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Public Utilities Board
400-330 Portage Avenue
Winnipeg, Manitoba R3C 0C4

Attention: Rachel McMillin, Associate Secretary

Dear Sirs/Mesdames:

Re: Manitoba Hydro 2023/24
and 2024/25 General Rate Application
Our Matter No. 0194440 AFH

MIPUG submission in respect of Bowman Recommendation #4

In Order 42/23, the Public Utilities Board ("PUB") indicated it will consider Recommendation #4 from the evidence of Mr. Bowman (April 3, 2023) by way of written submissions. The Board requested parties address the following questions:

- Is it appropriate to write off Board-approved regulatory deferral accounts against 2022/23 net income?
- Are there adverse consequences (e.g., a perceived lack of regulatory certainty) to writing off a Board-approved regulatory deferral account? If so, what is the anticipated impact of those consequences?
- Should any other deferral accounts be written off completely or partially against 2022/23 net income?

The specific recommendation from Mr. Bowman is as follows:

> Balances in the Conawapa deferral account, the Loss on Disposal account related to discontinued operations, and the Asset Removal cost deferral account, totalling approximately $382 million, should be written-off to income in

2022/23. The Board should ensure the necessary Orders are provided in time for this transaction to be recorded in the 2022/23 fiscal year.

The recommendation cites evidence of Hydro in PUB information requests (PUB/MH-I-33b) which give the basic requirements and impacts of considering such transactions.

Is it appropriate to write-off Board approved regulatory deferral accounts?

Yes, it is appropriate for the PUB to reduce the amortization period to one year so the transactions are recorded in the 2022/23 fiscal year. Doing so would be consistent with what was envisioned in NFAT and would be an appropriate use of unexpected additional revenue. Doing so would be consistent with the continued expectation that Conawapa is not the next required resource. There is no reason to continue to put the burden of the sunk costs of Conawapa or of Selkirk GS on future ratepayers. Those costs are not used and useful on a go forward basis.

The $380 million in sunk costs for Conawapa was categorized by Hydro as costs required to protect in-service dates. While that may have been a valid objective by Manitoba Hydro prior to NFAT, the NFAT decision and the passing of time have confirmed that this objective should not be pursued. One of the reasons for a 30 year amortization period was that there might still be a justification for including Conawapa in a preferred development plan. As explained in Mr. Bowman's evidence, that fundamental assumption is not supported by the current filing and evidence and it is therefore appropriate, given the other unexpected developments described in this submission, that the balance of the accounts be amortized as of 2022/23.

To the extent that the PUB was or continues to be concerned about rate shock caused by accelerated amortization, the unexpected announcement of retroactive relief by the Government of Manitoba in its charges addresses that concern. In its NFAT report, at p. 191, the PUB had encouraged the Government of Manitoba to provide rate relief and specifically identified the sunk costs of Conawapa as a justification for that rate relief. Implementing Mr. Bowman's recommendation would therefore not undermine any messaging by the PUB on rates and stability as it appears that the PUB recommended that the Government of Manitoba reduce the provincial charges to address, in part, the sunk costs of Conawapa. Now that the Government of Manitoba has finally implemented the spirit of the PUB's recommendation, it is appropriate to implement Mr. Bowman's recommendation which includes immediately addressing the balance of Conawapa sunk costs. Doing so would be consistent with the NFAT decision. One of the benefits of the retroactive adjustments announced on November 23, 2022, is that they allow the PUB to address the sunk costs in Conawapa immediately as was the PUB's hope expressed as follows at p. 191 of its NFAT decision:

> **It would be reasonable for the Government of Manitoba to give serious consideration to a reduction of increment provincial benefits from the Keeyask Project. This should**

> **involve the Government directing a portion of its incremental capital taxes and water rental fees** to be used to mitigate the impact of rate increases on lower-income customers, as well as northern and aboriginal communities.
>
> Manitoba Hydro can contribute to the impact of rate increases in two ways. It can relax is 75/25 debt-to-equity ratio policy to moderate its proposed electricity rate increases. Manitoba Hydro should also mitigate rate increases by seeking to reduce its own expenditures through operational savings.
>
> The development of the Conawapa Project would result in even higher ratepayer commitments to 50 years, after which the rate increases are not as great as other options. Based on current circumstances, the risks related to Conawapa's development far exceed any rewards to ratepayers over the next 50 years. It would not be prudent to continue spending money on **Conawapa. The Panel also notes the importance of sunk costs and their impact on rates, particularly when those costs have to be written off**. (emphasis added)

Appropriate amortization period

As a preliminary comment, it should be noted that although the colloquial term "write-off" is used throughout the PUB information requests, Mr. Bowman's evidence, and the PUB Order 42/23, a more accurate description of the transaction proposed would be to adjust the amortization period in rates for the following three accounts to be one-year, as of 2022/23:

- **Conawapa planning costs**: from an amortization period of 30 years to an amortization period of one-year as of 2022/23.
- **Selkirk GS Loss on Retirement:** from a deferral account treatment with no defined amortization period at this time, to a period of one-year as of 2022/23.
- **Removal costs for electric assets that were not replaced:** from a deferral account treatment with no defined amortization period at this time, to a period of one-year as of 2022/23.

The distinction is important as the transaction is a regulatory approval tied to a fiscal year for which rates remain interim. The premise is not linked to Hydro's shareholder bearing the costs (as may be understood by a more technical understanding of the term "write-off") but instead Hydro's ratepayers bearing the cost by way of rates paid in 2022/23, which contributed to revenue being well above costs for that year.

