this ratemaking principle, rates should be well understood, logical and straightforward and free as possible from controversy.[130]

The fact that MH did not consider this rate making principle or attribute in the formation of its rate increase proposals is concerning. With the expectation of a record net income of $751 million for 2022/23 that would likely be released to the general public in August of 2023, there is an issue of public acceptability of a proposed rate increase to be implemented by the PUB

[128] Coalition/MH I-43 a to h and II-24 a b c
[129] Coalition/MH I-9 a
[130] Bonbright Second Edition, Page 384

commencing on September 1, 2023, essentially concurrent with the public release of these record financial results.

In addition, the imposition of two rate increases within a 12-month period is not consistent with prior PUB policy. In Order 59/16, the PUB directed that to minimize the impact on ratepayers, that it was not appropriate to increase rates two times within a 12-month period.[131]

As a result of these concerns and the prior policy of the PUB, the Consumers Coalition Alternate Rate Scenarios, focused on rate smoothing scenarios with a single rate increase for April 1, 2024, followed by consistent annual rate increases on April 1 of the subsequent 20-year forecast period. These alternate rate scenarios also included considerations of cost containment by MH.

One of the deficiencies of a goal seeking approach to evaluating rate paths over a 20-year forecast period to reach a defined debt to equity ratio, is that the smoothed even annual rate increase is relatively in-sensitive to changes in MH's underlying cost structure. Perhaps somewhat counter-intuitive to what one might assume in rate-setting, 20-year goal seeking provides less weight to short-term to mid-term financial projections and more weight to the back end of the financial projections. Another concern with respect to 20-year goal seeking is that by the back end of the forecast period, net income levels are excessive and debt to equity ratios, which are normally quite sticky and normally improve slowly, tend to be improving in large increments (2% or more) with each passing year.

As a result, some degree of judgement and trial and iteration is required to properly consider alternative rate scenarios and analyze the changes in the various traditional rate setting metrics.

In particular, Consumers Coalition Alternative Rate Scenarios #10 and #11 (CC10 and CC11 for shorthand) with even annual rate increases of between 1.2% and 1.5% commencing in 2024/25 and continuing on to 2041/42, appeared as reasonable alternate rate scenarios to the MH 2% rate path goal seek in MH22. CC10 and CC11 also included cost containment by MH. As such, the evaluation below focuses on comparing and analyzing CC10 (1.2%) and CC11 (1.5%) – versus MH22 (2.0%).

Incorporation of Conclusions in Sections 3.0 to 8.0 into Rate Smoothing Evaluation

In addition to alternate rate path assumptions, the Consumers Coalition Alterative Rate Scenarios also were designed to incorporate the analysis summarized in Sections 3.0 to 8.0 of this Evidence. This is accomplished through specifying alternate assumptions with respect to prudency of costs and cost control, debt management strategies, regulatory deferral account treatment and consistency of financial targets, for rate-setting purposes.

[131] PUB Order 59/16, Page 4

The alternate assumptions for CC10 and CC11 and their consistency with the conclusions in Sections 3.0 to 8.0 of this Evidence, are as follows:

1. O&A costs were held to 2% increases in each year after the 2022/23 forecast and BOC spending forecasts were reduced by 10% for each year. These assumptions were in recognition of (i) the concerns, lack of focus and unknowns related to Strategy 2040 and associated cost increases (Section 3.0) and (ii) the concerns that MH's revised budgets are inconsistent with and unresponsive to prior PUB findings and regulatory signalling with respect to cost control (Section 6.0);
2. Floating rate debt levels of 5% in the first 10-years and 10% in the second 10-year of the forecast period were specified. These assumptions were in recognition of the concerns that MH's revised Debt Management Strategy and reduced tolerance to treasury risks are unnecessarily increasing Finance expenses (Section 7.0);
3. Depreciation related deferral accounts continued the deferral of amounts as previously directed by the PUB, but with amortization over amortization periods proposed by MH. This assumption was in recognition of a pragmatic approach of dealing with the disagreement related to depreciation matters and primary weighting to rate stability and intergeneration equity (Section 8.0); and
4. Rate increase assumptions for 2024/25 to 2041/42, were set on a consistent basis each year (not a goal seek) and the Capital Coverage Ratio was based on its historic presentation for consistency for rate-setting purposes. These assumptions were in recognition that the PUB has ruled that the new legislative framework is not in place for this proceeding, that the primary weight should be placed on traditional rate-setting metrics as defined for rate-setting purposes and a balanced risk assessment does not demonstrate an elevated level of risk (Sections 4.0 and 5.0).

CC10 and CC11 also assumed that the 3.6% interim rate increase that was approved by the PUB for 2021/22 is confirmed as final. Hindsight with respect to the record profit levels in 2022/23 would indicate that when looking at the combined financial results of 2021/22 and 2022/23, that the 3.6% increase was not required to mitigate the deleterious impacts of drought in 2021/22. However, for the purposes of a rate smoothing evaluation, it appeared counter intuitive to roll-back the 3.6% interim rate increase – only to then to reimpose higher rate smoothing increases in future years.

The approach used in the rate smoothing evaluation is somewhat analogous to the basis that the PUB used to approve a 3.6% rate increase in the 2018/19 GRA, using the financial scenario in MH Exhibit #93 from that proceeding as directionally reflective of many of its decisions on major topic areas in Order 59/18.[132] As mentioned previously, the MCOS is a judgemental rate-setting

[132] PUB Order 59/18, Section 13.3, Page 173

methodology that does not result in the PUB making detailed determinations of approvals of costs and disallowance of costs but rather overall levels of costs.

The analysis that follows generally compares the outcomes of CC10 and CC11 and MH22 (and MH16) and the consistency of these outcomes with traditional rate-setting metrics and prior policy decisions of the PUB and considers appropriately balancing rate impacts on customers with the financial health of MH.

O&A and BOC Comparisons – CC10 & CC11 vs MH22 & MH16

As noted above, the O&A costs in CC10 and CC11 were based on 2022/23 O&A costs forecast by MH and escalated at 2% for the rest of the forecast period and BOC spending in CC10 and C11 was based on a 10% reduction from the levels in CEP22, from 2023/24 on-ward to the end of the forecast period.

The following Figure provides a comparison of O&A costs in CC10 and CC11 to MH22 (and MH16 from the 2018/19 GRA):

Figure 26: O&A Expenses - CC10 & CC11 vs MH22 & MH16 -$Millions

1	2	3	4
Year	CC10/ CC11	MH22	MH16
2023	589	589	536
2024	601	657	548
2025	613	687	559
2026	625	683	571
2027	638	697	583
2028	650	711	595
2029	663	724	607
2030	677	736	620
2031	690	739	633
2032	704	754	646
2033	718	769	660
2034	732	785	674
2035	747	800	688
2036	762	816	702
2037	777	833	NA
2038	793	849	NA
2039	809	872	NA
2040	825	896	NA
2041	841	914	NA
2042	858	939	NA
Averages:			
1 - 10 Years	**645**	**698**	**590**
11-20 Years	**786**	**847**	NA
1-20 Years	**716**	**773**	NA

Observations from Figure 26, are as follows:

1. CC10 and CC11 used the 2022/23 O&A costs of $589 million as a base, despite the fact that that PUB found in Order 69/19 that the appropriate O&A target for 2019/20 was $489 million and the appropriate escalation factor for rate-setting purposes is 1% per year. Using the parameters from Order 69/19 would have resulted in an O&A target of $504 million for 2020/23. As a result, O&A costs in 2022/23 are $85 million or 16.9% higher than prior PUB direction from Order 69/19;
2. The O&A assumptions in CC10 and CC11, results in O&A costs that are on average $53 million lower in the first decade of the forecast period, $61 million lower in the second decade of the forecast and $57 million lower over the 20-Year period, as compared to MH22 averages; and
3. The O&A assumptions in CC10 and CC11, results in O&A costs that are on average $55 million higher in the first decade of the forecast period that MH16, for which a comparable number of years of data is available.

