Order No. 9/22

ORDER SETTING OUT FURTHER REASONS FOR DECISIONS IN ORDER 137/21 WITH RESPECT TO MANITOBA HYDRO'S 2021/22 INTERIM RATE APPLICATION

January 26, 2022

BEFORE: Robert Gabor, Q.C., Chair
Marilyn Kapitany, B.Sc., (Hon), M.Sc., Vice-Chair
Hugh Grant, Ph.D., Member
Irene A. Hamilton, Q.C., Member
Shawn McCutcheon, Member
Larry Ring, Q.C., Member

Public Utilities Board | Régie des services publics

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1.0 Executive Summary

This Order is the third of the three planned Orders by the Public Utilities Board ("Board") related to Manitoba Hydro's 2021/22 Interim Rate Application ("Interim Application"), filed November 15, 2021, and contains the substantive reasons for the Board's decisions in the prior two Orders. This Order does not change the interim electricity rates approved in Order 140/21.

Order 137/21, issued December 24, 2021, was the first of three planned Orders by the Board to address Manitoba Hydro's 2021/22 Interim Rate Application. In Order 137/21, the Board varied Manitoba Hydro's requested 5% General Consumers Revenue increase to instead approve a 3.6% increase. In this Order, the Board varies its direction in 137/21 with respect to the period of time that this revenue increase is in effect. The Board now directs that the additional revenue will be realized through new interim consumer rates that remain in effect until November 30, 2022, unless Manitoba Hydro files a General Rate Application by November 15, 2022 to confirm the 2021/22 interim rate increases and seek rates for 2022/23, and for 2023/24 if it so chooses. If Manitoba Hydro does not file a General Rate Application by November 15, 2022, the rates will revert to those in effect prior to Order 140/21.

Order 140/21, issued December 31, 2021, was the second of the three planned Orders and approved the specific rates and rate increases for each customer class. A summary of the average rate increases by customer class is as follows:

Customer Class	Average Increase
Residential	3.8%
General Service Small – Non-Demand	2.5%
General Service Small – Demand	3.6%
General Service Medium	3.8%
General Service Large 750V – 30kV	3.8%
General Service Large 30kV – 100kV	3.8%
General Service Large >100kV	3.8%
Area & Roadway Lighting	1.3%
Diesel Zone – Residential	0%

2.0 Background and Procedural History

Background

Under Manitoba law, the Board must set electricity rates for Manitoba Hydro's customers that are just and reasonable and in the public interest. In so doing, as confirmed by the Manitoba Court of Appeal, the Board balances the interests of Manitoba Hydro's ratepayers and the financial health of Manitoba Hydro. Together and in the broadest interpretation, these interests represent the general public interest.

Pursuant to subsection 25(1) of *The Crown Corporations Governance and Accountability Act*, CCSM c C336, the prices charged by Manitoba Hydro with respect to the provision of power ("rates for services") are reviewed by the Board. No changes in rates for services can be made and no new rates for services can be introduced without the approval of the Board. *The Act* requires Manitoba Hydro to submit proposals regarding rates to the Board for its review and approval.

When Manitoba Hydro applies to the Board for rate increases, including the rate increases sought in the Interim Application addressed in this Order, Manitoba Hydro bears the statutory onus of demonstrating that the increases sought are just and reasonable.

Notably, Manitoba Hydro filed its Interim Application seeking approval of January 1, 2022 interim, not final, rate increases. Any interim rate increases must be further reviewed by the Board and either varied or finalized in a subsequent public proceeding.

In Order 59/16, the Board determined that interim rate applications ought not to be the norm for Manitoba Hydro because interim rate applications do not offer the same level of public review as do General Rate Applications.

In Order 59/18, the Board found interim rates are set without the benefit of a full evidentiary record, involve an abbreviated process, and are adjudicated against a less onerous legal standard than are final rates. This finding by the Board is consistent with Manitoba Hydro's acknowledgment of the Supreme Court of Canada's fundamental principle that interim applications are "*made in an expeditious manner on the basis of evidence which would often be insufficient for the purposes of the final decision*."

The Board also found that interim rates may create a regulatory status quo that is difficult to overturn, despite a lack of full regulatory review when they are initially approved. Furthermore, interim rate processes are not to be used for purposes of convenience or as substitutes for the proper planning of General Rate Applications. Both ratepayers and Manitoba Hydro benefit from a robust and transparent process that results in final rates that are just and reasonable.

Therefore, as stated by the Board in Order 59/18, in the absence of unforeseen or emergency circumstances, interim rate increases are not to be sought.

Against that background, the Board accepted the position of Manitoba Hydro that the Government processes that resulted in Manitoba Hydro not filing a rate application with the Board in a timely manner in calendar year 2021 were beyond the control of Manitoba Hydro. From March 2020 when Bill 44 *The Public Utilities Ratepayer Protection and Regulatory Reform Act* was introduced until the September 22, 2021 ministerial directive for Manitoba Hydro to file an interim application with the Board (and with the re-numbered Bill 35 subsequently being withdrawn on October 6, 2021), Manitoba Hydro expected annual rate increases to be imposed by Government, as the Government did December 1, 2020. By the September 22, 2021 date of the ministerial directive, drought conditions had resulted in a decrease in forecast Net Extraprovincial Revenue. The Board found that the emergent drought conditions, the Government's unforeseen withdrawal of Bill 35 with its expected legislated electricity rate increases, and the Board's objective to avoid rate shock resulting from delayed rate increases required to address the costs of major new capital expenditures justified the use of an interim application process.

Procedural History

The Procedural History leading to this Order includes draft legislation, a Status Update Motion filed by the Consumers Coalition on March 26, 2021, and the November 15, 2021 Interim Application filed by Manitoba Hydro.

Draft Legislation

In March 2020, the provincial Government introduced Bill 44 *The Public Utilities Ratepayer Protection and Regulatory Reform Act* to establish a new legislated framework for the regulation of electricity rates and natural gas rates. Under the draft framework, both electricity and natural gas rates would be regulated in five-year intervals by the Board, commencing April 1, 2024, under *The Manitoba Hydro Act.* In the transition years leading to 2024, electricity rates would be set by the Government, through regulation.

Bill 44 was held over to the fall of 2020 and reintroduced as Bill 35 on October 14, 2020.

On December 1, 2020, Manitoba Hydro's rates were increased 2.9% for all customer classes pursuant to provincial legislation.

On July 8, 2021, the Government announced that it planned to amend Bill 35 to legislate three years of annual 2.5% electricity rate increases.

On October 6, 2021, Bill 35 was withdrawn from the Legislative Assembly.

Status Update Motion

The Consumers Coalition, representing residential electricity ratepayers, supported by the Manitoba Industrial Power Users Group, the Assembly of Manitoba Chiefs, and Manitoba Keewatinowi Okimakanak, applied to the Board for a status update hearing to determine whether rates charged by Manitoba Hydro were just and reasonable and whether Manitoba Hydro's costs were fairly allocated among the customer classes. The Consumers Coalition's Status Update Application maintained that, in light of the substantial changes in Manitoba Hydro's circumstances since electricity rates were last adjudicated in Board Orders 59/18 and 69/19, ratepayers need up-to-date information through an independent Board process to determine whether they are paying just and reasonable rates for the essential monopoly electricity service.

Consistent with the process followed by the Board in determining Manitoba Hydro's request in the 2017/18 & 2018/19 General Rate Application for an interim rate increase, by letter of April 1, 2021, the Board requested that Manitoba Hydro and past Interveners of Record provide written submissions on whether the Board should consider the Status Update Application and, if so, what the process should be. On April 12, 2021, Manitoba Hydro, the Assembly of Manitoba Chiefs, the Manitoba Industrial Power Users Group, and Manitoba Keewatinowi Okimakanak provided written submissions.

In its response to the Board, Manitoba Industrial Power Users Group stated it has consistently held the position that a transparent and independent regulatory process is the best approach to establishing appropriate oversight for Manitoba Hydro. It is critically important for industrial enterprises to have forward-looking information about the level of rates and related risks that they will face today and in the future. Industrial companies use this information to make reasonable inferences about Manitoba's competitive position with respect to energy rates when planning for future long-term production output and capital investment in Manitoba. Manitoba Industrial Power Users Group asserts that the failure of Manitoba Hydro to produce an appropriate long-term financial forecast since 2016 and a lack of transparency regarding the most recent rate and regulatory changes imposed by the legislature, means that industry in Manitoba is presently operating with an unprecedented lack of confidence. According to this Intervener, conditions related to rate competitiveness in Manitoba are opaque and with industry making important decisions regarding capital investment and post-pandemic production scheduling, industrial enterprises are already beginning to direct critical resources elsewhere. If allowed to continue, opportunities for Manitoba-based operations will inevitably be lost. Manitoba Industrial Power Users Group maintains routine and transparent regulation, overseen by an independent regulator, is the only way to achieve ratepayer confidence.

On April 19, 2021, the Consumers Coalition provided written Reply submissions to the Board.

On May 10, 2021, in Order 53/21 and in response to the Consumers Coalition's Motion before the Board, additional procedures were ordered to assist the Board in examining:

a) whether current Manitoba Hydro rates were just and reasonable and costs were fairly allocated among customer classes;
b) unfinished business from Order 69/19 in terms of the Major Capital Projects Deferral Account that was established to protect future Manitoba Hydro ratepayers from rate shock; and
c) other unfinished directives in Orders 59/18 and 69/19.

In Order 53/21, the Board also directed Manitoba Hydro to provide financial, operational, capital expenditure, hydrology, and cost of service information (which was then currently in existence and in use in the operations and management of Manitoba Hydro).

On June 18, 2021, the Board requested submissions from parties with respect to Manitoba Hydro's response to Order 53/21. On June 24, in its submission, Manitoba Industrial Power Users Group stated that under the Government's Bill 35 framework Manitoba industrial ratepayers can take no comfort that they are paying rates that are likely to be stable, predictable, and at the lowest reasonable level. This Intervener submitted rates that are too low will harm ratepayers if rates are held too low for too long, necessitating large future rate increases that will drive rate instability.

On August 17, 2021, the Board issued Order 89/21 directing a Status Update Proceeding and for Manitoba Hydro to provide evidence to assist the Board in its determination of whether Manitoba Hydro's rates were just and reasonable and its costs were fairly allocated among the various customer classes.

On September 9, 2021, the Board proposed certain Minimum Filing Requirements for the Status Update Proceeding for comment by Manitoba Hydro.

Interim Rate Application

On September 22, 2021, the Minister of Crown Services issued a Ministerial Directive to the Manitoba Hydro-Electric Board providing specific instruction for Manitoba Hydro to take all steps necessary to proceed with an interim rate application to this Board for the 2021/22 fiscal year, as well as directing Manitoba Hydro to engage with the Board on the timing and parameters of Manitoba Hydro's next multi-year General Rate Application.

On September 29, 2021, Manitoba Hydro advised the Board that it intended to file an interim rate application to address the financial impacts due to the current drought conditions to ensure the financial health of Manitoba Hydro. On that date, Manitoba Hydro advised the Board that Manitoba Hydro would be including in its Interim Application responses to the Minimum Filing Requirements that were issued as part of the Status Update Proceeding.

On October 12, 2021, recognizing Manitoba Hydro would be seeking urgent approval from its Board of Directors to file a 2021/22 Interim Rate Application with the Board, this Board suspended the Status Update Proceeding initially commenced by the Consumers Coalition. The Board suspended the Status Update Proceeding until November 3, 2021, pending Manitoba Hydro filing its interim rate application.

The Board's October 12, 2021 Decision Letter, with the noted support of Manitoba Hydro, approved Intervener status in Manitoba Hydro's Interim Application for the Assembly of Manitoba Chiefs, the Consumers Coalition, Manitoba Industrial Power Users Group, and Manitoba Keewatinowi Okimakanak.

Additionally, as indicated in the Board's October 12, 2021 Decision Letter, the longstanding use of Minimum Filing Requirements assists in the efficient and focused filing of complete rate increase applications by Manitoba Hydro and reduces subsequent written information requests. Interveners were invited to submit, for Board approval, their proposed Minimum Filing Requirements for Manitoba Hydro to include in its interim rate application.

On October 13, 2021, Manitoba Hydro requested an extension of the Board's deadline to file an interim rate application until November 15, 2021 in order to prepare a complete application including the Minimum Filing Requirements.

On October 19, 2021, the Board granted Manitoba Hydro's request for an extension to file the interim rate application, citing Manitoba Hydro's explanation that November 15 is the earliest date by which Manitoba Hydro would be able to receive approval from its Board of Directors.