The reason revenues are well above costs for 2022/23 is set out in Mr. Bowman's testimony, generally as follows:

1) **Interim Rate Increase:** Interim rates were set for 2022/23 in Board Order 137/21. The Board noted: "One of the most significant reasons for Manitoba Hydro bringing its Interim Application to the Board was the drought experienced in 2021/22."[1] Further, the Board took note that: "Looking forward, and given the 2021 drought conditions, Manitoba Hydro indicates there is an elevated likelihood of below average inflows occurring in 2022/23."[2]

   Instead, Manitoba Hydro experienced a year of "well above average water supply conditions"[3] For this reason, the interim rates for 2022/23 no longer are linked to the underlying premise on which they were set. This is a positive unexpected event.

2) **Export Market Prices:** Tied to the above issue, at a time of drought, high export market prices are a compounding factor. During the review of the interim rate increase still in place, MISO prices were relatively higher than had been the case in the previous few years[4]. Instead, with the turn to high water, higher export prices become a factor in support of higher net income and lower rate requirements. The GRA filing notes that the export markets have increased substantially: "the average monthly on-peak and off-peak export prices in the current 2022/23 Forecast are roughly 65% higher than those assumed in the 2022/23 Budget."[5] This is also a positive unexpected event.

3) **Government Charges:** The adjustment to water rentals and debt guarantee fees were announced November 23, 2022, retroactive to April 1, 2022. This information was not part of the input to establishing interim rates for 2022/23. This is a significant positive unexpected event which benefits the whole 2022/23 financial year.

At the same time as the above factors were developing, the 2022/23 year regulatory balances included three items which had no enduring benefit to customers, and which are proposed to be either amortized over very long periods into the future (Conawapa) or have no amortization period at all as yet established (Selkirk GS Loss on Retirement, and Removal Costs for Electric Assets that were not replaced).

[1] Order 9-22, page 14.
[2] Order 9-22, page 17.
[3] Application, Tab 4 (Amended), page 8.
[4] Order 9-22, page 20.
[5] Application, Tab 4 (Amended), page 9.

Under normal circumstances, reflecting a year with final rates, no adjustments to Board-approved regulatory deferral accounts should be expected. This is true whether the year in question had high or low net income. However, the unexpected events outlined above justify an exception.

In short, it is appropriate and justified to direct a one-year amortization of the noted balances in 2022/23.

Are there adverse consequences (e.g., a perceived lack of regulatory certainty) to writing off a Board-approved regulatory deferral account? If so, what is the anticipated impact of those consequences?

The obvious potential concern of a PUB decision electing to revise the amortization period during the interim rate year of 2022/23 is a perception of loss of certainty regarding regulatory deferral accounts.

However, as explained in the previous section, we submit there are no adverse consequences such as perceived lack of regulatory certainty. The Board recommended relief from Government charges in NFAT to address rate pressure issues including rate pressures caused by writing off Conawapa sunk costs. The Government granted retroactive relief in its charges, and therefore regulatory certainty is enhanced by the Board addressing, in the same year as the Government announcement, the full amortization of the regulatory accounts, the largest of which is the Conawapa deferral account.

The impact of doing so should be seen as positive. The reduction of Government charges is used in a way which is consistent with the NFAT decision. The acceleration of amortization reduces the revenue requirements as of 2023/24.

Another unique factor for 2022/23 is the confluence of (a) interim rates, which were (b) predicated on a set of facts that no longer exist, and (c) the revised facts led to higher net income and lower net revenue requirement than was forecast when the interim rates were set.

Absent the 2022/23 year-end requiring finalization, the above set of facts would readily support a revision to the amortization period for the regulatory accounts in question as part of the upcoming 2023/24 test year review. However, in this case Hydro has indicated that in order to match the revised amortization periods to the fiscal year in which interim rates apply, these Orders from the Board are needed before the final Orders from the upcoming hearing.

It would be MIPUG's submission that the Board should adjust the regulatory account deferral periods as proposed, with explicit acknowledgement that this is (a) part of the rate setting process, (b) the amounts are funded by rates (including the 3.6% interim rate increase) not by Hydro's shareholder's retained earnings, and (c) that absent adjustments as part of implementing interim rates or an unexpected event such as the Government announcement of a retroactive reduction in its charges, such revisions should not be expected in the future.

Should any other deferral accounts be written off completely or partially against 2022/23 net income?

MIPUG is of the view that regulatory deferrals are appropriate mechanisms to use where they improve the matching of costs and benefits. For example, this would include deferring the costs of DSM to match their long-term benefit to the system, or the costs of overheads that are linked to capital asset acquisition.

MIPUG generally cautions against establishing regulatory deferrals that solely serve to rate smooth, or to defer costs and revenues from the year in which they would otherwise be recorded solely for the purpose of managing rate impacts. It appears that managing rate impacts was one of the drivers for the general rationale for the Conawapa deferral, and may be the basis for the Selkirk disposal deferrals. In the case of Selkirk, there is no ongoing benefit of the plant now that it is not available for generating power. The noted costs have been incurred. Absent a regulatory deferral there would be no basis to amortize the costs in any future year.

At this time, MIPUG is not aware of any other regulatory deferrals that match the characteristics of those noted in the Bowman evidence – that is, accounts which lack enduring benefits or relevance to future periods.

Yours truly,

THOMPSON DORFMAN SWEATMAN LLP

Per:

Antoine F. Hacault

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AFH/av
cc: Board Counsel (all via e-mail)
Manitoba Hydro, and Intervenors

*Services provided through A. F. Hacault Law Corporation