In summary, the O&A assumptions in CC10 and CC11 are in the middle of the range between the substantial O&A cost increases forecast in MH22 and the O&A costs in MH16 from the 2018/19 GRA, where the PUB found that there were opportunities for further FTE and cost reductions. As such, the O&A assumptions in CC10 and CC11 are generous and provide ample room for cost escalation and accounting changes up above the judgement of the PUB at the last MH GRA related to O&A levels in rates, but not to the extreme levels forecast by MH in MH22.

In addition, as noted in Sections 6.4 and 6.5 of this Evidence, there are potential overstatements of pension and benefit costs in the range of $37 million to $74 million, as a result of understated discount rates in MH22 and MH's FTE forecasts are under forecast by 89 to February of 2023. This further adds to the cushion in CC10 and CC11 to provide ample room for cost escalation and accounting changes, while still respecting the prior directives of the PUB with respect to O&A costs.

The following Figure provides a comparison of BOC spending in CC10 and CC11 to MH22 (and MH16 from the 2018/19 GRA):

Figure 27: BOC Spending - CC10 & CC11 vs MH22 & MH16 - $Millions			
1	2	3	4
Year	CC10/ CC11	MH22	MH16
2023	495	495	549
2024	484	538	561
2025	503	559	618
2026	555	617	643
2027	582	647	663
2028	650	722	671
2029	675	750	697
2030	710	788	688
2031	744	827	727
2032	779	866	734
2033	814	905	748
2034	827	919	760
2035	840	933	835
2036	853	948	852
2037	867	963	NA
2038	881	979	NA
2039	895	994	NA
2040	909	1010	NA
2041	924	1027	NA
2042	939	1043	NA
Averages:			
1 - 10 Years	**618**	**681**	**655**
11-20 Years	**875**	**972**	NA
1-20 Years	**746**	**827**	NA

Observations from Figure 27, are as follows:

1. BOC spending assumptions in CC10 and CC11 are on average $63 million lower in the first decade of the forecast period, $97 million lower in the second decade of the forecast period and $81 million lower over the 20-Year forecast period, as compared to MH22; and
2. BOC spending assumptions in CC10 and CC11 are on average $37 million lower than MH16 for the first decade of the forecast period, for which a comparable number of years of data is available.

In summary, the BOC assumptions in CC10 and CC11 are consistent with the PUB findings in Orders 59/18, that MH find reductions in BOC spending from those included in MH16 (CEF16).

Traditional Rate Setting Financial Metric Comparisons – CC10 & CC11 vs MH22 & MH16

In this part of the rate smoothing analysis, comparisons are made between (i) CC10 and CC11 which use judgement and cost containment (O&A, BOC and finance expense) to analyze a balanced rate path and (ii) MH22 and MH16, which are essentially mechanical goal seeking exercises to force a debt to equity ratio outcome towards the end of the 20-year forecast period.

In the Figures below, the traditional rate-setting metrics of net income, retained earnings, net debt, Equity ratio, EBITDA interest coverage ratio and capital coverage ratio are all analyzed to judgementally assess a balance rate path. The summary observations for each of these six financial metrics, are provided in the paragraphs below the relevant Figure.

Figure 28: Net Income & Retained Earnings - CC10 & CC11 vs MH22 & MH16 - $Millions

1	2	3	4	5	6	7	8	9	10
		Net Income:					Retained Earnings:		
Year	CC10	CC11	MH22	MH16		CC10	CC11	MH22	MH16
2023	751	751	751	-29		3575	3575	3575	3311
2024	498	498	469	-111		4073	4073	4044	3200
2025	322	328	295	-69		4395	4401	4339	3132
2026	159	170	149	-128		4554	4571	4488	3003
2027	170	187	166	-68		4724	4758	4654	2935
2028	93	117	97	-13		4817	4875	4751	2922
2029	79	111	92	81		4897	4986	4843	3002
2030	86	125	111	190		4983	5111	4953	3192
2031	57	106	105	261		5040	5217	5058	3453
2032	107	167	169	398		5147	5385	5227	3851
2033	111	182	190	512		5258	5567	5417	4363
2034	122	205	219	641		5380	5772	5635	5004
2035	158	253	277	793		5539	6024	5912	5798
2036	105	213	250	883		5644	6237	6162	6680
2037	106	230	282	NA		5750	6467	6444	NA
2038	97	238	309	NA		5848	6705	6753	NA
2039	106	268	358	NA		5953	6973	7112	NA
2040	145	326	439	NA		6098	7299	7551	NA
2041	157	363	507	NA		6255	7663	8058	NA
2042	166	396	569	NA		6421	8059	8628	NA
Averages:					Change:				
1 - 10 Years	232	256	240	51	1 - 10 Years	1572	1810	1652	540
11-20 Years	127	267	340	NA	11-20 Years	1274	2674	3401	NA
1-20 Years	180	262	290	NA	1-20 Years	2846	4484	5053	NA

Metric #1 = Net income (Figure 28):

- **First decade of forecast**: net income per year averages between $232 million in CC10 and $256 million in CC11 - as compared to $240 million in MH22 and $51 million in MH16;
- **Second decade of forecast**: net income per year averages between $127 million in CC10 and $267 million in CC11 - as compared to $340 million in MH22; and

- **Over the 20-year forecast**: net income per year averages between $180 million in CC10 and $262 million in CC11 - as compared to $290 million in MH22.

Metric #2 = Retained Earnings (Figure 28):

- **First decade of forecast**: retained earnings increase between $1.6 billion in CC10 and $1.8 billion in CC11 - as compared to $1.6 billion in MH22 and $540 million in MH16;
- **Second decade of forecast**: retained earning increase between $1.3 billion in CC10 and $1.7 billion in CC11 - as compared to $3.4 billion in MH22; and
- **Over the 20-year forecast**: retained earnings increase between $2.8 billion in CC10 and $4.5 billion in CC11 - as compared to $5.0 billion in MH22.

Figure 29: Net Debt & Equity Ratio - CC10 & CC11 vs MH22 & MH16 - $Millions & %

1	2	3	4	5	6	7	8	9	10
		Net Debt:					Equity Ratio:		
Year	CC10	CC11	MH22	MH16		CC10	CC11	MH22	MH16
2023	22963	22963	22963	24666		15%	15%	15%	13%
2024	22440	22440	22529	24702		17%	17%	17%	13%
2025	22168	22164	22341	24765		18%	18%	18%	12%
2026	22134	22118	22371	24891		19%	19%	18%	12%
2027	22031	21998	22322	24963		19%	**20%**	19%	12%
2028	22019	21963	22356	24971		**20%**	20%	19%	12%
2029	22037	21948	22401	24899		20%	21%	**20%**	12%
2030	22070	21943	22451	24713		21%	21%	20%	13%
2031	22102	21928	22471	24476		21%	21%	21%	14%
2032	22086	21850	22424	24091		21%	22%	21%	15%
2033	22085	21776	22372	23592		22%	23%	22%	17%
2034	22060	21668	22270	22950		22%	24%	23%	19%
2035	21986	21499	22090	22221		23%	**25%**	24%	22%
2036	22063	21469	22030	**21403**		24%	26%	**25%**	**25%**
2037	22271	21555	22063	NA		**25%**	27%	27%	NA
2038	22407	21552	21983	NA		25%	28%	28%	NA
2039	22479	21459	21798	NA		25%	29%	29%	NA
2040	22642	21440	21656	NA		26%	**30%**	**30%**	NA
2041	22700	21292	21355	NA		27%	31%	32%	NA
2042	**22686**	**21051**	**20930**	NA		**27%**	**32%**	**34%**	NA
Change:					Change:				
1 - 10 Years	-877	-1113	-539	-575	1 - 10 Years	6%	7%	6%	2%
11-20 Years	600	-799	-1494	NA	11-20 Years	6%	10%	13%	NA
1-20 Years	-277	-1912	-2033	NA	1-20 Years	12%	17%	19%	NA

Metric #3 = Net Debt (Figure 29):

- **First decade of forecast**: net debt decreases between $877 million in CC10 and $1.1 billion in CC11 - as compared to $539 million in MH22 and $575 million in MH16;
- **Second decade of forecast**: net debt increases of $600 million in CC10 and decreases of $799 million in CC11 - as compared to a decrease of $1.5 billion in MH22; and
- **Over the 20-year forecast**: net debt decreases between $277 million in CC10 and $1.9 billion in CC11 - as compared to $2.0 billion in MH22.