With its October 19, 2021 letter, and after hearing from Interveners, the Board approved the list of Minimum Filing Requirements for Manitoba Hydro to include in its Interim Application. The Board also invited Manitoba Hydro and approved Interveners to submit process options for the public review and the Board's adjudication of the Interim Application.

On October 22, 2021, the Board received submissions from Manitoba Hydro, the Consumers Coalition, and Manitoba Industrial Power Users Group as to various process options that could be used related to Manitoba Hydro's matters before the Board, including the expected Interim Application.

On November 15, 2021, Manitoba Hydro filed its Interim Application with the Board seeking an Order of the Board for the following:

a) Approval, on an interim basis, of rate schedules incorporating an overall increase in General Consumers Revenue of 5.0% effective January 1, 2022. The requested rate increase would generate $27 million in the remaining three months of fiscal 2021/22 and $88 million on an annualized basis. To generate that additional revenue, Manitoba Hydro proposed rate increases differentiated by customer class; and

b) Approval to begin recognizing the revenues from the Major Capital Projects Deferral Account, established by the Board in Order 69/19, commencing on January 1, 2022 with the balance to be amortized over 24 months.

On November 25, 2021, Interveners filed, for Board approval, proposed written information requests of Manitoba Hydro.

On November 26, 2021, the Board forwarded the approved information requests to Manitoba Hydro.

In advance of the commencement of the hearing, the Board received 64 written comments from ratepayers expressing concerns with the rate increase proposed in the Interim Application.

On December 1, 2021, the Board heard oral public presentations from:

- Bannerman Green Housing Co-op Inc.
- Gerdau Long Steel North America – Manitoba Mill
- Electrochem, a Division of Chemtrade Logistics Inc.
- Interchurch Council on Hydropower

In its presentation, Bannerman Green Housing Co-op Inc. explained that for Manitoba to reach its net zero carbon emissions targets, Manitoba Hydro should offer feed-in tariffs to encourage the development of local sources of carbon-free electricity generation. Feed-in tariffs provide a price for power, which is above the wholesale price, to private power generators to encourage the establishment of renewable power generation facilities.

In its presentation, Gerdau Long Steel North America – Manitoba Mill ("Gerdau") stated that the cost competitiveness of its Manitoba mill has eroded to the point where electricity, its third-largest variable cost, is now greater than the overall average of its North American mills. Gerdau's Manitoba plant must compete internationally both with its competitors but also within Gerdau's family of plants. Gerdau stated that the cost advantage of the

Manitoba plant with respect to electricity costs is eroding, which threatens capital expenditures and potential plant expansions. Gerdau is looking for stability and predictability of rates through a transparent public process.

In its presentation, Electrochem, a Division of Chemtrade Logistics Inc., stated that it understands the need for Manitoba Hydro to raise rates to remain a viable entity, but expressed its concern that the need for those rate increases should be transparent. Increasing electricity rates over the past several years have reduced the competitive cost advantage of its Brandon plant. If the trend continues, it will mean reduced capital investment in the Brandon plant and the shifting of production to other plants outside of Manitoba.

The Interchurch Council on Hydropower (“Council”) is an advocacy group for northern Manitoba communities that have been affected by hydroelectric development. The Council expressed its concern about the impact of the proposed electricity rate increase on First Nations, especially following the elimination of the First Nations On-Reserve Residential customer class in 2020. The Council requested that Manitoba Hydro develop an alternative solution to protect First Nations customers in hydro-affected communities from the negative effects of the proposed rate increase.

On December 3, 2021, Manitoba Hydro filed its written responses to the Board-approved information requests.

On December 10 and 13, 2021, the Board heard oral testimony by Manitoba Hydro witnesses, including its President & Chief Executive Officer and its Vice President & Chief Financial Officer.

On December 14 and 15, 2021, the Board heard oral closing submissions.

On December 16, 2021, Manitoba Hydro filed its written Reply to the Interveners’ closing submissions.

On December 24, 2021, the Board issued Order 137/21 which varied Manitoba Hydro's requested 5% increase to instead approve a 3.6% increase in General Consumers Revenue. That additional revenue will be realized through new consumer rates that remain in effect only until November 15, 2022 – which date has now been varied in this Order to November 30, 2022 – unless Manitoba Hydro files a General Rate Application by November 15, 2022 seeking rates for 2022/23, and for 2023/24 if it so chooses, and to confirm the 2021/22 interim rate increases.

Order 137/21 also directed that the 3.6% revenue increase was to be recovered from rate increases that are differentiated by customer class. The Board also varied Manitoba Hydro's request to begin recognizing the balance in the Major Capital Projects Deferral Account into its revenue over a period of 24 months. The revenues from the 2.5% rate increase approved in Order 69/19 and 73/19 that were being deferred may now be recognized beginning January 1, 2022; however, the timing of the recognition of the previously deferred revenues will be decided at the 2022/23 General Rate Application.

On December 31, 2021, the Board issued Order 140/21 which approved the specific interim rate schedules applicable to each Manitoba Hydro customer class.

This Order contains the substantive and more detailed reasons for the Board's decisions in Order 137/21 related to Manitoba Hydro's Interim Application.

3.0 2021/22 Drought

One of the most significant reasons for Manitoba Hydro bringing its Interim Application to the Board was the drought experienced in 2021/22. Manitoba Hydro filed evidence explaining how the drought unfolded and how Manitoba Hydro updated its forecasts of water flow conditions, hydraulic generation, and Net Extraprovincial Revenue. The following section details the evidence provided by Manitoba Hydro in the course of the Interim Application hearing.

Drought Conditions

In 2020, Manitoba Hydro prepared its financial operating Budget for its fiscal 2021/22 year, which commenced April 1, 2021. Manitoba Hydro stated that the Budget was prepared based on the financial average of the most recent 40 years of water flow data in Manitoba Hydro's hydrological history. Manitoba Hydro calculated the average of the financial results of the energy revenues and costs from each of the 40 years of water flow data, assuming that Manitoba Hydro's current fleet of generating stations was in existence for each of the 40 years of water flows.

Manitoba Hydro's 2021/22 Budget was based on water storage conditions as of November 2020, assuming inflows would transition to a range of possible inflow scenarios in 2021/22 based on the recent 40 years of historic hydrology.

In addition to monitoring its financial position, Manitoba Hydro noted that it continuously monitors its hydrological situation. Until mid-summer 2020, the primary focus of Manitoba Hydro's reservoir operations was on managing high inflows at various locations across the system. By mid-August, Lake Winnipeg water levels receded below the licence flood reduction threshold level of 715 feet, allowing Manitoba Hydro to reduce outflows and alleviate flooding conditions on the Lower Nelson River. At the same time, Manitoba Hydro managed outflows from its reservoirs for economic reasons. This means Manitoba Hydro planned reservoir releases to optimize Net Extraprovincial Revenue assuming a range of possible flow conditions that could occur in the future.

Winnipeg River basin precipitation had been well below normal since the fall of 2019. Despite this, overall system inflows were above average and storage levels were near normal heading into winter 2020/21.

Following a below average snowmelt runoff in the south and in anticipation of above average snowmelt runoff in northern tributaries, in April 2021 Manitoba Hydro reduced Lake Winnipeg outflows from near median to below lower quartile flows for that time of year. These Lake Winnipeg outflow reductions resulted in reduced summer opportunity exports and required increased imports relative to the 2021/22 Budget.

In May 2021, Manitoba Hydro projected that total hydraulic generation would be below the 2021/22 Budget, assuming normal precipitation for the remainder of that fiscal year.

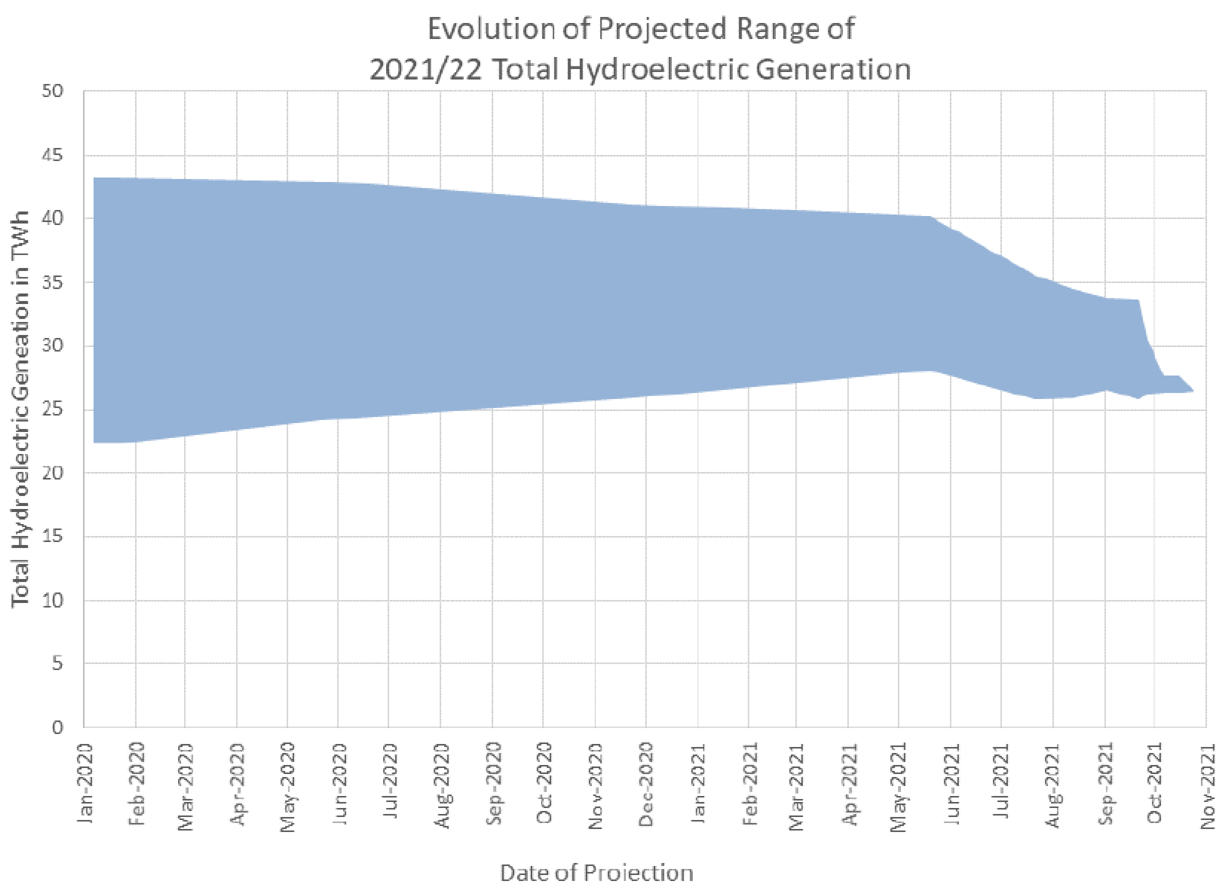
As dry conditions persisted and expanded across southern portions of the Nelson River Basin through early summer 2021, Manitoba Hydro stated that its operations transitioned from a regime governed by economic conservation, with reduced opportunity exports, to being governed by energy reliability. Manitoba Hydro considered it necessary to restrict the release of water from reservoirs to ensure energy reliability. Manitoba Hydro sought to ensure firm electricity demands by Manitobans and firm export customers could be met assuming the drought conditions persisted for the remainder of the fiscal year, above normal winter loads in winter 2021/22, followed by severe drought and above normal winter loads in 2022/23.

By mid-September 2021, it was apparent to Manitoba Hydro that a recovery to average or above average water flows was increasingly unlikely. Precipitation was well below average and below the levels experienced during the 2002 and 2003 drought. Accordingly, the range of potential future flow scenarios was narrowed in September 2021 to a subset of 10 of the 40 historic flow years.

By early October, due to continued dry conditions and unfavourable precipitation forecasts, Manitoba Hydro further reduced the subset of 10 plausible 2021/22 future water flow scenarios down to four.

By late October 2021, there was very low potential for additional precipitation along with an expectation that additional precipitation would fall as snow and not be available for hydraulic generation until the spring of 2022. Accordingly, the expected range of flows narrowed further for the remainder of the 2021/22 fiscal year, effectively leaving a single water flow scenario which was utilized in Manitoba Hydro's financial analysis. With the additional certainty in the water flows, Manitoba Hydro had additional certainty in the amount of hydraulic generation and in electricity export and import purchase volumes for the remainder of the 2021/22 fiscal year. This additional certainty informed the updated financial forecast for 2021/22 which was filed with the Board as part of this Interim Application.

The figure below shows the evolution of the range of projected hydraulic generation as drought conditions worsened through the summer and fall of 2021, showing the range of potential water flow scenarios narrowing from 40 possible flow conditions to only one.



Source: Manitoba Hydro's Interim Application page 20

Looking forward, and given the 2021 drought conditions, Manitoba Hydro indicates there is an elevated likelihood of below average inflows occurring in 2022/23. Manitoba Hydro does not forecast drought more than a few months into the future using short-term antecedent regression forecasting techniques. As a result, Manitoba Hydro advises that because annual hydraulic generation is very dependent on spring and summer rainfall and given the long lead time through to the end of 2022/23, Manitoba Hydro is not able to quantify the increase in likelihood of drought occurring next year.

Water Flow Forecasting

Manitoba Hydro has a hydrological record of water flows and water levels dating back to approximately 1912. While having previously utilized this full record of water flow data, Manitoba Hydro has, in preparing its budgets since the 2020/21 budget, restricted its hydraulic analysis to the most recent 40 years only. According to Manitoba Hydro's evidence, the most recent 40 years of water flow data provide better forecasts of its operations and financial results than the longer hydrological record. The most recent 40 year flow records have daily, instead of monthly, measurements. There are now 41 locations where Manitoba Hydro obtains flow data compared to 16 from the longer-term record.

Manitoba Hydro states that it does not rely on medium or long-term precipitation forecasts. Manitoba Hydro states that it cannot predict the amount or the location of precipitation with any accuracy. Manitoba Hydro uses antecedent, or historical, water flow forecasting and regression techniques to help inform the forecast for the upcoming months. However, these techniques lose accuracy further into the future and do not provide reliable long-term forecasts of water flows. Manitoba Hydro states that it has been adding new tools to improve inflow forecasting and system modelling for operations planning. These new tools rely on the more detailed water flow records contained in the recent 40 year flow record.

With respect to whether there will be a drought in 2022/23, Manitoba Hydro states that there is a higher probability of lower water flow conditions in the year following a low water year. Manitoba Hydro referenced a report from ICF International Inc. provided to Manitoba Hydro in 2011 which stated that there is a strong correlation of water flow conditions from year to year.

Net Extraprovincial Revenue

Manitoba Hydro relies on its 2021/22 Financial Forecast, approved by the Manitoba Hydro Board of Directors on November 10, 2021, to assert that the current drought conditions have severely and negatively affected its financial health. At the public hearing, Manitoba Hydro presented evidence that drought conditions have reduced projected Net Extraprovincial Revenue by $398 million in fiscal 2021/22 compared to the 2021/22 Budget.

Net Extraprovincial Revenue comprises electricity export revenues minus Fuel & Power Purchases (i.e. electricity imports) minus Water Rentals & Assessments. The projected $398 million reduction in Net Extraprovincial Revenue is a result of a reduction in dependable export sales ($46 million), a reduction in opportunity export sales ($122 million), an increase in opportunity import purchases ($262 million), with a small offset in the level of water rental fees ($32 million) as shown on the table below.

Net Extraprovincial Revenue
($ Millions)

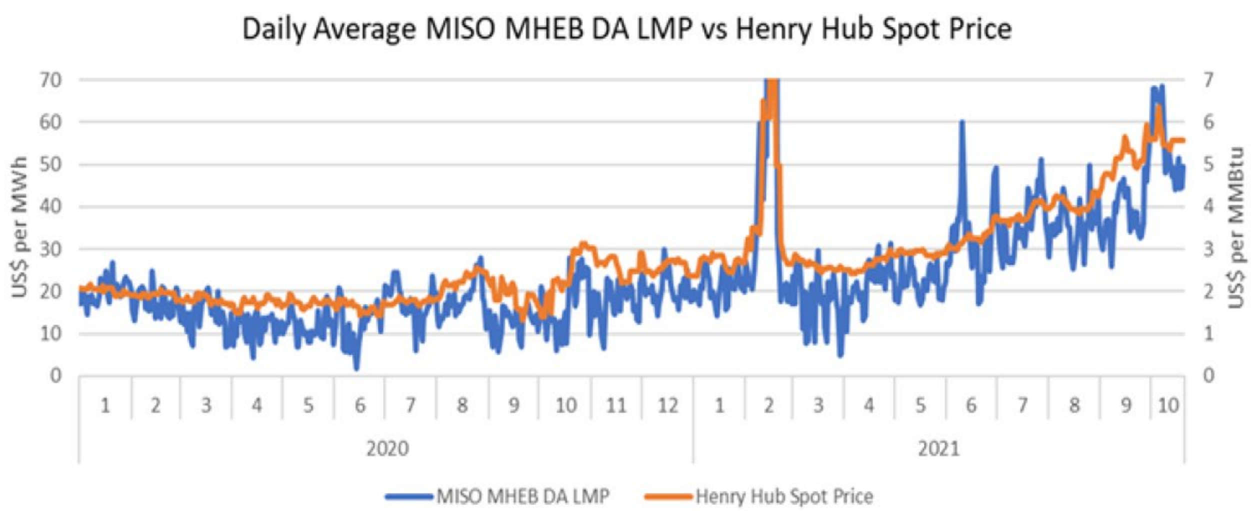
	2021/22 Budget	2021/22 Forecast	Difference
Extraprovincial Revenues			
Dependable Export	590	544	(46)
Opportunity Export	210	88	(122)
Transmission Credits	3	3	(0)
Other Export Revenue	2	2	(0)
Total Extraprovincial Revenue	806	637	(168)
Fuel & Power Purchased			
Dependable Purchases	73	73	1
Opportunity Import Purchases	9	272	262
Thermal Costs	6	6	(0)
GNTL Charges	39	39	(1)
Transmission Charges	37	38	1
Other Import Costs	0	(0)	(0)
Total Fuel & Power Purchased	**166**	**428**	**262**
Water Rentals & Assessments			
Water Rentals	120	88	(32)
Assessments & Other	11	10	(0)
Total Water Rentals & Assessments	**131**	**98**	**(32)**
Net Extraprovincial Revenue	**509**	**111**	**(398)**

Source: Manitoba Hydro's Interim Application page 18

Notably, the $262 million of increased opportunity, or spot market, purchases is a result of not only increased volumes of import purchases, but also increased energy market prices. Energy market prices have increased substantially from the summer through the fall of 2021. Actual Midcontinent Independent System Operator ("MISO") market prices had increased by approximately 40% from August 2021 to October 2021, as shown by the blue line in the graph below. The MISO market is Manitoba Hydro's primary export market located in the Midwest United States with a northern region that includes North

Dakota, Minnesota, Wisconsin, Michigan, Iowa, Illinois, and Indiana. Increased energy market prices are not a trend localized to the MISO market, as increases in worldwide demand have put pressure on available energy supplies.

Following the short-term price spike in early 2021 due to generation outages in Texas and neighbouring states caused by cold weather, both actual MISO market prices as well as natural gas market prices (as represented by the Henry Hub Louisiana[1] spot price shown by the orange line in the graph below) have been increasing at a similar pace in the rising energy price environment as shown in the graph below:



Source: Manitoba Hydro's Interim Application page 15

2021/22 Financial Forecast

The $398 million reduction in Net Extraprovincial Revenue is the primary driver behind a negative swing of $366 million in projected operating results, from Net Income of $177 million in the 2021/22 Budget to a net loss of $190 million in 2021/22 Forecast as shown in the table below:

[1] Henry Hub is a pricing hub for natural gas futures contracts, including for contracts traded on the New York Mercantile Exchange (NYMEX).

ELECTRIC OPERATIONS
OPERATING STATEMENT
(In Millions Of Dollars)

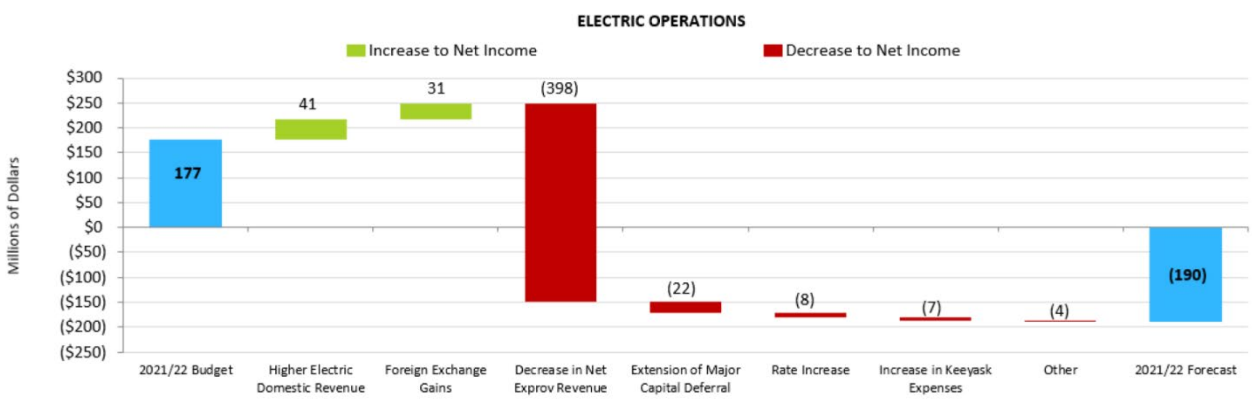
	2021/22 Budget	2021/22 Forecast
Revenue		
Domestic Revenue		
At Approved Rates	1,751	1,792
Additional (from rate increase)	35	**27**
Extraprovincial	806	637
Other	29	29
	2,620	2,485
Expenses		
Operating And Administrative	557	557
Net Finance Expense	1,019	994
Depreciation And Amortization	583	579
Water Rentals And Assessments	131	98
Fuel And Power Purchased	166	428
Capital And Other Taxes	154	152
Other Expenses	77	87
Corporate Allocation	8	8
	2,694	2,902
Net Income Before Net Movement In Regulatory Deferral	(74)	(417)
Net Movement In Regulatory Deferral	234	214
Net Income	160	(203)
Net Income Attributable To:		
Manitoba Hydro	**177**	**(190)**
Non-Controlling Interests	(16)	(13)
	160	(203)
Proposed Percent Increase	3.50%	5.00%

Source: Manitoba Hydro’s Minimum Filing Requirement #3

As seen in the table above, in its 2021/22 Budget, Manitoba Hydro projected Net Income of $177 million for its Electric Operations, assuming average financial results of its projected water flow conditions and a projected general revenue increase of 3.5% effective October 1, 2021.

Manitoba Hydro's updated 2021/22 Forecast in the table above, which incorporates actual financial results to the end of September 2021, water conditions to October 20, 2021, and updated forecast assumptions, projects a $190 million net loss in 2021/22, assuming a 5.0% overall general revenue increase effective January 1, 2022. The $190 million net operating loss assumes $27 million of additional revenues from the January 1, 2022 rate increase designed to raise General Consumers Revenues by 5%.

A further illustration of the primary factors resulting in the projected $366 million reduction in Manitoba Hydro's 2021/22 Forecast Net Income is shown in the graph below:



Source: Manitoba Hydro's Interim Application page 33

The most significant factor driving the change in 2021/22 Forecast Net Income compared to the original 2021/22 Budget Net Income is the $398 million reduction in Net Extraprovincial Revenue. The other factors driving the change in the 2021/22 Forecast financial results as shown in the above graph include:

Increases to Forecast Net Income:

- Electric domestic revenue is higher by $41 million primarily due to lower projected impacts of COVID-19 on Top Consumers revenues along with favourable weather and higher actual usage (up to September 2021) than budgeted.
- There are $31 million in foreign exchange gains on finance expense due to the strengthening Canadian dollar from a CAD-USD exchange rate of 1.32 in the 2021/22 Budget to 1.22 in the 2021/22 Forecast, which offsets $17 million of foreign exchange losses in the export market.

Decreases to Forecast Net Income:

- The 2021/22 Budget assumed that amortization of the funds in the Major Capital Projects Deferral Account would commence October 1, 2021. The 2021/22 Forecast now assumes amortization of this account will commence January 1, 2022. This results in $12 million of additional revenues being allocated to the deferral account by extending the funding of this account by three months to December 31, 2021, and $10 million less revenue recognized in 2021/22 due to the delay in commencing the amortization of the balance to January 1, 2022, for a $22 million total decrease to Net Income.
- The 2021/22 Budget assumed a 3.5% general revenue increase effective October 1, 2021, while the 2021/22 Forecast assumes a 5.0% general revenue increase effective January 1, 2022. This results in $16 million less revenue from the change in the proposed implementation date of the assumed electric general revenue increase, partially offset by an additional 1.5% rate increase or $8 million in general revenue for an $8 million net decrease to Net Income.
- The $7 million increase in Keeyask expenses (and decrease in Manitoba Hydro's Net Income) is primarily due to earlier recognition of interest on Keeyask Cree Nation loans and a timing difference associated with in-service dates of Keeyask Generating Station units. The 2021/22 Budget assumed the first unit would be placed in service March 31, 2021. It was actually placed in service in February

2021. These increases are partially offset by lower depreciation from refining the componentization of Keeyask assets resulting in a lower composite depreciation rate and later than expected project spending.