Metric #4 = Equity Ratio (Figure 29):

- **First decade of forecast**: equity ratio increases between 6% in CC10 and 7% in CC11 - as compared to 6% in MH22 and 2% in MH16;
- **Second decade of forecast**: equity ratio increases between 6% in CC10 and 10% in CC11 - as compared to 13% in MH22;
- **Over the 20-year forecast**: equity ratio increases between 12% in CC10 and 17% in CC11 - as compared to 19% in MH22; and
- **The historic equity ratio target of 25%** is met in CC10 in 2037 and in CC11 in 2035 – as compared to 2036 in both MH22 and MH16;
- While not operative until April 1, 2025 – **the 80% debt ratio target** (or 20% equity ratio) is met in both CC10 and CC11 in 2028 (7 years ahead of target date) – as compared to 2029 in MH22 (6 years ahead of target date); and
- While not operative until April 1, 2025 – **the 70% debt ratio target** (or 30% equity ratio) is not met in CC10 and met in CC11 in 2040 (on the target date) – as compared to 2040 in MH22 (on the target date); and
- The forecast **equity ratios at the end of the 20-year forecast period**, are 27% in CC10 to 32% in CC11 – as compared to 34% in MH22.

Figure 30: EBITDA Interest Coverage & Capital Coverage Ratios - CC10 & CC11 vs MH22 & MH16

1	2	3	4	5	6	7	8	9	10
		EBITDA Interest Coverage Ratio:					Capital Coverage Ratio:		
Year	**CC10**	**CC11**	**MH22**	**MH16**		**CC10**	**CC11**	**MH22**	**MH16**
2023	2.48	2.48	2.48	**1.58**		2.50	2.50	2.26	1.33
2024	2.25	2.25	2.21	**1.52**		2.79	2.79	2.23	1.27
2025	2.11	2.11	2.06	**1.57**		2.10	2.10	1.61	1.24
2026	1.94	1.95	1.92	**1.53**		1.57	1.59	1.20	1.12
2027	1.96	1.97	1.95	**1.58**		1.56	1.59	1.21	1.20
2028	1.88	1.91	1.89	**1.63**		1.37	1.41	**1.08**	1.29
2029	1.88	1.91	1.90	**1.72**		1.32	1.37	**1.06**	1.39
2030	1.90	1.94	1.95	1.82		1.28	1.34	**1.06**	1.57
2031	1.91	1.96	1.99	1.87		1.24	1.30	**1.08**	1.61
2032	2.01	2.09	2.12	2.01		1.29	1.36	**1.16**	1.81
2033	2.04	2.13	2.17	2.11		1.27	1.36	**1.16**	1.95
2034	2.07	2.18	2.24	2.25		1.29	1.39	1.21	2.12
2035	2.14	2.26	2.33	2.42		1.35	1.46	1.29	2.12
2036	2.12	2.27	2.36	2.56		1.29	1.42	1.27	2.21
2037	2.15	2.32	2.44	NA		1.31	1.45	1.32	NA
2038	2.18	2.37	2.53	NA		1.32	1.47	1.37	NA
2039	2.23	2.46	2.64	NA		1.35	1.53	1.43	NA
2040	2.30	2.57	2.79	NA		1.41	1.61	1.52	NA
2041	2.34	2.66	2.92	NA		1.42	1.64	1.59	NA
2042	2.39	2.76	3.07	NA		1.45	1.70	1.66	NA
Averages:					**Averages:**				
1 - 10 Years	**2.03**	**2.06**	**2.05**	**1.68**	**1 - 10 Years**	**1.70**	**1.74**	**1.40**	**1.38**
11-20 Years	**2.20**	**2.40**	**2.55**	NA	**11-20 Years**	**1.35**	**1.50**	**1.38**	NA
1-20 Years	**2.11**	**2.23**	**2.30**	NA	**1-20 Years**	**1.52**	**1.62**	**1.39**	NA

Metric #5 = EBITDA Interest Coverage Ratio (Figure 30):

- **First decade of forecast**: EBITDA interest coverage ratio averages between 2.03 in CC10 and 2.06 in CC11 - as compared to 2.05 in MH22 and 1.68 in MH16;
- **Second decade of forecast**: EBITDA interest coverage ratio averages between 2.20 in CC10 and 2.40 in CC11 - as compared to 2.55 in MH22;
- **Over the 20-year forecast**: EBITDA interest coverage ratio averages between 2.11 in CC10 and 2.23 in CC11 - as compared to 2.30 in MH22; and
- **The historic EBITDA interest coverage ratio target of 1.80** is significantly exceeded in all forecasts, other than MH16 where it was below target from 2022/23 to 2028/29.

Metric #6 = Capital Coverage Ratio (Figure 30):

- **First decade of forecast**: capital coverage ratio averages between 1.70 in CC10 and 1.74 in CC11 - as compared to 1.40 in MH22 and 1.38 in MH16;
- **Second decade of forecast**: capital coverage ratio averages between 1.35 in CC10 and 1.50 in CC11 - as compared to 1.38 in MH22;
- **Over the 20-year forecast**: interest coverage ratio averages between 1.52 in CC10 and 1.62 in CC11 - as compared to 1.39 in MH22; and
- **The historic capital coverage ratio target of 1.20** is exceeded in all forecasts, other than MH22 where it is below average from 2027/28 to 2022/33. The reason for lower capital coverage ratio in MH22 is two-fold (i) higher BOC spending levels and (ii) the restatement of the ratio by MH for financial reporting purposes.

From an overall perspective, the above noted observations result in the following additional **general observations**:

1. In the first decade of the forecast, the lower rate increases in CC10 and CC11 (1.2% to 1.5% as compared to 2% in MH22), are more than offset by lower spending (cost containment) in O&A, BOC and Finance expense. As a result, the financial metrics in CC10 and CC11 are generally equivalent to or better than MH22;
2. As is the case with MH22 (and MH16) and goal seeking to obtain equity ratio targets towards the end of the forecast period – the lower spending (cost containment) in CC10 and CC11 is overtaken by the cumulative rate increases in MH22 in the second decade of the forecast period to meet the goal seek. As a result, the financial metrics in CC10 and CC11 in the second decade are generally poorer than MH22;
3. However, the stronger financial metrics in MH22 towards the end of the forecast period tend to exceed reasonable targets of a GBE with a Provincial debt guarantee, with the Equity ratio in particular approaching the range of an IOU, that borrows debt on a stand-alone basis and without a Provincial guarantee (Equity ratio of 34% and EBITDA interest coverage of over 3.00 by the end of the forecast period);

4. CC10 and CC11 financial metrics are more in-line with reasonable financial targets for a GBE with a Provincial debt guarantee and reflect stronger cost control that is expected of a regulated utility (as well as consistency with prior PUB findings on the need for cost control); and
5. CC10 produces an equity ratio of 27%, an EBITDA interest coverage of 2.39 and a capital coverage of 1.45, by the end of the forecast period. CC11 produces an equity ratio of 32% an EBITDA interest coverage of 2.76 and a capital coverage of 1.70, by the end of the forecast period. All of these financial ratios are above the long-standing targets used by the PUB for rate-setting purposes; and
6. CC10 is most congruent with the traditional financial metric targets used by the PUB to set MH rates. CC11 exceeds these targets but is more balanced than MH22.

In summary, the conclusion from the rate smoothing analysis, is that a single 1.2% to 1.5% rate increase on April 1, 2024 and similar indicative annual rate increases in the forecast period represent – combined with cost control on the part of MH - represent a more appropriate balancing of the interests of customers with the financial health of MH.

This range of rate increases is most consistent with MH's status as a GBE with a Provincial debt guarantee and the preliminary nature of significant expenditures on Strategy 2040 and related initiatives. This range is more aligned with prior policy directives and regulatory signalling from the PUB with respect to risks, appropriate financial metrics and need for cost containment and considerations of public acceptance of rate increases in a year when MH expects to post a record level of net income.