4.0 Manitoba Hydro's Response to Drought and 2021/22 Financial Forecast

As identified in Order 137/21, the most significant factor driving the change in Manitoba Hydro's 2021/22 financial position is the $398 million reduction in Net Extraprovincial Revenue. This revenue reduction is the result of a decrease in dependable and opportunity export sales, as well as an increase in opportunity import purchases, both resulting from lower hydraulic generation due to drought conditions.

In its Interim Application and in response to written information requests, Manitoba Hydro explained the steps it took to address the drought and the financial effects arising from the drought.

Transition of Operations From Economics to Reliability

Manitoba Hydro Position

As explained above in Section 3.0, when dry conditions persisted and expanded across southern portions of the Nelson River Basin through early summer 2021, Manitoba Hydro's operations transitioned from economic conservation, with reduced opportunity exports, to being governed by energy reliability.

Manitoba Hydro stated that it transitioned to governing its reservoir operations for energy reliability in order to protect its ability to serve Manitoba customers in the winters of 2021/22 and 2022/23, even if these are colder than normal winters with higher electricity demand, and if the drought persists into 2022/23.

Intervener Positions

Manitoba Industrial Power Users Group stated that in light of the information available in this interim proceeding, no concerns have been noted with regard to Manitoba Hydro's physical management of the water reservoirs and the export market transactions.

Board Findings

The Board accepts Manitoba Hydro's account of how it managed the drought from a reservoir operation perspective. The Board will inquire further of Manitoba Hydro on this topic at the next General Rate Application to demonstrate on the public record whether Manitoba Hydro made and continues to make prudent decisions with respect to the management of its water reservoirs.

Hedging

In response to the drought and to mitigate the price risk on energy imports required to address its reduced hydraulic generation, Manitoba Hydro implemented a price hedging strategy.

Hedging involves Manitoba Hydro entering fixed-price purchase arrangements to reduce the price risk for its future projected import requirements. These fixed-price arrangements allow Manitoba Hydro to lock in purchase prices and "hedge" against the risk of increased energy market prices. Manitoba Hydro substantially hedged its projected imports for the November 2021 to March 2022 timeframe and entered into arrangements for fixed-price firm delivered natural gas supply for electricity generation purposes.

The results of these hedging arrangements will not be known until after the respective months of hedging activity are financially settled.

Manitoba Hydro Position

Manitoba Hydro considers water conditions as an imposed risk, which Manitoba Hydro defines as a risk that originates from an uncontrollable and unavoidable external factor which it is not possible to accurately predict, and which Manitoba Hydro stated that it cannot mitigate. However, price risk associated with drought can be mitigated to a certain extent. Manitoba Hydro implemented a hedging strategy to mitigate its price risk associated with projected energy imports based on the amount of energy imports required to address the reduced hydraulic generation and rising energy market prices due to high demand globally for electricity and natural gas.

Manitoba Hydro's objective with placing financial hedges was to protect against the price risk from adverse movement in the energy markets and the impact this would have on Manitoba Hydro's Net Income.

Manitoba Hydro requested that the hedging details be kept confidential and proposed that only the Board, its Staff, and its Advisors be granted access to this commercially sensitive information.

Intervener Positions

The Board did not grant Interveners access to the commercially sensitive hedging information. Accordingly, the Interveners took no position on the merits of Manitoba Hydro's individual hedging transactions. However, the Assembly of Manitoba Chiefs submitted that there is a cost to Manitoba Hydro's customers for the hedging even though it is unknown until after the hedges settle. This Intervener raised the concern that Manitoba Hydro placed hedges when future prices were high and therefore exposed ratepayers to unnecessary risks when the electricity prices for the hedged months later dropped in October and November.

Board Findings

As detailed in Order 128/21, the Board reviewed the unredacted copies of Manitoba Hydro's Appendix 2 and its response to the Board's Minimum Filing Requirement 11, which were filed in confidence with the Board and provided information on Manitoba Hydro's hedging activities. In Order 128/21, the Board found that information, if publicly disclosed, could reasonably be expected to significantly harm Manitoba Hydro's competitive positions. The Board further found that the interest in maintaining confidentiality over Appendix 2 and Minimum Filing Requirement 11 outweighed the public interest in the disclosure of that information. Therefore, the Board received this information in confidence in accordance with the Board's Rules of Practice and Procedure.

While the Board finds, on a prima facie basis, the hedging strategy to be reasonable, this topic will be further examined, along with the Manitoba Hydro's actions to respond to the drought, at the 2022/23 General Rate Application when Manitoba Hydro seeks to finalize the 2021/22 interim rates.

Business Operations Capital Expenditures

Manitoba Hydro's Business Operations Capital expenditures are investments in assets made to address the needs of its customers, including to:

- connect new customers,
- increase the capacity of its transmission and distribution networks due to ongoing load growth,
- sustain aging assets through renewal, efficiency improvements, or to comply with mandatory external requirements, and
- support business operations.

Manitoba Hydro forecasted $526 million of Business Operations Capital expenditures in its 2021/22 Budget. Manitoba Hydro updated this in its 2021/22 Forecast to $523 million with an additional $545 million of Business Operations Capital for 2022/23.

Manitoba Hydro Position

Manitoba Hydro estimates there to be approximately 3,000 business operations capital projects and programs. Of these, Manitoba Hydro estimates 90% are ‘in-flight’, meaning some are in the scoping phase, some in the design phase, and some in the actual construction or implementation phase. Because these capital expenditures are in-flight, Manitoba Hydro has not postponed nor cancelled any of them to ease cash flow problems during the drought. Instead, Manitoba Hydro has borrowed $348 million to fund its operations, including its Business Operations Capital spending.

Manitoba Hydro explained that it did not, and has no plans to, reduce its Business Operations Capital spending in 2021/22 to mitigate the financial impacts of the 2021/22 drought.

Manitoba Hydro maintains that deferring annual capital spending will generally erode value by increasing risks associated with aging assets, increasing costs associated with remediation of those risks, decreasing asset reliability, or some combination of the three.

According to Manitoba Hydro, the impacts of deferral of annual capital spending will ultimately negatively affect customers through decreased reliability and increased costs for Manitoba Hydro that will need to be passed on to customers.

Intervener Positions

According to the Consumers Coalition, Manitoba Hydro has not managed the financial impacts of the drought appropriately, as it has not reduced its 2021/22 Business Operations Capital spending.

According to this Intervener, Manitoba Hydro's actions are inconsistent with what it said it would do in the face of a drought at the 2014 Needs For and Alternatives To Manitoba Hydro's Preferred Development Plan ("NFAT") public proceeding. At that proceeding, Manitoba Hydro sought approval to proceed with the Keeyask Generating Station, the Manitoba-Minnesota Transmission Project, and the Great Northern Transmission Line.

The Consumers Coalition referenced Manitoba Hydro's statements from the NFAT proceeding with respect to how Manitoba Hydro said it would maintain sufficient cash flows in the event of a drought:

> *And so during a severe prolonged drought, Manitoba Hydro will -- would provide sufficient cashflows for the continuity of business operations. I mean, we're going to continue to have business as usual for Manitoba Hydro. That's what happened in '03/'04. And Manitoba Hydro's debt will remain to be self-supporting.*
>
> *So what measures would we undertake? There's three (3) measures, and we would use them in some combination of -- and we talk about it generally here, but the first one is cash conservation. So Manitoba Hydro would curtail or delay its operating and capital expenditures as required and as appropriate. And in severe circumstances, this may include exercising the optionality available within the development plans. But our first approach would be to see what can we do, just -- and as any homeowner, any person would do when faced with a situation, we would see what can we do maybe not to have as many cash outflows. And we would certainly and we would do that, and we have done it and we would continue to do that.*

The Consumers Coalition also referenced findings from Board Order 59/18:

> *…while in a period of major capital spending on Keeyask and Bipole III, Manitoba Hydro should find savings in Business Operations Capital.*

The Consumers Coalition submits that Manitoba Hydro's failure to prioritize its Business Operations Capital amounts to an implicit rejection of prior Board findings on cost control and is contrary to what Manitoba Hydro told the Board at the NFAT proceeding.

The Consumers Coalition recommends that Business Operations Capital be reduced by at least $55 million, which comprises the 10% of projects that are not in-flight (i.e. have not commenced). This Intervener acknowledges this reduced spending will have minimal impact on Manitoba Hydro's Net Income but such reduced spending improves core cash flow by $55 million.

Manitoba Industrial Power Users Group submits that Manitoba Hydro has repeatedly indicated that it could not make further cuts without causing increased risk in asset failure and without affecting the ability to provide “safe and reliable energy”. However, when directed by the Province to find savings, Manitoba Hydro found ways to contain operating costs and capital costs.

This Intervener is concerned that Manitoba Hydro is now planning to undo much of its prior cost containment by increasing spending on additional capital projects. Manitoba Industrial Power Users Group questions what Manitoba Hydro is considering as cost cutting measures, if any, at all.

Manitoba Industrial Power Users Group maintains that absent strong Board direction, the vague statements by Manitoba Hydro that it will look into additional savings do not bind or incent Manitoba Hydro to implement any cost cutting measures at all.

Board Findings

The Board finds that with less than three months remaining in the fiscal year, Manitoba Hydro may be too late in 2021/22 to achieve significant savings in Business Operations Capital spending. With the concerns expressed by Manitoba Hydro over its cash flow shortfall in 2021/22, it appears Manitoba Hydro missed an opportunity to preserve some of its cash flow earlier in the year by postponing or reducing its spending on Business Operations Capital.

If the drought continues and Manitoba Hydro's cash flow concerns continue next year, the Board finds that Manitoba Hydro shall seek savings in its Business Operations Capital, just as it committed to do at the NFAT proceeding when it explained how it would confront financial liquidity concerns related to drought. The Board will consider Manitoba Hydro's steps to reduce its Business Operations Capital at the next General Rate Application. While the Board does not have the legal jurisdiction to approve specific capital projects or order Manitoba Hydro to reduce its capital spending, it will consider Manitoba Hydro's efforts to control costs (including operating statement costs from new Business Operations Capital) when adjudicating rate increases. The Board directs Manitoba Hydro to demonstrate the savings in Business Operations Capital that are found by showing the updated Business Operations Capital spending compared to the spending proposed at this interim proceeding. Manitoba Hydro should be planning for the drought to continue and it must therefore control its Business Operations Capital spending to address the financial impacts of a continuing drought. However, Manitoba Hydro is to seek these savings regardless of whether the water conditions recover and the drought ends.

Operating & Administrative Expenses

Operating & Administrative ("O&A") expenses are comprised primarily of labour and benefits, material, contracted services, and overhead costs associated with operating and maintaining all of Manitoba Hydro's facilities and providing service to its customers. Employee labour and benefits are the most significant components of O&A expenses.

Manitoba Hydro points out that in 2021 the Manitoba Labour Board awarded general wage increases to employees represented by the International Brotherhood of Electrical Workers totalling 3.5% which has an ongoing impact on Manitoba Hydro's O&A expenses. Additionally, Manitoba Hydro identifies inflationary pressures on its non-salary related O&A expenses, environmental monitoring of Keeyask Generating Station, zebra mussel treatment for its generating stations and control structures, and increased fleet vehicle costs as upward pressures on O&A costs.

In response to the COVID-19 pandemic, Manitoba Hydro incurred incremental O&A costs totalling $6.1 million in 2020/21 and $1.4 million from April 1 through September 30, 2021 related to: the mobilization of a backup control centre, additional cleaning measures required for corporate facilities, the purchase of personal protective equipment for staff, as well as the costs to implement social distancing protocols in motor vehicles.

In addition, a government-directed cost savings initiative contained two components related to O&A expenses: workforce reductions and non-salary operating reductions. Workforce reductions reduced O&A expenses by $19 million (net of capitalization) and non-salary operating reductions totalled $35 million.

Manitoba Hydro's COVID-19 savings commitment to Government was $86.2 million, of which $26.2 million related to O&A and $60 million related primarily to Other Capitalized Expenditures, including Efficiency Manitoba programs and Business Operations Capital spending.

Manitoba Hydro Position

Manitoba Hydro did not reduce its 2021/22 O&A expenses in response to the drought. Manitoba Hydro stated that its O&A expenses from 2016/17 to 2022/23 have grown at an annual rate of 1.75%, which is aligned with the change in the Consumers Price Index ("CPI") over the same period of 1.73%.

Manitoba Hydro defended its decision by identifying the CPI-aligned growth in O&A expenses and the additional expenses beyond Manitoba Hydro's control. As major capital projects wind down and are completed, the salaries of employees previously working on these projects are no longer capitalized and instead form part of the O&A expenses. Manitoba Hydro further states that the number of Full Time Equivalent ("FTE") employees is the lowest since the acquisition of Winnipeg Hydro in 2002 but that this level of FTEs is not sustainable. Manitoba Hydro considered the reductions in FTEs to be a short-term, temporary situation to address the pandemic. Manitoba Hydro maintains that with the winding down of major capital projects, O&A costs are increasing as there is a shift from resources working on construction activities, focused mainly on hydro-electric and transmission development, to operating activities in support of Strategy 2040 and building up the capability to meet the evolving energy landscape.

Intervener Positions

According to the Consumers Coalition, Manitoba Hydro has not managed the financial impacts of the drought appropriately, as it has not reduced its O&A expenses. Similar to the Consumers Coalition's observations of Manitoba Hydro's statements at the 2014 NFAT public proceeding with respect to how Manitoba Hydro would reduce its expenditures in response to drought conditions, the Consumers Coalition noted that Manitoba Hydro has not reduced its O&A expenses in response to the 2021/22 drought.

Instead of reducing O&A, this Intervener calculated Manitoba Hydro has increased its O&A spending by 4.3% from 2019/20 to 2020/21 and is projecting a cumulative increase from 2019/20 to 2022/23 of 16.2% (i.e. 5.4% per year on average).

Manitoba Industrial Power Users Group had the same concerns with Manitoba Hydro's O&A expenses as noted above for Manitoba Hydro's Business Operations Capital expenditures. Manitoba Industrial Power Users Group stated that Manitoba Hydro is now proposing to undo much of this cost containment and increase spending on additional FTEs. Given that the budget increasing the FTEs has been approved by the Manitoba Hydro Board of Directors, Manitoba Industrial Power Users Group questions the O&A cost-cutting measures that Manitoba Hydro is considering and whether Manitoba Hydro is considering cost-cutting measures at all.

Board Findings

The Board finds the position of Manitoba Hydro previously expressed at the NFAT proceeding has changed with respect to addressing the financial impacts of drought. If the drought continues and Manitoba Hydro's cash flow concerns continue next year, the

Board finds that Manitoba Hydro shall seek savings in its O&A expenses in order to confront liquidity concerns related to drought.

Manitoba Hydro stated that its O&A expenses are not easily adjusted in response to the drought as they are made up primarily of employee wages, salaries, and benefits. The Board notes that Manitoba Hydro was able to adjust its O&A expenses relatively quickly in response to the directive from the provincial Government to do so in light of the pandemic. The Board also finds that as major capital projects wound down and were completed, Manitoba Hydro should have planned for the fact that the salaries of employees previously working on these projects would no longer be capitalized and instead form part of the O&A expenses. The Board will consider Manitoba Hydro's steps to reduce its O&A expenses at the next General Rate Application. The Board directs Manitoba Hydro to demonstrate the savings in O&A expenses that are found by showing the updated O&A expenses compared to the O&A expenses proposed in this interim proceeding. Manitoba Hydro should be planning for the drought to continue and it must therefore control its O&A expenses to address the financial impacts of a continuing drought, although Manitoba Hydro is to manage these expenses regardless of whether the water conditions recover and the drought ends.

While compliance with prior Board directives was out of scope of the Interim Application proceeding, the Board notes that there are outstanding directives related to O&A expenses, including Order 58/19 Directives 12 and 13 and Order 69/19 Directive 8. The Board will review Manitoba Hydro's responses to these Directives at the next General Rate Application.

Debt Management

Manitoba Hydro plans to borrow $348 million in 2021/22 to fund its operations, which represents 90% of the projected reduction from previously forecast Net Extraprovincial Revenue.

Manitoba Hydro adjusted its debt portfolio which has reduced its Finance Expense. Manitoba Hydro shifted the forecast term to maturity of new debt issuance for fiscal 2021/22, issuing debt with a weighted average term to maturity ("WATM") of 15.4 years at a weighted average interest rate ("WAIR") of 2.09% year to date (versus a WATM of 37.2 years and a WAIR of 2.15% for debt issued in 2020/21). As a result, the weighted average term to maturity for Manitoba Hydro's entire debt portfolio is 19.4 years with a weighted average interest rate of 3.4% (including the provincial debt guarantee fee). Shortening the term to maturity of long-term debt adds refinancing risk to the debt profile earlier than planned. Manitoba Hydro's debt borrowings for the construction of the Keeyask Generating Station are expected to end in 2021/22 as the final generating units will be placed into service this fiscal year.

Manitoba Hydro Position

The annual interest cost on the $348 million of borrowings required in 2021/22 to fund operations is $13 million. Of the 5% proposed revenue increase, 0.8% is necessary just to cover this annual interest cost. Manitoba Hydro cites the current economic environment, where inflation is running high and current forecasts are showing short-term interest rates will be rising in the next fiscal year and beyond, as its reasoning not to employ the strategy of increasing floating rate debt and risk the related rising finance expense in the near term. Manitoba Hydro is, however, anticipating the issuance of a small amount of its own commercial paper.

The strategy to shift the new debt issues to a shorter WATM has benefited Finance Expense, as rates across the yield curve have risen above forecasted levels for the year to date in 2021/22.

Manitoba Hydro states that the increased limit of $1.5 billion for the commercial paper program has not been approved for use, nor guaranteed yet, by the Province of Manitoba.

Intervener Positions

Both Manitoba Industrial Power Users Group and Consumer Coalition note that the cost of the borrowing for operations arising from the drought can be financed with a 0.8% increase in consumer rates.

Manitoba Industrial Power Users Group submits that, by definition, the current debt level is sustainable as all interest is being paid in full every year. By 2022/23, there is no addition of new debt being issued, and there is an effective repayment of debt through a quarter billion dollars in the sinking fund.

This Intervener notes that all interest is being paid from cash receipts, and there remains positive cash from operating activities of $778 million in the approved 2022/23 Plan budget. Furthermore, Manitoba Industrial Power Users Group submits the current debt levels are more than sustainable at current receipts from customers, while acknowledging Manitoba Hydro cannot fully fund interest from internal cash flows as well as pay $250 million into the sinking fund plus spend $886 million on new capital expenditures.

As explained above, Consumers Coalition noted that at the 2014 NFAT public hearing Manitoba Hydro explained that it would address the financial impacts of drought in three principal ways. The second way for Manitoba Hydro to address the impacts of drought is to utilize bridge financing including the use of its $500 million short-term borrowing facility. As stated by Manitoba Hydro at the NFAT proceeding:

> *The second piece to this is bridge financing. I've already indicated that we have our $500 million short-term borrowing program; or, alternatively, could access the capital markets for shorter-dated debt. You know, could be one (1) year, two (2) year, three (3) years, such that they could be retired upon resumption of positive cashflow from operations.*

According to the Consumers Coalition, the short-term borrowing facility has increased to $1.5 billion but is awaiting Provincial Government approval. This Intervener submits that Manitoba Hydro has multiple sources of liquidity to draw upon. Additionally, ratepayers are paying over $200 million per year in “liquidity insurance” in the form of the Provincial Debt Guarantee Fee of 1% on Manitoba Hydro’s outstanding debt. According to the Consumers Coalition and based on the evidence in this Interim Application, Manitoba Hydro experienced no challenges obtaining debt financing due to its creditworthiness. Instead, any challenges Manitoba Hydro experienced with obtaining debt financing resulted from a global market disruption during the initial six weeks of the COVID pandemic when global debt markets froze.

Board Findings

The Board finds Manitoba Hydro’s shift in the term to maturity of new 2021/22 debt issuances of $1.4 billion to be beneficial in the short term as it has reduced Finance Expense.

Cash Flow

In its Interim Application, Manitoba Hydro presented a new cash flow metric called Cash Sufficiency/Deficiency to Fund Core Business Operations.

Manitoba Hydro’s total financing requirements are derived by subtracting Cash Provided by Operating Activities from Cash Used for Investing Activities. If the total financing requirements are greater than the financing requirements related to the major capital projects, a cash deficiency exists, and Manitoba Hydro borrows to fund its core business activities.

Put another way, Manitoba Hydro calculates this metric by looking at its net cash flow position with the borrowing and investing for major capital projects removed. In doing this, Manitoba Hydro assumes that major capital projects, such as Keeyask Generating Station, are fully funded by debt.

Using this new metric, Manitoba Hydro calculated a $348 million cash shortfall for its core business operations in 2021/22. This means that Manitoba Hydro must borrow funds to pay for its interest obligations, ongoing Business Operation Capital expenditures, and ongoing obligations such as mitigation payments.

Despite indicating a $348 million shortfall in Cash Sufficiency/Deficiency to Fund Core Business Operations, Manitoba Hydro projects a $1.121 billion positive cash balance at the end of 2021/22, which is almost the same cash balance as at the end of 2020/21.

Manitoba Hydro Position

According to Manitoba Hydro, the new Cash Sufficiency/Deficiency to Fund Core Business Operations metric is superior to the previously used Capital Coverage Ratio because it focuses on whether revenues from operations are sufficient to pay for those operations. The Capital Coverage Ratio has limited effectiveness given the quantum of the core business cash requirements excluded from the calculation.

Because Manitoba Hydro's Net Extraprovincial Revenue has been reduced by $398 million, that revenue is not available to fund its core business operations. To bridge that revenue shortfall, Manitoba Hydro borrowed $348 million in 2021/22 to pay for its operations. Such borrowings add to the already heavy debt level of Manitoba Hydro and are not sustainable.

The drought comes at a time when Manitoba Hydro is highly leveraged, with a debt ratio of 87%, as a result of funding major capital projects. According to Manitoba Hydro, this level of debt has left very little cash to deal with non-controllable risks as they materialize.

While Manitoba Hydro projects a positive cash balance at the end of 2021/22, this cash balance results from borrowing and is not generated through core operations. Manitoba Hydro maintains this cash balance in order to have six months of working capital.

Intervener Positions

The Consumers Coalition noted that according to its cash flow statement, Manitoba Hydro has a cash reserve balance of $1.121 billion entering 2022/23. According to the

Consumers Coalition, this level of cash on Manitoba Hydro's balance sheet indicates that Manitoba Hydro does not have a liquidity problem.

With respect to the new Cash Sufficiency/Deficiency to Fund Core Business Operations, the Consumers Coalition notes that this is a new financial metric for Manitoba Hydro and that Manitoba Hydro has abandoned the long-standing Capital Coverage Ratio which was supported by the Board in its last two General Rate Application Orders 58/19 and 69/19.

The Consumers Coalition concludes that the Board should continue to apply traditional rate-setting metrics, including the Capital Coverage Ratio, to this interim application, especially given Manitoba Hydro's financial forecasting and rate strategy are in a state of flux. The Consumers Coalition sees risks if the Board applies Manitoba Hydro's unconventional and, in its opinion, flawed rate-setting metrics.

Finally, the Consumers Coalition notes that any rate increase proposed by Manitoba Hydro will not make a material difference to the financial metrics for the fiscal year 2021/22, considering the late effective date of the requested rate increase.

Manitoba Industrial Power Users Group compared Manitoba Hydro's cash flow position in the current drought year with its cash flow position in the 2003/04 drought year. Manitoba Industrial Power Users Group noted that Manitoba Hydro has a positive cash flow from operating activities (excluding financing and investing activities) of $270 million in 2021/22, compared to a cash deficit of $101 million in 2003/04.

Board Findings

The Board notes that Manitoba Hydro introduced a new cash flow metric in this interim rate proceeding. Manitoba Hydro also introduced a new, different cash flow metric in its 2017/18 & 2018/19 General Rate Application. In that proceeding, Manitoba Hydro stated that its Capital Coverage Ratio metric did not provide an accurate view of its cash flow position.

The Board provided its findings with respect to the previously introduced new cash flow metric in Order 58/19, at page 66:

> *The Board finds that, in assessing whether Manitoba Hydro is meeting its ongoing financial obligations, the focus should be on the accrual accounting methodology used in the Utility's audited financial statements and the financial forecasts used for rate setting. This methodology was also previously used by Manitoba Hydro for rate setting purposes and continues to be used by Manitoba Hydro for its financial forecasting and reporting. Accrual accounting used by Manitoba Hydro includes capitalizing interest to capital projects until those new assets enter service for ratepayers. Once in service, the financing and depreciation costs are recorded on the Income Statement to be recovered in consumer rates.*
>
> *Manitoba Hydro's new cash flow analysis does not appear, from the evidence, to be a typical part of financial analysis, and its value is somewhat obscure. The newly presented cash flow analysis is a "new view" created by Manitoba Hydro that the Board does not accept for rate-setting purposes.*

Furthermore, and as accepted by Manitoba Hydro, the Board finds that due to the interim nature of these proceedings, including the insufficient evidence on this topic, the Board will not be altering its prior findings on cash flow or other financial metrics.