Rate Smoothing Scenarios - Cumulative Rate Impacts – CC10 & CC11 vs MH22

Figure 31 below provides the cumulative rate increases associated with CC10 and CC11 as compared to MH22:

Figure 31: Cumulative Rate Increases - CC10 & CC11 vs MH22 - %				
1	2	3	4	
Year	CC10	CC11	MH22	
2023	0.00%	0.00%	0.00%	
2024	0.00%	0.00%	2.00%	
2025	1.21%	1.50%	4.04%	
2026	2.43%	3.02%	6.12%	
2027	3.67%	4.57%	8.24%	
2028	4.93%	6.14%	10.41%	
2029	6.20%	7.73%	12.62%	
2030	7.48%	9.34%	14.87%	
2031	8.78%	10.98%	17.17%	
2032	10.10%	12.65%	19.51%	
2033	11.43%	14.34%	21.90%	
2034	12.78%	16.05%	24.34%	
2035	14.15%	17.79%	26.82%	
2036	15.53%	19.56%	29.36%	
2037	16.92%	21.36%	31.95%	
2038	18.34%	23.18%	34.59%	
2039	19.77%	25.02%	37.28%	
2040	21.22%	26.90%	40.02%	
2041	22.69%	28.80%	42.82%	
2042	24.17%	30.73%	45.68%	
Change:				
1 - 10 Years	10.10%	12.65%	19.51%	
11-20 Years	14.07%	18.08%	26.17%	
1-20 Years	24.17%	30.73%	45.68%	

The differences between the cumulative rate impacts to customers associated with CC10 and CC11, as compared to MH22, can be summarized as follows:

1. In the **first decade of the forecast period**, cumulative rates increases range between 10.1% for CC10 and 12.7% for CC11 – as compared to 19.5% for MH22. This represents a decrease of between 6.8% and 9.4% over that period of time; and
2. By the **end of the 20-year forecast period**, cumulative rates increases range between 24.2% for CC10 and 30.7% for CC11 – as compared to 45.7% for MH22. This represents a decrease of between 15.0% and 21.5% over that period of time.

In summary, a more balanced rate smoothing scenario represents significant rate relief for ratepayers of between 15% and 22% over the 20-year forecast period.

9.5 Analytical Perspective #3: Consideration of Longer -Term Intergenerational Equity Over 30-years Would Suggest a Mid-Term Rate Pause for Current Customers

There is a plethora of discussion in the MH Application and record of this proceeding with respect to multi-year journeys associated with strategy and enterprise planning. However, the most important journey for rate setting purposes - is the multi-decade (30-year) journey of customers

to pay for rate increases to first cover the carrying costs of the major capital projects and secondly, recovery of MH's financial metrics after the in-service of these projects.

For the last decade or more, MH has proposed and the PUB has approved significant rate increases (42% cumulative from 2011/12 to 2021/22) in excess of inflation not only to cover cost increases in past test years, but also to smooth in rate increases that were anticipated as a result of the in-service of a number of major capital projects[133].

As a result of the cumulative rate increases in the last 12 years of 42%, revenues at existing rates are now sufficient to cover the carrying costs of the major capital projects and MH's other costs forecasts and produce a net income for MH.

MH is now proposing a 2% rate path in the next 19-year period forecast to result in another cumulative rate increase of 46%, to not only recover its financial metrics, but also pay-down net debt and attain an Equity ratio of 34% and other financial metrics well in excess of historic targets.

One of the key ratemaking principles is that of intergenerational equity or the principle that customers should pay for the cost incurred to provide them service and not for the costs to provide service to customers in another period.

The third analytical perspective evaluates longer-term intergenerational equity considerations over the extended 30-year period that encompasses both the increase in rates to cover major capital projects carrying cost and to recover MH's financial metrics.

The following Figure provides a high-level analysis that compares the cumulative rate increases, cumulative average rate increases and the cumulative Manitoba CPI for the actual rate increases between 2011/12 to 2021/22 and forecast rate increases between 2023/24 and 2041/42 in MH22 and CC10 and CC11:

Figure 32: Cumulative Rate Increases - 2012 to 2022 and 2023 to 2042

	1	2	3	4 (1 - 3)	5 (1 / 3)
	Cumulative Rate Increase	Cumulative Average Rate Increase	Cumulative MB CPI	Over (Under) MB CPI	Ratio To MB CPI
Actual - 2012 to 2022 (12 Years)	42.16%	2.97%	24.63%	17.53%	1.71
MH22 - 2023 to 2042 (19 Years)	45.68%	2.00%	48.11%	-2.43%	0.95
CC10 - 2023 to 2042 (18 Years)	24.17%	1.21%	48.11%	-23.94%	0.50
CC11 - 2023 to 2042 (18 Years)	30.73%	1.50%	48.11%	-17.38%	0.64

[133] Coalition/MH I-13 b

Observations related to Figure 32, are as follows:

1. Actual rate increases for the 12-year period of 2011/12 to 2021/22 accumulate to 42% or a cumulative average rate of around 3% per year in that period. Cumulative Manitoba CPI over that actual period was around 25% and as such ratepayers paid around 18% in excess or 1.7 times the cumulative rate of inflation in advance of the major capital projects going into service;
2. Proposed rate increases in MH22 for the 19-year period of 2023/24 to 2041/42 accumulate to 46% or a cumulative average rate of around 2% per year in that period. Cumulative Manitoba CPI over that forecast period is around 48% and as such ratepayers are projected to pay around 2% less or 0.95 of the cumulative rate of inflation in the forecast period; and
3. Proposed rate increases in CC10 and CC11 for the 18-year period of 2024/25 to 2041/42 accumulate to 24% to 31% or a cumulative average rate of around 1.2% to 1.5% per year in that period. Cumulative Manitoba CPI over that forecast period is around 48% and as such ratepayers would be projected to pay around 17% to 24% less or 0.55 of the cumulative rate of inflation in the forecast period, under these scenarios.

The implications of this high-level analysis are that ratepayers having been paying average rate increases of 3% per year during the last 12-years period when the major capital projects were not in-service, and these customers were not receiving the benefits of these projects. In contrast, under either MH22 and the 2% rate path and CC alternative rate scenarios CC10 and CC11, ratepayers who are now receiving the benefits of these projects that are in-service are projected to pay average rate increases of 2% per year or less.

This analysis points to the potential intergenerational inequity between ratepayers over the last 12 years and the next 19 years. A potential remedy to this situation is for a rate-pause in the forward Test Years (2023/24 and 2024/25) such to provide a mid-term course correction in the form of rate relief to current customers for a more even distribution of the total costs of the major capital projects entering service – based on a longer-term multi-decade perspective.

A rate-pause in the forward Test Years may result in slightly higher rate increases in years 4 to 20 of the forecast period, but this is not unfair based on the above noted analysis. One of the Consumer Coalition alternative rate scenarios, CC3, demonstrates that rate increases at the level of 1.35% would be sufficient to attain a 25% equity ratio by 2041/42, assuming more cost control by MH and a rate pause in the forward Test Years. A MH rate sensitivity demonstrates that without more cost control by MH, that a rate-pause in the forward Test Years would require a 2% rate increases to attain a 25% equity ratio by 2041/42.

Currently, there is a confluence of a number of positive financial developments for MH: (i) a significantly improved financial outlook for MH in comparison to past forecasts (ii) near-term record levels of export revenues ($1.2 billion) and net income ($751 million) and (iii) a large

reduction in MH's cost structure in the form of $180 million annual reductions to payments to government (which represents about 7% of MH's normal level of revenues of $2.6 billion).

One must ask the questions – if now is not the time for a rate-pause or a short-term course correction – then when would there ever be a time – and would a rate pause assist customers with the current period of high inflation and rising interest rates?

The other option is a longer-term course correction through a single 1.2% to 1.5% rate increase on April 1, 2024 and comparable indicative rate increases thereafter, but this course correction will take 18 years.

In summary, a valid perspective based on longer-term intergenerational equity considerations, would be for the PUB to approve a rate pause in the forward Test Years of 2023/24 and 2024/25. Such a rate pause would be of assistance to customers. For the residential class, the total cumulative rate increases proposed by MH for the four Test Years under consideration in this Application would be 8.84%, including rate differentiation (3.8% was already implemented on January 1, 2022).[134] For the former First Nations on-reserve residential rate class, rate increases back to September of 2020 have already accumulated to 13.8%, with the additional proposed differential rate increases accumulating to 19.3%.[135]

9.6 Weighting the Three Analytical Perspectives Results in a Recommendation of a Single 1.3% Overall Average Rate Increase on April 1, 2024 & Confirmation of the 3.6% Interim Rate Increase Effective January 1, 2022

Judgemental weighting of the three analytical perspectives presented in Sections 9.3 to 9.6 results in a recommendation of a single 1.3% overall average rate increase on April 1, 2024 and confirmation of the 3.6% interim rate increase effective January 1, 2022, as final. This recommendation considers cost containment by MH as noted in the Sections above.

The PUB describes its rate-setting mandate as setting electricity rates for MH customers that balance two concerns (i) the interests of MH ratepayers and (ii) the financial health of MH.

While the additional revenues sought in the rate application are important to MH's maintaining MH's financial health over time, they are also important to the finances of ratepayers and the economy of Manitoba, over time. The NPV in perpetuity of the three rate increases to customers for which MH is seeking final approval in this Application is approximately $2.8 billion.

In order to provide recommendations to the PUB with respect to MH's rate increase proposals, the six conclusions and recommendations from Sections 3.0 to 8.0 of this Evidence and the

[134] Coalition/MH II-8 a
[135] AMC/MH II-12

financial information on the record of the proceeding were examined from three analytical perspectives:

1. The financial metrics in the 2023/24 and 2024/25 Test Years only;
2. Rate-smoothing in the 20-year financial forecast period to 2041/42; and
3. Longer-term intergenerational equity considerations for the 30-year period between 2011/12 and 2041/42.

The results from analytical perspective #1 (Test Year Only Analysis) is that there is no Justification for 2% Rate Increases in 2023/24 & 2024/25 based on traditional rate-setting metrics, contained solely in the Test Years themselves. The traditional rate-setting metrics in the Test Years are all above long-standing targets or showing progress towards the attainment of longer-term targets, without any further rate increases.

The results from analytical perspective #2 (20 Year Rate Smoothing Analysis), is that a single 1.2% to 1.5% rate increase on April 1, 2024 and indicative annual rate increases in the forecast period in the same range represent a more appropriate balancing of the impacts on customers and the financial health of MH. This range is also more consistent with MH's status as a GBE, the preliminary nature of Strategy 2040 expenditures, PUB policy directives from prior orders (including active cost containment on the part of MH) and public acceptance of rate increases in a record net income year. This more balanced rate smoothing represents significant rate relief for ratepayers of between 15% and 22% over the 20-year forecast period, as compared to MH's proposed 2% rate path.

The results from analytical perspective #3 (Longer Term Intergenerational Equity Analysis), would suggest the potential for a mid-term course correction in the form of a rate pause for current customers in the forward Test Years (2023/24 and 2024/25) for a more even distribution of funding the costs of the major capital projects. Ratepayers have paid average rate increases of 3% per year in the last 12-years period before the major capital projects were in-service. In contrast, under MH's rate proposals or the alternative rate scenarios, ratepayers who are now receiving the benefits of these projects are projected to pay average rate increases of 2% per year or less. This analysis points to the potential intergenerational inequity between ratepayer over the last 12 years and the next 19 years.

These analytical perspectives provide a continuum of between 0% and 1.5% rate increases as a recommendation to the PUB to more appropriately balance the interests of ratepayers with the financial health of MH and considering more active cost containment by MH.

On balance and giving some weight to each of the three analytical perspectives, it is recommended that a single 1.3% overall rate increase be approved by the PUB on April 1, 2024, which is towards the lower end of the indicative range of rate smoothing.

There certainly is ample justification if intervenors decide to advocate for a rate pause in the forward Test Years in their final arguments, considering the exceptional circumstances surrounding this Application, public acceptance of the outcome of this hearing and longer-term intergenerational considerations. The recommendation of a single 1.3% overall rate increase on April 1, 2024, provides more weighting to the PUB's policy of rate smoothing to phase in the required rate increases that result from the major capital projects.

Based upon similar considerations, it is recommended that the PUB provide final approval to MH with respect to the 3.6% interim rate increase that was approved by the PUB effective January 1, 2022. Rolling back the 3.6% rate increase, only to impose larger rate increases in future test years appears counter productive to the objective of rate smoothing. If the PUB determines that further rate relief is due to ratepayers, then this is recommended to be implemented on a prospective basis through a rate pause or lower annual rate increases.

The cumulative rate increase that results from these recommendations is 4.94% (1.036 * 1.013), which when considered over the four test years that are the subject of this Application is about 1.24% per test year – which is consistent with the recommended indicative rate increase for rate smoothing purposes.

Appendix A: Darren Rainkie *Curriculum Vitae*

Darren Rainkie, CPA, CA, CBV

Principal – Darren Rainkie Consulting
Phone: 204.782.5877 or Email: darrenrainkie@gmail.com

HANDS ON & MULTI-FACETED EXPERTISE

IMPROVED REGULATORY & BUSINESS OUTCOMES FOR CLIENTS

QUALIFICATIONS & EXPERTISE

- Executive Utility Leadership
- Regulatory Policy & Strategy
- Revenue Requirement Specialist
- Regulation Process Management
- Financial Management
- Adept Expert Witness

CAREER HIGHLIGHTS

- Deep and multi-faceted expertise in all aspects of rate-regulation (1990-Present)
- Extensive experience testifying as a policy & subject matter expert at regulatory proceedings (2000-Present)
- Executive experience (Acting CEO, CFO, Controller & Treasurer) at Manitoba Hydro & Centra Gas (2006-2017)
- Senior level expertise in a broad range of financial management disciplines (2000-2017)

PROFESSIONAL EXPERIENCE

- Independent Consultant 2017-Present
- Manitoba Hydro 1999-2017
- Centra Gas 1994-1999
- Price Waterhouse 1988-1994

EDUCATION

- Chartered Business Valuator 1993
- Chartered Professional Accountant (Chartered Accountant) 1991
- B. Com. (Hons. – With Distinction), University of Manitoba 1988

PROFILE

Darren leverages his 30+ years of **hands on experience** and **multi-faceted expertise** in rate-regulation, utility & financial management to **improve regulatory & business outcomes for clients** that participate in and are impacted by rate-regulation - including applicants, intervenors, utility customers, regulatory tribunals & government agencies. He specializes in providing rate-regulation and financial advisory services, with an emphasis on regulatory policy & strategy and revenue requirement & fiscal matters.

The **client benefits** from **Darren's advisory services** are summarized as follows:

Access to a Comprehensive Suite of High-Quality Regulatory Services – Darren's deep specialization in rate-regulation and multi-faceted regulatory expertise enables him to provide high-quality advice to clients on regulatory policy, strategy, issues and process – that is customized/adapted to the relevant sector, ownership structure, rate-setting framework, subject matter and type of regulatory proceeding.

Effective Diagnosis of Issues & Sound, Practical Advice – Decades of hands on and executive level public utility experience - gives Darren the ability to effectively identify critical issues, evaluate alternative options & risks and develop pragmatic solutions for clients that are aligned with longer-term vision and strategic direction and balance utility and customer interests.

Integrated, Broad-Based & Credible Recommendations – Darren's financial management expertise results in recommendations to clients that evaluate the broader financial implications & integrates these implications into the ratemaking framework – with the inherent credibility associated with first-hand & senior level experience applying this financial expertise in a complex regulated enterprise.

Sustainable Solutions & Greater Potential of Stakeholder Acceptance – Clients benefit from Darren's leadership experience, collaborative approach and ability to effectively engage with stakeholders – which leads to more sustainable solutions, greater potential of stakeholder acceptance, as well as opportunities to facilitate client knowledge transfer and learning.