The Board will consider the merits of Manitoba Hydro's new Cash Sufficiency/Deficiency to Fund Core Business Operations, as well as Manitoba Hydro's apparent abandonment of the long-standing Capital Coverage Ratio, at the 2022/23 General Rate Application.

The Board finds that due to the severity of the drought and the $398 million reduction in Net Extraprovincial Revenue, Manitoba Hydro will experience a cash flow deficiency in 2021/22. The Board expects the deficiency to be greater than the $348 million indicated in the Interim Application to fund its operations and Business Operations Capital expenditures, due to the approved revenue increase being varied to 3.6%, from the Manitoba Hydro requested 5%.

The Board further finds that reductions in cash flow outlays are available to Manitoba Hydro by reducing its discretionary O&A expenses as well as its Business Operations Capital expenditures, as explained elsewhere in this Order.

Retained Earnings

Manitoba Hydro's financial reserves, or Retained Earnings, are the sum of all profits received by Manitoba Hydro through customer revenues since the Utility's inception, primarily from domestic ratepayers but also from export sales. Manitoba Hydro's financial reserves are not cash and are not retained in a bank account, but rather have been reinvested back into the Utility, including through reducing the amount of new borrowing requirements. Put another way, equity and Retained Earnings represent debt that is avoided. Manitoba Hydro's Retained Earnings are included in the Utility's measurement of its total equity level.

At the end of 2020/21, Manitoba Hydro's Consolidated Retained Earnings were $3.26 billion, the highest in Manitoba Hydro's 70-year history, as were Total Net Debt and Total Assets, as shown in the table below.

Manitoba Hydro Consolidated Financial History ($million)

Year Ending	Total Net Debt*	Total Assets	Retained Earnings
2021	24,186	30,715	3,260
2020	23,288	29,306	3,141
2019	21,552	27,431	3,042
2018	19,200	25,169	2,936
2017	16,438	22,338	2,899
2016	14,527	19,780	2,828
2015	12,566	17,567	2,779
2014	10,757	15,639	2,716
2013	9,633	14,542	2,542
2012	9,010	13,791	2,450
2011	8,365	12,882	2,389
2010	8,155	12,437	2,239
2009	7,521	11,547	2,076
2008	6,853	11,766	1,822
2007	6,597	10,922	1,407
2006	6,614	10,482	1,285
2005	6,642	9,952	870
2004	6,675	9,903	734
2003	6,320	10,234	1,170
2002	6,146	10,405	1,302
2001	6,114	9,966	1,088
2000	5,488	8,692	818
1999	4,772	7,866	666
1998	4,559	7,617	566
1997	4,493	7,133	455
1996	4,685	6,737	354
1995	4,507	6,449	284
1994	4,948	6543	228
1993	4,533	6,025	159
1992	4,972	6,505	183
	*Net of sinking fund		

Source: Manitoba Hydro's Interim Application Appendix 3, which represents consolidated financial information from the Corporation's Annual Reports and does not include all components of the Balance Sheet.

As shown in the table above, the past two decades have seen Manitoba Hydro's Retained Earnings increase by over two billion dollars while its total assets and total debt have more than tripled.

However, because of the drought and the expected net loss of $190 million, Manitoba Hydro projects its electricity-segmented Retained Earnings to fall to $2.885 billion at the end of 2021/22 from $3.074 billion, assuming its proposed 5% revenue increase was approved.

Manitoba Hydro estimated the "cost" of a five-year drought to be a $1.3 billion reduction in Net Extraprovincial Revenue, and a seven-year drought to be $1.8 billion. Unlike previous proceedings, in this Interim Application, Manitoba Hydro did not quantify the reduction in Retained Earnings due to a 5-year or 7-year drought.

Manitoba Hydro Position

Manitoba Hydro stated that it could not calculate the full cost of a multi-year drought – including finance expense impacts and the resulting impact on Retained Earnings – because it does not have a long-term financial forecast. Manitoba Hydro explained that it could not provide a long-term financial forecast because Manitoba Hydro is waiting for the Government to complete its Energy Policy and Manitoba Hydro must also first complete its Integrated Resource Plan.

Manitoba Hydro does not consider Retained Earnings to be the same as reserves. Manitoba Hydro stated that it has no financial reserves that are liquid in nature. The only liquid assets that Manitoba Hydro has on hand are borrowed funds.

According to Manitoba Hydro, its Retained Earnings do not resolve the cash flow deficiency in 2021/22. Manitoba Hydro does not see its Retained Earnings as being there to smooth the financial downturn resulting from the drought as there are no liquid assets available to Manitoba Hydro. Instead, the benefit of holding Retained Earnings is that they are an indicator of the equity of Manitoba Hydro.

Manitoba Hydro stated that while mathematically its Retained Earnings are being reduced by $190 million because of the drought, it does not view this as a cushion or reserve for the drought because of the insufficient cash flow to pay for its operations. Instead, Manitoba Hydro states that it must borrow its way out of the drought.

Manitoba Hydro confirmed that its long-term plan is not to set aside cash in a reserve account but to pay down long-term debt.

Intervener Positions

According to Manitoba Industrial Power Users Group, both the Board and Manitoba Hydro have previously been clear that Retained Earnings are the key factor intended to manage water flow risk. Manitoba Industrial Power Users Group quoted from Manitoba Hydro's Corporate Risk Management report of 2015 which states:

> *Adequate financial reserves are required to protect against a repeat of the worst drought on record. At March 31, 2015, retained earnings totaled $2.8 billion.*

It is the view of the Manitoba Industrial Power Users Group that it reflects appropriate treasury practices that Retained Earnings are not being held as cash reserves, with Manitoba Hydro instead reducing its debt. However, for Retained Earnings to protect against drought, the role of Retained Earnings is to enable Manitoba Hydro to take on debt. Retained Earnings allow Manitoba Hydro to take on debt that it avoided with the Retained Earnings in the first place.

As submitted by the Manitoba Industrial Power Users Group, the role of Retained Earnings must also be understood from the context of the rates that are paid by customers. Manitoba Hydro sets its financial projections and consumer rates based on average revenues and costs of all long-term flow scenarios. But in many years (and for effectively all of the last 18 years), water has been better than average. As a result, current ratepayers have funded 18 years of Retained Earnings growth during the higher-than-average water conditions in order to be afforded stable and predictable rates when the lower water conditions arise.

Manitoba Industrial Power Users Group further notes that Manitoba Hydro's Retained Earnings just before the drought in 2003/04 were $1.17 billion. At that time, Manitoba Hydro estimated the cost of the worst drought on record as $1.1 billion, excluding the compounding cost of financing. This Intervener points out that such a drought would have eliminated Manitoba Hydro's Retained Earnings. Manitoba Industrial Power Users Group contrasts that situation with the current situation, which is that the current drought is expected to result in a loss of $190 million against Manitoba Hydro's $3 billion of Retained Earnings. A seven-year drought has an estimated cost of $1.8 billion against the $3 billion of Retained Earnings. Therefore, according to the Manitoba Industrial Power Users Group, the situation is completely different now.

Manitoba Industrial Power Users Group submits the approach to the build-up of Retained Earnings, and the primary driver for Retained Earnings being the risk of drought, is not new to Manitoba Hydro. In the Manitoba Hydro annual report for the year ending March 31, 2004, Manitoba Hydro noted with respect to the drought:

> *While the net loss in 2003-04 was significant, it was not unexpected. Manitoba Hydro's long-term financial forecasts take into account that drought conditions will typically occur about once every 10 years and that such conditions will have negative financial consequences. The risk of drought was one of the primary drivers behind the significant buildup in retained earnings over the past decade.*

According to the Consumers Coalition, Manitoba Hydro downplayed the use of Retained Earnings as a drought mitigation tool, contradicting its position articulated in its financial statements. The Annual Report from the Manitoba Hydro-Electric Board for 2020/21 states:

> *Manitoba Hydro manages its capital structure to ensure that there is sufficient equity to absorb the financial effects of adverse circumstances and to ensure continued access to stable low-cost funding for capital projects and ongoing operational requirements.*

<u>Board Findings</u>

The Board finds that Manitoba Hydro's $3.074 billion of electricity-segmented Retained Earnings, as reported on its audited 2020/21 balance sheet, is the highest in the 70-year history of Manitoba Hydro.

The Board also finds that Manitoba Hydro's current position of not considering its Retained Earnings as 'reserves' to be inconsistent with its previous position. While acknowledging Retained Earnings are not on deposit as cash reserves, the Board finds that Retained Earnings represent equity in Manitoba Hydro's capital structure and enhance Manitoba Hydro's ability to borrow money in the event of a drought.

In Order 59/18, the Board provided extensive findings on the role of Retained Earnings in managing the impacts of drought. Through this Interim Application hearing process, the Board remains of the view that:

> *In making this determination, the Board is guided by two considerations. The first is: what "reserves" should Manitoba Hydro hold to manage risk and which risks should it take into account? As an example, as per the question posed in the evidence of Morrison Park Advisors, what is the level of retained earnings needed in the event of a five-year drought? The second is to place concerns about the amount of debt and retained earnings in a different perspective by also considering cash flow, using two long-standing financial metrics used by Manitoba Hydro: interest coverage ratio and the capital coverage ratio.*
>
> *...*

> *In addition, the Board accepts the evidence of Morrison Park Advisors that Retained Earnings should be used to manage drought risk in combination with regulatory action by the Board. The Board further agrees that interest rate and export price risks over the long term should be addressed with rate increases as and when those risks materialize. Rates should not be set to increase Retained Earnings to manage those longer-term risks. As discussed elsewhere in this Order, the Board is prepared to consider regulatory action when required to address emerging risks facing Manitoba Hydro.*

The Board finds that it has taken regulatory action with respect to the drought, with the customer class rate increases approved in Orders 137/21 and 140/21. As for Retained Earnings, the Board notes that Manitoba Hydro's Retained Earnings are being used to manage the current drought, as evidenced by the reduction in Retained Earnings that will result from the net loss in 2021/22. With any drought as severe as the current drought that produces a reduction in Net Extraprovincial Revenue of $398 million, Manitoba Hydro will experience a net loss and a cash flow shortfall, unless its Net Income under average water conditions is extraordinarily high such that a $398 million reduction still results in a positive Net Income.

Put another way, for Manitoba Hydro to "use" Retained Earnings to address the financial impact of a drought, the Retained Earnings will be reduced, which means sustaining a net loss. This will usually mean that Manitoba Hydro must borrow funds in severe drought years to fully fund its core operations.

When the Board says it is prepared to take regulatory action in combination with the use of Retained Earnings, it is in effect saying that it will balance its response to the drought using these two tools. However, the Board expects Manitoba Hydro to use its tools to respond to the financial effects of the drought, specifically reductions in O&A expenses and Business Operations Capital expenditures, as described elsewhere in this Order.

In the current situation, because Manitoba Hydro's Interim Application is filed three-quarters of the way through the fiscal year, the Board finds there is no reasonable opportunity through regulatory action to avoid the reduction in Retained Earnings for 2021/22.

Also, as described elsewhere in this Order, Manitoba Hydro is forecasting a return to positive Net Income in 2022/23. Therefore, some amount of the Retained Earnings will be replenished next year, assuming water flows return to normal or above normal. If the drought continues, the Board may be presented with a similar decision next year, which is to balance a rate increase with a reduction in Retained Earnings.

The Board's additional reasons for its decisions with respect to specific rate increases in this Interim Application, which are used in combination with Retained Earnings, are included elsewhere in this Order.

The Board finds the lack of a long-term financial forecast unacceptable for a Utility that generates over $2.5 billion of annual revenue. The lack of a long-term financial forecast impedes the rate-setting process. Manitoba Hydro has not fulfilled its commitment to have a long-term financial forecast filed with the Board in late 2019. Furthermore, Manitoba Hydro produced its approved financial forecast only four months ahead of the April 1, 2022 start of the 2022/23 fiscal year. As explained later in this Order, for rate-setting purposes Manitoba Hydro is required to prepare a long-term financial forecast ahead of its 2022/23 General Rate Application.