Building Consensus & Commitment to Implement Recommendations – Darren's uses his excellent communication & influencing skills, along with his extensive experience providing testimony at regulatory proceedings – to assist clients in obtaining a shared understanding of issues & options with internal and external stakeholders and building consensus for and commitment to implementing recommendations.

OVERVIEW OF PUBLIC UTILITY REGULATORY EXPERIENCE

Deep Specialization in Rate Regulation & Multi-faceted Regulatory Expertise

- A deep specialization in rate-regulation encompassing the majority of a professional career spanning over 30 years, including employment with/advising **multiple parties** to the regulatory process: providing advisory services to provincial regulators, executive oversight and management of rate applications and regulatory filings of applicant utilities and providing independent expert advice to intervenors and applicants.
- Multi-faceted regulatory expertise including **multiple sectors** (electricity, natural gas, mandatory auto insurance, water & waste, energy efficiency, district energy, propane, group 2 pipeline), a number of **jurisdictions** (British Columbia, Alberta, North West Territories, Manitoba, New Brunswick, Nova Scotia), various **ownership structures** (crown-owned, investor-owned and municipally-owned utilities) and a number of **rate-setting/legislative frameworks** (rate base/rate of return, modified cost of service, historic & future test years, multi-year applications).
- Extensive experience in a broad range of **regulatory proceedings** (general rate applications, revenue requirement applications, major capital project and certificate of public convenience and necessity reviews, integrated resource plan, decarbonization and demand-side management reviews, cost of service methodology reviews, back-up/top-up service pricing & terms, commodity cost prudence reviews/pass throughs, franchise expansion & feasibility test reviews, natural gas broker service improvements, debt & equity issues, accounting policy selection, depreciation rates, intercompany cost allocations & affiliate transactions, pipeline safety, integrity & construction methods, customer disconnections, automated meter reading and natural gas cooperative acquisitions) and expertise in all aspects of **rate-regulation subject matter** (regulatory policy, revenue requirements, cost of capital/capital structure, cost allocation and rate design).
- Experience with different types of **regulatory processes** (oral hearing, paper hearing, ex-parte, complaint based and alternative dispute resolution) and through all **regulatory cycle components** (strategy development & case planning, application & evidence preparation/evaluation, stakeholder engagement, witness training & preparation, discovery & hearing process management, presentation of expert testimony, cross examination & argument strategy/content, regulatory decision drafting, compliance filing preparation/evaluation, regulatory process improvement recommendations).

Hands On & Executive Level Public Utility Experience

- Hands on **public utility experience** through **23 years of employment** with a privately-owned natural gas utility and one of Canada's largest publicly owned, vertically integrated electric and natural gas utilities.
- Over 11 years of **executive leadership experience** actively collaborating in the management of the corporation, developing corporate & business unit strategic plans, developing risk management plans and successfully managing multiple strategic initiatives simultaneously.
- A **comprehensive understanding** of the **business, operations** and **risks** related to **regulated public utilities**, how decisions are made in this environment - as well as the strategic challenges facing regulated entities.
- A proven track record of developing **innovative financial** and **regulatory strategies** that are aligned with the overall vision and strategic direction of the organization - to ensure the on-going financial sustainability of the utility and respond to future business requirements.

Broad Range of First-Hand Financial Management Expertise – Applied to a Complex Regulated Enterprise

- Over 17 years of senior level and first-hand expertise in a **broad range** of **financial management disciplines** including: setting financial targets/key performance indicators, long-term financial forecasting, operating cost budgeting, capital cost budgeting, treasury & debt management, corporate risk management, accounting policy selection, financial & management reporting and internal cost allocation between lines of business.

- A **comprehensive understanding of utility financial models** and the elements that impact the model and financial performance, including key inputs, underlying processes, best practices, expected outcomes, options and key performance indicators. Demonstrated experience in applying this diverse financial management expertise and integrating them into the ratemaking framework of a complex regulated enterprise.
- Initiated, championed and actively participated in a number of transformational initiatives to ensure the ongoing financial sustainability of Manitoba Hydro during a period of extensive major capital investment, including: a comprehensive **review of corporate financial targets**, a complex **scenario analysis** to review the adequacy of financial reserves/forecast long-term rate impacts, a **multi-year budgeting strategy** designed to achieve operating cost savings; a **corporate asset management framework** to improve the prioritization of sustaining capital expenditures, an **alternate debt management strategy** to retire debt and improve the financial outlook and a top-down strategy driven approach and **transformation of rate applications** to balance financial integrity with interests of ratepayers.
- Demonstrated ability to **effectively identify issues impacting** the **long-term financial outlook** of **regulated enterprises**, evaluate historic and expected performance against key performance indicators, develop options & identify levers that can be used to positively impact rates to customers and make credible recommendations to intervenors, applicants and regulatory tribunals.

Collaborative Approach & Stakeholder Engagement Experience

- A principled and **collaborative leader** with extensive experience leading, developing, mentoring, collaborating and providing direction to a diverse team of senior professionals as well as cross-disciplinary project teams.
- **Worked collaboratively** with **internal officials** – such as subject matter experts, senior management, executive team, board committees and board of directors to achieve the **strategic, operational** and **financial goals.**
- Managed the interactions with and **build strong relationships** with **external stakeholders**, including provincial government officials, indigenous business partners, external auditors, investment banking institutions and credit rating agencies. As a result of the direct involvement with external stakeholders, have experience explaining the perspectives and issues of these stakeholders to regulatory stakeholders as an executive policy witness.
- Demonstrated capability to **engage with** and **build strong relationships** with **regulatory stakeholders**, including regulatory tribunal staff & advisors, consumer group/intervenor representatives & experts and applicant officials. Provided oversight and actively participated in a number of **regulatory stakeholder engagement sessions** with the objectives of fostering positive relationships, building shared understanding of participants and reducing the number of issues to be reviewed/contested during regulatory proceedings.

Adept Witness & Excellent Communication and Influencing Skills

- As a utility executive, oversaw and participated in the development and delivery of **numerous persuasive presentations** and **recommendations** to obtained direction/approvals from the executive committee, audit committee, board of directors and regulatory tribunal - with respect to financial targets, long-term financial forecasts, proposed rate increases, operating and capital expenditure plans, financing and risk management plans, depreciation study changes, accounting policy selection/IFRS implementation and financial reporting. As an advisor to a regulatory tribunal, intervenors and applicants, have delivered numerous briefings to the client on the significant issues arising in regulatory applications.
- An excellent **reputation** for the **ability to draft well constructed documents** and **reports**, and to organize complex business & regulatory concepts into compelling evidence, using clear and understandable language. The range of experience includes five years drafting regulatory decisions for a regulatory tribunal, 23 years drafting regulatory applications/reports for applicants and four years developing independent reports for intervenors and applicants.

- Over 20 years of **experience testifying** as a **subject matter witness**, **executive policy witness** and **independent expert** at regulatory proceedings. Areas of testimony include: policy & strategy (electric & natural gas general rate applications, major capital projects review, cost of gas prudence review, cost of service methodology review), financial targets, long-term financial forecasts, operating & capital cost forecasts, debt management strategies, depreciation studies, adoption of IFRS accounting policies for rate setting purposes, financial results, general revenue requirement components, rate base, return on equity, capital structure, financial feasibility tests, as well as regulatory approvals and procedural matters.

PROFESSIONAL EXPERIENCE

PRINCIPAL, DARREN RAINKIE CONSULTING 2017 – Present

- Provide **rate-regulation advisory services** in the subject matter areas of policy, strategy, revenue requirements, cost of capital/capital structure, cost allocation, rate design, major capital project reviews, planning and management of regulatory applications and associated hearing processes, stakeholder engagement and witness testimony in regulatory proceedings.
- Provide **financial advisory services** in the subject matter areas of financial targets, long-term forecasting, operating & capital cost budgeting, debt management, risk management, intercompany cost allocation, financial reporting and business valuation.
- Provided regulatory consulting services on regulatory policy and revenue requirement matters to the **Consumers Coalition** (Consumers Association of Canada (Manitoba), Aboriginal Council of Winnipeg and Harvest Manitoba) in connection with the **Manitoba Hydro 2021/22 Interim Rate Application** and associated **Review & Vary Application** before the Manitoba Public Utilities Board.
- Provided regulatory consulting services to the **Consumers Coalition** and **Consumers Association of Canada (Manitoba)** in connection with the **Manitoba Hydro/Centra Gas Manitoba Inc. Combined Hearing Application** - before the **Manitoba Public Utilities Board.**
- Provided regulatory consulting services on regulatory policy and revenue requirement matters to the **Consumers Coalition** in connection with its **Application for an Order Requiring a Manitoba Hydro Status Update Hearing**, before the **Manitoba Public Utilities Board.**
- Provided independent expert evidence and advice on policy evaluation and practice research matters on behalf of the **Consumers Association of Canada (Manitoba)** in the **Centra Gas Manitoba Inc. Natural Gas Cost of Service Review** proceeding before the **Manitoba Public Utilities Board.**
- Provided independent expert evidence and advice on policy evaluation, customer research and stakeholder engagement matters on behalf of the **Consumers Association of Canada (Manitoba)** in the **Centra Gas Manitoba Inc. Rate Re-bundling** proceeding before the **Manitoba Public Utilities Board.**
- Conducted a review of the potential for cross-subsidy between distribution of gas and sale of gas at **Liberty Utilities (Gas New Brunswick) LP** during 2021 for the **New Brunswick Energy & Utilities Board.**
- Provided regulatory consulting services to the **BCOAPO ET AL** Intervenor Group (British Columbia Old Age Pensioners' Organization, Active Support Against Poverty, Disability Alliance BC, Council of Senior Citizens' Organizations of BC, Tenants Resource & Advisory Centre and Together Against Poverty Society) in connection with numerous applications before the **British Columbia Utilities Commission**, including:
    - **FortisBC Energy Inc. (gas)** - Pattullo Gas Replacement Project Certificate of Public Convenience & Necessity (CPCN), Biomethane Energy Recovery Charge Rate Methodology & Comprehensive Review of a Revised Renewable Gas Program, Tilbury Liquefied Natural Gas Storage Expansion Project CPCN, 2022 Long-Term Gas Resource Plan and 2023 Demand-Side Management Expenditures Plan.

- **FortisBC Inc. (electric)** - 2023 to 2027 Demand-Side Management Expenditures Plan.
- **Pacific Northern Gas Ltd.** - Salvus to Galloway Gas Line Upgrade Project CPCN, PNG West Division 2022 Revenue Requirements Application and PNG North-East Division 2022 Revenue Requirements Application.
- **Creative Energy Vancouver Platforms Inc.** - 2021 Long-Term Resource Plan, 2021 Revenue Requirements Application for the Core Steam System, 2021 Application for Heating Rates for the Thermal Energy System & Cooling Rates for the District Cooling System, Core Steam System Decarbonization Project CPCN, and Beatty-Expo Redevelopment Project CPCN.
- **Corix Multiutility Services Inc.** – Burnaby Mountain District Energy Utility 2020 to 2023 Revenue Requirement & Rates Application.
- **Insurance Corporation of British Columbia** - 2021 Policy Year (2021/22 & 2022/23) Revenue Requirements Application.
- **British Columbia Utilities Commission** - Inquiry into the Acquisition of Renewable Natural Gas by Public Utilities in British Columbia - Phase 2.

- Provided independent expert evidence and testimony to the **Nova Scotia Utility and Review Board** regarding **Nova Scotia Power Inc.'s 2021 Back-Up/Top-Up Amendment Application** with respect to pricing and terms and conditions of service of municipal electric utilities.
- Provided advisory services to **Efficiency Manitoba** in connection with its **2020-2023 Efficiency Plan** filing to the **Manitoba Public Utilities Board**, including regulatory on-boarding, filing review process design and strategic filing preparation advice.
- Provided independent expert evidence and testimony on regulatory policy, financial reserve targets and revenue requirement matters on behalf of the **Consumers Association of Canada (Manitoba)** in the **Centra Gas Manitoba Inc. 2019/20 General Rate Application** proceeding before the **Manitoba Public Utilities Board.**
- Independent expert evidence and testimony on regulatory policy, financial reserve targets and revenue requirement matters on behalf of the **Consumers Coalition** in the **Manitoba Hydro 2019/20 Rate Application** proceeding before the **Manitoba Public Utilities Board.**
- Conducted an independent review of the **2019/20 Chestermere Utilities Inc. rate proposal** (water, sanitary & storm services) and associated financial implications for the **City of Chestermere** (acting as the regulator).
- Provided independent advice to the **Consumers Association of Canada (Manitoba)** on case strategy and the capital management plan in connection with the **Manitoba Public Insurance 2019/20 General Rate Application** before the **Manitoba Public Utilities Board.**
- Conducted a review and made recommendations on the implementation of a revised **internal cost allocation methodology** (allocation of corporate and shared service costs) for **Corix Infrastructure Inc.** (a leading provider of energy, water & wastewater utilities for small to medium-sized communities across North America).
- Provided independent advice to an Industrial Intervenor on the Advanced Metering Infrastructure (AMI) project in connection with **New Brunswick Power Corporation 2018/19 General Rate Application** before the **New Brunswick Energy & Utilities Board.**
- Provided independent advice to legal counsel for an intervenor with respect to case strategy, evidence evaluation and revenue requirement matters in connection with the **Northwest Territories Power Corporation 2016-2019 General Rate Application** before the **Northwest Territories Public Utilities Board.**
- Provided strategic advice on financial reporting matters to the **Manitoba Department of Health** as part of the Health Sector **Financial Budgeting & Reporting Improvement Project.**

MANITOBA HYDRO & CENTRA GAS **1999 – 2017**

Acting President and Chief Executive Officer **September to December 2015**

- Responsible for the **overall executive leadership** of one of the largest integrated electric and natural gas utilities in Canada with over $20 billion in assets, $2.3 billion in revenues, 568,000 electricity and 277,000 natural gas customers and over 6,000 employees.
- Maintaining progress on **delivery of key strategic objectives, execution on major capital projects** and effective transition to the newly appointed CEO while simultaneously managing several complex finance & regulatory projects in the on-going role as CFO.

Vice-President, Finance & Regulatory Affairs and Chief Financial Officer **2013 – 2017**

- Responsible for the **executive leadership** of the **Finance & Regulatory Affairs business unit** (Controller, Treasury, Rates & Regulatory Affairs, Financial Planning and Corporate Risk Management) and **Manitoba Hydro International** (professional consulting and project management services to energy sectors world-wide).
- Member of the **Executive Committee** that actively collaborated in the **management of the corporation** and the formation, revision and achievement of the **corporate strategic plan** and establishment of **business unit goals & strategies** that align with the strategic objectives of Manitoba Hydro. Led, developed and mentored a diverse team of senior professionals as well as cross-disciplinary project teams.
- **Chief regulatory officer** and provided executive direction with respect to regulatory affairs before the Manitoba Public Utilities Board (MPUB) (Manitoba Hydro & Centra Gas) and National Energy Board (Minell Pipelines). Represented the corporation as **executive policy witness** and chief regulatory strategist for several significant electric and gas regulatory proceedings before the MPUB, as follows:
    - The **2016 Electric Cost of Service Methodology Review** before the MPUB to review the methodology underpinning the allocation of a $2 billion revenue requirement and $20 billion rate base among 568,000 customers.
    - The **2015 Electric General Rate Application** before the MPUB which included final approval of interim rates for 2014/15 and rates for 2015/16 as well as the establishment of a process to review interim rates for 2016/17. Applied a top-down strategy driven approach and drove the transformation of rate applications to increase revenues, ensure the on-going financial sustainability of the corporation, maintain reliable service and stable rates - while balancing the interest of ratepayers with the financial integrity of the corporation.
    - The **2015 Cost of Gas Application** before the MPUB and directed the development of the regulatory strategy and principles associated with the prudence review and recovery of additional gas costs of $46 million incurred during the record cold winter weather of 2013/14.
    - The finance witness panel at the **2014 MPUB review of the Need For and Alternatives To** (NFAT) Manitoba Hydro's proposed Major Generation and Transmission capital projects involving a planned investment of over $17 billion. The finance panel witness responsibilities included the potential impact on customers rates, financial outlook and financial risk associated with the planned investments.
    - The **2013 Centra Gas General Rate Application** before the MPUB to set gas costs and non-gas revenue requirement for 2013/14.