5.0 Major Capital Projects Entering Commercial Service

As shown in the table below, Manitoba Hydro has a number of large capital projects that have recently entered commercial service or are imminently entering service. For many years, as expressed in its prior Orders, the Board has been concerned with the additional annual costs and revenue requirements of these major projects and the resulting impact on the rates set for Manitoba Hydro's customers.

While assets are under construction, the capital expenditures and associated financing costs are held on Manitoba Hydro's balance sheet in 'Construction Work In Progress'. Once these assets are placed into commercial service, the associated costs (i.e. operating expenses, finance expense, depreciation expense, water rentals, and capital taxes) form part of Manitoba Hydro's annual revenue requirements on its operating statement and are sought to be recovered from electricity ratepayers through the rates approved by this Board.

The following projects have recently entered commercial service or, in the case of Keeyask Generating Station, have partially entered service:

Project	**Control Budget ($ millions)**
Keeyask Generating Station	8,726
Bipole III Transmission Line	4,770
Manitoba-Minnesota Transmission Project	490
Great Northern Transmission Line * (US$)	712
Birtle (Manitoba-Saskatchewan) Transmission Line	69

* Based on a 2014 capital cost forecast in 2020 US dollars as the current capital cost remains confidential. Manitoba Hydro is responsible for 72% of the capital costs and 66.7% of the operating costs.

Manitoba Hydro's Interim Application, in the figure below, sets out the estimated annual revenue requirements for each project by year:

Revenue Requirement Impact of Major Capital Projects

($ millions)	**2021/22**	**2022/23**	**2023/24**
Keeyask Generating Station	282	499	526
Bipole III Transmission Line	327	316	316
Manitoba-Minnesota Transmission Project	30	29	29
Great Northern Transmission Line	66	64	64
Birtle (Manitoba-Saskatchewan) Transmission Line	3	3	3
Gross Impact	**708**	**912**	**938**
Amortization of Major Capital Projects Deferral*	(12)	(50)	(37)
Amortization of Bipole III Reserve*	(77)	(77)	(20)
Net Impact	**619**	**785**	**881**

*Amortization of Capital Reserves projected to cease in 2023/24

Source: Manitoba Hydro's Interim Application p.36

The above figure also shows the revenue requirements net of the previously approved amortization of the Bipole III Reserve deferral account and the proposed amortization of the Major Capital Projects Deferral Account. These amounts are the amortization and recognition on the operating statement of deferred ratepayer revenues from previously approved electricity rate increases. The Bipole III Reserve was first approved in Order 43/13 and the revenues from some or all of subsequent rate increases were deferred and not recognized on Manitoba Hydro's operating statements. The Major Capital Projects Deferral Account was approved effective June 1, 2019, in Order 69/19 with approximately 2.4% of annual consumers revenue being deferred into this account.

Manitoba Hydro Position

Manitoba Hydro submits that in addition to the financial impact of the current drought, 3.5% of the 5% proposed general revenue increase is required as a result of the substantial increases in Manitoba Hydro's annual revenue requirements due to the major capital projects that are being, or have recently been, brought into commercial service.

Intervener Positions

While it recognizes the short-term financial impact of the drought is negative, the Consumers Coalition characterizes the underlying financial health of Manitoba Hydro as a “good news” story. The Consumers Coalition notes that Manitoba Hydro is in a better financial position now than was projected at the 2017/18 & 2018/19 General Rate Application. In addition to net debt being lower by $1.1 billion, the revenue requirements of some of the major new capital projects are lower than previously projected. The annual revenue requirement for Bipole III is approximately $50 million lower, and for the Great Northern Transmission Line, it is approximately $30 million lower. In addition, the Manitoba-Minnesota Transmission Project was completed with costs tracking within the control budget of $490 million. Keeyask is still on track for completion within the control budget of $8.7 billion.

Like the Consumers Coalition, Manitoba Industrial Power Users Group notes that Manitoba Hydro’s current financial situation is superior to where any party expected it to be at this time. Manitoba Industrial Power Users Group states that having Manitoba Hydro’s Net Income be positive in the first year that all Keeyask units are in service is an indisputably positive financial result compared to each prior long-term scenario Manitoba Hydro presented in its annual financial forecasts going back to 2012.

Board Findings

While the drought and the resulting $398 million of reduced Net Extraprovincial Revenue were major factors considered by the Board in reaching its decision to approve a 3.6% increase in Manitoba Hydro’s General Consumers Revenue, the Board was also concerned with the increasing annual revenue requirements for the recently completed and soon to be completed capital projects.

The Board notes that collectively these projects increase Manitoba Hydro’s annual revenue requirement, paid by ratepayers, by $708 million in 2021/22 and by $912 million in 2022/23.

To avoid large and irregular rate increases or 'rate-shock' for consumers, the Board has, with the support of Manitoba Hydro and Interveners, been smoothing-in lower rate increases and also creating revenue deferral accounts in anticipation of these large expenses coming due, with previously deferred revenue being recognized when the major capital projects enter service. The Board's rate smoothing process utilized long-term financial forecasts by Manitoba Hydro, but Manitoba Hydro does not currently utilize a current long-term financial forecast to assist in rate setting.

The Board further notes that Manitoba Hydro's last long-term financial forecast was developed in 2016 and finalized in April of 2017. As found by the Board in Order 137/21, without such a current planning document, the Board and all Parties are at a disadvantage when considering the important concepts of rate smoothing and reasonable rate trajectories when balancing the interests of ratepayers with the financial health of Manitoba Hydro.

Without a current long-term financial forecast, the Board gave general consideration to the rate trajectories from such prior documents when considering rate increases to generate additional revenues to pay the additional annual costs of these new major capital projects entering commercial service.

As explained in Section 10.0, the Board directs that long-term financial forecasts be filed in the 2022/23 General Rate Application when the January 1, 2022, interim rates are further examined.

Major Capital Projects Deferral Account

In Order 69/19, the Board approved a 2.5% rate increase to most customer classes, with lower rate increases to some classes, effective June 1, 2019 and directed all revenues from these increases to be deferred in a Major Capital Projects Deferral Account to help mitigate rate increases when the major projects under construction are placed in service.

Several major capital projects have entered service since this deferral account was established (i.e. Manitoba-Minnesota Transmission Project, Birtle Transmission Project, Great Northern Transmission Line, and five of seven units of Keeyask Generating Station). Consistent with the treatment of the Bipole III Deferral Account, Manitoba Hydro proposes to cease funding the Major Capital Projects Deferral Account effective December 31, 2021, such that the revenues previously deferred from the 2.5% rate increase will thereafter flow to Manitoba Hydro's general revenues.

Manitoba Hydro Position

Manitoba Hydro proposes ceasing deferrals into the Major Capital Projects Deferral Account and, commencing January 1, 2022, to begin amortizing the balance in this deferral account, expected to be approximately $100 million as of December 31, 2021, over 24 months. Ceasing deferral of revenue results in approximately $38 million of additional revenue being recognized annually on Manitoba Hydro's operating statement. The proposed amortization period will allow Manitoba Hydro to recognize $12 million in revenue in 2021/22, a further $50 million in 2022/23, and $37 million in 2023/24.

The combination of the amortization of the Major Capital Projects Deferral Account and the Bipole III Deferral Account reduces the overall revenue requirement of the major new capital projects by $89 million in 2021/22, $127 million 2022/23, and $57 million in 2023/24, as shown in the above figure.

According to Manitoba Hydro's Interim Application, after 2023/24, both deferral accounts will be fully amortized and depleted and will no longer provide an offset to annual revenue requirements in future years. Manitoba Hydro states that a 24 month amortization period for the Major Capital Projects deferral balance is appropriate because it is approximately the period of time over which the balance was accrued.

Intervener Positions

The Consumers Coalition recommends a longer amortization period for the Major Capital Projects Deferral Account balance. The purpose of the deferral account was to smooth in the increased revenue requirements from the Major Capital Projects. These assets have long lives and regulatory precedent would suggest an amortization period of a least five years.

Manitoba Industrial Power Users Group recommends that the revenues in the Major Capital Projects Deferral Account not be amortized at this time. This Intervener submits that amortization beginning January 1, 2022 does not assist Manitoba Hydro with debt or liquidity issues. Furthermore, there is no evidence that 24 months is the appropriate period over which to recognize these revenues.

The Assembly of Manitoba Chiefs submits the purpose of the Major Capital Projects Deferral Account is to provide a benefit to ratepayers by smoothing rate increases and guarding against rate shock when new major capital projects enter service. According to this Intervener, Manitoba Hydro's proposed use of this deferral account balance (i.e. over 24 months) does not meet this purpose. The Assembly of Manitoba Chiefs also submits that amortizing the balance into operating revenue may help Manitoba Hydro's Net Income but that amortization does not address Manitoba Hydro's cash flow situation. The Assembly of Manitoba Chiefs recommends a shorter amortization period be considered to benefit ratepayers with a lower rate increase.

Board Findings

In Order 137/21, the Board found that the amortization of the $99 million January 1, 2022 balance in the Major Capital Projects Deferral Account was an issue to be determined at the 2022/23 General Rate Application. The Board found that there is disagreement among the Parties related to the amortization of the revenues from the Major Capital Projects Deferral Account. Therefore, the Board did not approve Manitoba Hydro's request to commence the recognition of the revenues in this deferral account commencing January 1, 2022 with the balance amortized over 24 months. This issue will be determined at the 2022/23 General Rate Application.

However, with the pending completion of the Keeyask Generating Station this fiscal year, the Board finds that it is appropriate to discontinue the deferral of revenues into the Major

Capital Projects Deferral Account effective December 31, 2021 with the resulting revenues flowing to Manitoba Hydro's operating statement, commencing January 1, 2022, rather than into the deferral account.

By terminating the deferral of revenues into the major Capital Projects Deferral Account, the revenues resulting from the rate increases on June 1, 2019 flow to Manitoba Hydro's operating statement rather than into the deferral account.

Keeyask In-Service Deferral Account

In its Interim Application, Manitoba Hydro sought to introduce a Keeyask In-Service Deferral Account in order to maintain the revenue requirement impact of its prior accounting practice with respect to the timing of the recognition of costs related to its hydroelectric generating stations under construction. Now that it has adopted International Financial Reporting Standards, Manitoba Hydro states that the Keeyask In-Service Deferral Account is required to maintain the revenue requirement impact of the prior accounting methodology that Manitoba Hydro used under Canadian Generally Accepted Accounting Principles.

Manitoba Hydro Position

As noted in its Interim Application, the Keeyask In-Service Deferral Account was established based on Manitoba Hydro's past practice of recognizing expenses associated with the generating station on a per-unit basis for rate-setting purposes. Manitoba Hydro indicated it would seek regulatory approval for this deferral and associated amortization at a future regulatory proceeding.

Intervener Positions

No parties took a position with respect to the proposed Keeyask In-Service Deferral account.

<u>*Board Findings*</u>

As stated in Order 137/21, the Board will address the establishment and amortization of Manitoba Hydro's newly created Keeyask In-Service Deferral Account at the 2022/23 General Rate Application.

6.0 Financial Forecast for 2022/23

2022/23 Plan

Manitoba Hydro provided a budget for its 2022/23 fiscal year. At the time of filing the November 15, 2021 Interim Application, this budget had not received approval from the Manitoba Hydro-Electric Board, and so it was described by Manitoba Hydro as the 2022/23 Preliminary Plan. Prior to completion of the Interim Application public hearing, this budget was approved by the Manitoba Hydro-Electric Board and so it is no longer "preliminary" and is set out below:

ELECTRIC OPERATIONS
OPERATING STATEMENT
($millions)

	2022/23 Plan
Revenues	
Domestic Revenue	
At Approved Rates	1,769
Additional (From proposed 5% January 1, 2022 Rate Increase)	88
Extraprovincial	916
Other	29
	2,802
Expenses	
Operating And Administrative	595
Net Finance Expense	1,039
Depreciation And Amortization	621
Water Rentals And Assessments	134
Fuel And Power Purchased	157
Capital And Other Taxes	161
Other Expenses	106
Corporate Allocation	8
	2,820
Net Income Before Net Movement In Reg. Deferral	(19)
Net Movement In Regulatory Deferral	225
Net Income	206
Net Income Attributable To:	
Manitoba Hydro	**200**
Non-Controlling Interests	6
	206
Proposed Percent Increase in 2022/23	0.00%

Source: Manitoba Hydro's Minimum Filing Requirement #3

Manitoba Hydro forecasts $200 million of Net Income in 2022/23, assuming the end of the drought and the return to normal water flow conditions and approval of a 5% revenue increase in 2021/22. Manitoba Hydro calculates the $200 million of Net Income based on the average of the financial results of 40 years of water flow conditions, starting with a forecast of the water levels and reservoir conditions as of April 1, 2022 which is 20% lower than average. Had Manitoba Hydro utilized its former forecasting methodology with 108 years of water flow data, its 2022/23 forecast Net Income would be approximately $19 million higher, or $219 million.