- Guided the development of **corporate financial targets** and the **long-term financial forecast** as well as corporate operating, capital and financing plans that are consistent with the overall objectives of the Corporation and obtained endorsement from the Audit Committee and Manitoba-Hydro Electric Board (MHEB). Initiated and provided executive oversight to a **comprehensive review of corporate financial targets** to determine if they continued to be appropriate during a period of extensive capital investment of over $17 billion. Provided policy guidance to support the development of increasingly sophisticated **financial models to provide scenario analysis** (over 15,000 financial projections) on key financial variables (water flows, export prices, interest rates and capital costs) to evaluate the adequacy of financial targets and financial reserves and forecast the long-term rate impacts of major capital projects.
- Initiated target setting process and collaborated with the executive team to develop a **multi-year budgeting strategy** to substantially reduce the growth in operating expenditures. Championed the establishment of an overall **corporate asset management framework** and further development of systems to improve the planning and prioritization of sustaining capital expenditures in the generation, transmission, distribution and corporate functions.
- Provided executive oversight to the development and execution of **financing strategies** and plans to obtain long-term debt financing in the order of $1.5 billion to $2 billion annually and to effectively manage the corporation's liquidity, foreign exchange and interest rate risks. Provided policy guidance to treasury staff to develop a more cost-effective approach to **manage significant risk exposure from US currency fluctuations** on export revenues and to develop an **alternate debt management strategy** to retire debt and improve the financial outlook.
- Directed the **financial** and **management reporting** and **corporate risk management functions** and provided regular reports on the financial results and risks of the corporation to Executive Committee, Audit Committee and MHEB. Executive accountable to oversee the **transition** from Canadian Generally Accepted Accounting Principles (CGAAP) to **International Financial Reporting Standards** (IFRS) for financial reporting purposes and the strategy to use IFRS for rate-setting purposes.
- Chair of the **Corporate Risk Management** and **Rates Review committees**. Member of the Export Power and Gas Supply **Risk Management committees** and the **Corporate Asset Management Executive Council**. Member and **Treasurer of the Wuskwatim** and **Keeyask Limited Partnership Boards** working closely with Indigenous partners.

Corporate Controller, Controller Division **2008 - 2013**

- Directed the **preparation** of the **electric** and **gas revenue requirement filings** and represented the corporation as a **senior subject matter witness** at several MPUB **electric rate hearings** between 2008 and 2013 (2008/09, 2009/10, 2010/11 & 2011/12, 2012/13 & 2013/14 GRA's) providing witness testimony on financial results, long-term financial forecast, operating & capital cost forecasts, other revenue requirement components as well as implementation of depreciation studies and IFRS accounting policies for rate-setting purposes.
- Oversaw the development of the **long-term financial forecast** and the **coordination of the consolidated operating cost** and **capital expenditure forecasts** and presentation to the Audit Committee and MHEB.
- Led the **financial** and **management reporting functions** of the corporation and managed interaction with the provincial Comptroller's Division and external auditors. Guided the **provision of financial services** to the **business unit** management teams.

Corporate Treasurer, Treasury Division **2006 - 2008**

- Led the development of **debt management** and **financing strategies** to obtain corporate financing requirements and effectively manage the corporation's liquidity, foreign exchange and interest rate risks. Provided testimony as a **senior subject matter expert** at the 2007/08 & 2008/09 Centra GRA on rate base, return on equity, working capital allowance, finance expense and debt management.
- Managed interaction with **credit rating agencies**, the provincial Treasury Division and investment banking institutions.
- Guided **cash management**, cash forecasting and **credit risk management** functions and the administration of banking arrangements.

Manager, Regulatory Services Department **1999 - 2006**

- Responsible for **regulatory planning** and administration and providing **recommendations** to **senior management** on regulatory **strategy, issues** and **procedural matters**. Acted as a liaison with MPUB staff and advisors.
- **Managed** the preparation of **numerous regulatory applications**, **filings** and **reports** to the **MPUB**, the post-application/pre-hearing processes, the public hearing process and the interpretation and compliance with MPUB decisions from 1999 to 2006 (types of regulatory proceedings/matters include: general rate applications, commodity cost prudence reviews/pass throughs, franchise expansions & feasibility tests, natural gas broker service improvements & stakeholder engagement process, pipeline safety, integrity & construction methods, customer disconnections, acquisition of a natural gas cooperative).
- Represented the corporation as a **subject matter witness** at several MPUB **natural gas rate hearings** between 2000 and 2006 (2000 Interlake expansion, 2003/04 GRA, 2004/05 Cost of Gas, 2005/06 & 2006/07 GRA, 2007/08 & 2008/09 GRA), providing witness testimony on revenue requirements, rate base, cost of capital/return on equity, capital structure, lead-lag study, financial feasibility tests and regulatory approvals and procedural matters.
- Oversaw the development of the **Quarterly Primary Gas application** and associated processes in 2000 to adjust the cost of gas from western Canada on each gas quarter using an efficient and streamlined regulatory approval process.

CENTRA GAS MANITOBA INC. 1994 - 1999

Senior Coordinator, Regulatory Services Department **1997 - 1999**

- Responsible for the **coordination** and **preparation** of **regulatory applications, filings** and **reports** to the MPUB (types of regulatory proceedings/issues include: 1998 general rate application, commodity cost prudence reviews/pass throughs, franchise expansion & feasibility test reviews, debt & equity issues, accounting policy selection, depreciation rates, intercompany cost allocations & affiliate transactions).
- Provided **direction** to **regulatory staff** and **internal clients** with respect to regulatory process and procedural matters, the preparation of responses to MPUB decisions, directives and requests and participated in the **preparation of evidence** and **witnesses** for public hearings.

Senior Financial Analyst, Financial & Accounting Services Department **1994 - 1997**

- Acted as internal expert and **provided support** to **company witnesses** at MPUB public hearings with respect to business case and feasibility assessments as well as financing, capital structure and cost of capital/rate of return and feasibility test matters (1995 & 1997 GRA's). Developed the Centra **return on equity formula** proposal for the 1995 GRA.
- Provided advice and assisted in the **preparation of business cases** with internal management and project teams to support business expansion and growth opportunities, capital expenditures and operating decisions. Coordinated all aspects of **financial analysis** and **feasibility assessments** including the development of financial models, investment evaluation criteria and the presentation of results to internal management.

PRICE WATERHOUSE, CHARTERED ACCOUNTANTS (Winnipeg Office) 1988 - 1994

Assistant Manager, Financial Advisory Group **1990 – 1994**

- Acted as **accounting & finance advisor to the MPUB** between 1990 and 1994 on several Centra Gas regulatory applications (including 1990, 1991, 1992, 1993 GRA's), a 1994 Manitoba Hydro GRA and a Stittco Utilities Manitoba (propane) 1991 GRA. Drafted numerous regulatory decisions for the MPUB during that timeframe. Provided advice on all aspects of revenue requirements including operating costs, depreciation, finance expense, income & other taxes, rate base, working capital, capital structure and cost of capital/return on equity.
- Provided extensive **consulting advice to the MPUB** and drafted regulatory decisions on **capital structure** and **cost of capital/return on equity** matters including the last comprehensive decision on the allowed capital structure and return on equity for Centra Gas in 1994.
- Prepared **business valuations**, conducted business reviews for acquisition and divestiture purposes and prepared **quantifications of losses** or **damages** for use in litigation proceedings.

Audit Senior, Audit & Business Advisory Group **1988 - 1990**

- Provided **audit** and **business advisory services** to clients in several industries, including real estate, investment dealing and agriculture, as well as public sector clients.