Based on the 40 year flow record, and starting with reservoirs 20% below average, Manitoba Hydro is forecasting that a net loss would occur in only the two lowest water flow conditions of the most recent 40 year flow record, assuming a 5% rate increase in 2021/22.

Manitoba Hydro Position

Manitoba Hydro indicates that, even with no additional rate increase in the 2022/23 fiscal year, it will earn $200 million based on the above described average results from the 40 water flow conditions. However, Manitoba Hydro is concerned that, even with average water flow conditions next year, its cash flow sufficiency of $51 million is minimal with little room for negative deviation.

Manitoba Hydro testified that, even assuming there is no continuation of the 2021/22 drought, it will seek an additional rate increase in fiscal 2022/23 to continue the rate trajectory required to pay for the revenue requirements of the major capital projects that have now entered commercial service.

Manitoba Hydro's compliance filing in response to Order 137/21 indicates that the 3.6% revenue increase will generate an additional $64 million, compared to $88 million from the proposed 5% increase.

Intervener Positions

The Consumers Coalition states that current rates are sufficient to pay for the carrying costs of the major capital projects as well as all of Manitoba Hydro's other costs. The Consumers Coalition estimates that Manitoba Hydro will earn $112 million of Net Income in 2022/23 even if no rate increase is awarded. By contrast, at the NFAT proceeding, Manitoba Hydro projected eight years of losses totaling $638 million. At the 2017/18 & 2018/19 General Rate Application, Manitoba Hydro updated its projections to six years of losses totaling $418 million beginning in 2022/23.

Even without a rate increase, the Consumers Coalition states that Manitoba Hydro forecasts that its financial results will return to being in line with prior projections, based on the results of modeling the 40 year flow record even assuming starting reservoir levels that are 20% lower than average.

Manitoba Industrial Power Users Group notes that, based on Manitoba Hydro's Net Income projections for varying levels of rate increases, most of the net loss in 2021/22 will be recovered in 2022/23. Furthermore, all interest payments made by Manitoba Hydro are paid from cash receipts and there remains positive cash from operating activities of $778 million in the 2022/23 approved budget. Manitoba Industrial Power Users Group states that the current debt levels are more than sustainable at current receipts from customers, however Manitoba Hydro cannot fully fund interest payments from internal cash flow as well as make a $250 million contribution into the sinking fund plus make $886 million investments in new capital. Manitoba Industrial Power Users Group states that it may not be reasonable to expect Manitoba Hydro to be able to fund all of these from current year cash receipts.

Board Findings

The Board understands that the water flow conditions in 2022/23 remain uncertain and that the projection of $200 million of Net Income is dependent on a number of factors, including these uncertain water flow conditions. However, two factors have already affected the forecast 2022/23 Net Income: the Board approved a 3.6% revenue increase instead of the requested 5% increase, and Manitoba Hydro will not immediately recognize revenues in 2022/23 from the Major Capital Projects Deferral Account. Accordingly, the Board acknowledges that based on current assumptions Manitoba Hydro will not achieve $200 million of Net Income in 2022/23, unless water flow conditions are well above average.

As submitted by Interveners, there may be a “good news” story in the projections for 2022/23 Net Income. Even with the additional revenue from the rate increase reduced and no operating statement recognition of prior deferred revenues, the evidence projects a positive Net Income for Manitoba Hydro in most of the 40 assumed hydrological situations. However, it is premature to confirm this “good news” story absent a long-term financial forecast from Manitoba Hydro.

As explained above, the Board finds the lack of a Manitoba Hydro long-term financial forecast to be unacceptable. As previously directed and as explained later in this Order, Manitoba Hydro is to include a long-term financial forecast with its 2022/23 General Rate Application.

O&A Expenses

Having previously reduced its Operating & Administrative Expenses (“O&A”) expenses through a Voluntary Departure Program in 2017 and through government-directed pandemic savings, Manitoba Hydro now plans to increase its O&A expenses by 7% or $38 million in 2022/23 as shown in the table below.

Million$	2015/16 (Pre-VDP) Actual	2016/17 (Pre-VDP) Actual	2017/18 (VDP Beginning) Actual	2018/19 (VDP Complete) Actual	2019/20 (Pre-Pandemic) Actual	2020/21 (Pandemic) Actual	2021/22 Forecast	2022/23 Plan
O&A – electric	543	536	517	508	512	534	557	595
Net change	-	(7)	(19)	(9)	4	22	23	**38**
% change	-	-1%	-4%	-2%	1%	4%	4%	**7%**

Recognizing human resource costs are 79% of O&A expenses, Manitoba Hydro is targeting increasing staffing levels by 466 more Full-Time Equivalent employees ("FTE") than were employed during 2020/21. The actual and planned number of FTE positions from 2015/16 through to 2022/23 are as follows:

FTEs	2015/16 (Pre-VDP) Actual	2016/17 (Pre-VDP) Actual	2017/18 (VDP Beginning) Actual	2018/19 (VDP Complete) Actual	2019/20 (Pre-Pandemic) Actual	2020/21 (Pandemic) Actual	2021/22 Forecast	2022/23 Plan
Corporate FTEs[2]	6,410	6,411	5,998	5,475	5,393	4,954	5,022	5,420
FTE Net change	-	1	(413)	(523)	(82)	(439)	68	398
% change	-	-	-6%	-9%	-1%	-8%	1%	8%

Manitoba Hydro indicated the 5,420 FTE target reflected in the above table would be attained in the next two years and included funding for 5,175 FTEs in its 2022/23 Plan. Manitoba Hydro did not provide a detailed budget of O&A expense for 2022/23.

Manitoba Hydro Position

Manitoba Hydro indicates that because it has previously reduced FTEs and total O&A expenses in response to a Voluntary Departure Program in 2017 as well as Government

[2] Regular FTEs include employees of subsidiaries and seasonal, hourly, and part-time staff. It is derived by calculating total straight time hours in the year divided by 1916 hours per FTE.

direction, there is no further reduction of these O&A expenses planned to respond to the drought.

Manitoba Hydro indicates that FTEs are currently at the lowest levels since its purchase of Winnipeg Hydro in 2002 but this level is not sustainable. Manitoba Hydro considered the most recent reductions in FTEs to be a short-term, temporary situation to address the pandemic. Manitoba Hydro now has an external hiring plan in place to increase to pre-pandemic FTE levels, which Manitoba Hydro considers to be the minimum to continue to provide safe and reliable service to its customers and minimize the life cycle costs of its assets.

Intervener Positions

Manitoba Industrial Power Users Group submits that while Manitoba Hydro has repeatedly indicated that it could not make any spending cuts without affecting the ability to provide "safe and reliable energy", Manitoba Hydro has always found ways to contain operating costs when directed to do so by the Province. Manitoba Hydro is now proposing to undo much of its cost containment and increase spending in FTEs. Given that the budget increasing the FTEs has been approved by the Manitoba Hydro Board of Directors, Manitoba Industrial Power Users Group again questions what Manitoba Hydro is considering as cost-cutting measures. This Intervener repeats its recommendation for strong Board direction to incent Manitoba Hydro to retain cost savings for the benefit of consumers.

As noted in Section 4.0 above, instead of reducing O&A, the Consumers Coalition calculates Manitoba Hydro has increased its O&A spending by 4.3% from 2019/20 to 2020/21 and is projecting a cumulative increase from 2019/20 to 2022/23 of 16.2% (i.e. 5.4% per year on average).

The Consumers Coalition indicates a 2% O&A increase may be reasonable until it can be tested at the 2022/23 General Rate Application. This would amount to an $11 million increase, not the $38 million or 6.8% increase sought by Manitoba Hydro.

Board Findings

The Board finds that the 3.6% increase in General Consumers Revenue approved in Order 140/21 will annually yield $64 million. Manitoba Hydro's planned increase in O&A expenses in the current and next fiscal year totals $61 million.

While recognizing that O&A expenses were a contentious issue and not a principal focus of this Interim Application, the Board finds Manitoba Hydro's plans to increase its O&A expenses in 2022/23 to be unsupportable based on the evidence in this Interim Application. In a time of drought, with no evidence that the drought will end in 2022/23, Manitoba Hydro must reduce expenditures, as it explained it would when describing how it would address drought at the 2014 NFAT proceeding.

The Board notes that O&A cost savings realized to date ought not to be considered temporary savings. With Manitoba Hydro currently researching the future implementation of initiatives related to its now-finalized new corporate strategic plan ('Strategy 2040'), Manitoba Hydro is provided with an opportunity to solidify existing savings and find further efficiencies.

The Board finds that cost control should be ongoing and continue in the post-Voluntary Departure Program years, the pandemic years, and drought years.

If the drought continues and Manitoba Hydro's cash flow concerns continue next year, the Board finds that Manitoba Hydro must seek savings in its O&A expenses in order to confront liquidity concerns related to the continuing drought. The Board notes that Manitoba Hydro plans to increase its O&A expenses relatively quickly in the next fiscal year. Based on the record of this hearing, the Board finds that Manitoba Hydro can slow, pause, or suspend planned O&A increases. The Board will consider Manitoba Hydro's steps to manage its O&A expenses at the next General Rate Application.

7.0 Interim Rate Increase

Manitoba Hydro Position

Manitoba Hydro proposes using a combination of debt and rate increases to mitigate the $398 million reduction in Net Extraprovincial Revenue due to the drought.

In its 2021/22 Interim Application, Manitoba Hydro maintains that a 5% increase in General Consumers Revenue, to be realized through rate increases to its customer classes effective January 1, 2022, is just and reasonable.

Manitoba Hydro indicates it is not possible to recover from a cash flow deficiency of $348 million in one fiscal year or with one proposed rate increase to take effect on January 1, 2022. Even if Manitoba Hydro's proposed interim rate increases to generate 5% additional General Consumers Revenue were approved, those rate increases would generate $27 million of incremental revenue in 2021/22 and $88 million in 2022/23.

According to Manitoba Hydro, the level of rate increases required strictly from a financial perspective to recover the $190 million expected 2021/22 loss in Net Income is greater than 12%. A rate increase of greater than 21% would be required to recover, over 12 months, the $348 million borrowing to fund the cash flow deficiency in 2021/22. Manitoba Hydro submits that it took a more balanced approach in its rate increase request.

Manitoba Hydro's requested 5% increase is comprised of 3.5% for its regular operations and to meet the increasing revenue requirements for the new capital projects that have entered commercial service, with an additional 1.5% on account of the drought impacts.

Manitoba Hydro states that the cost of the drought exceeds the estimate by the Assembly of Manitoba Chiefs of $250 million. According to Manitoba Hydro, it is not possible to separate the export price risk from the drought risk. Manitoba Hydro had to purchase higher than forecasted amounts of power as a direct result of the drought and those higher volumes were purchased at prices that were higher than forecasted in the 2021/22 Budget.

Intervener Positions

Like Manitoba Hydro, Interveners also divided their rate increase recommendations between a specific amount for the drought impacts and a separate amount for Manitoba Hydro's operations in recognition of the revenue requirements for the new major capital projects.

While the Consumers Coalition supported 'rate smoothing' for known large future expenses, this Intervener submitted such a view could not be supported in this Interim Application because Manitoba Hydro did not provide a long-term or even a mid-term financial forecast to determine an appropriate future rate trajectory.

The Consumers Coalition opposed Manitoba Hydro's requested 5% increase because it is a $2 billion (net present value) long-term solution to a $348 million (cash flow) short-term problem. This Intervener noted that Manitoba Hydro is forecasting healthy financial metrics for 2022/23 even without any rate increase.

The Consumers Coalition recommended a 1.2% increase to smooth rates needed to address costs of major capital projects entering commercial service, plus an additional 0.8% increase to address the carrying cost for the funds Manitoba Hydro borrowed in 2021/22 as a result of the drought. The Consumers Coalition further calculates a 0.8% rate increase has a net present value of $320 million in perpetuity, exceeding the projected $190 million loss in Manitoba Hydro's 2021/22 Net Income.

The Consumers Coalition submitted that any amount of a reasonable rate increase would not eliminate the $190 million loss Manitoba Hydro forecasts for 2021/22. Even the 5% proposal by Manitoba Hydro only generates an additional $27 million this fiscal year.

This Intervener further noted that with a 2% total interim rate increase, Manitoba Hydro expects to earn $147 million of Net Income in 2022/23 along with being only $2 million cash flow negative after funding its core operations. Furthermore, Manitoba Hydro's financial metrics will be improved in 2022/23 from the last General Rate Application. Net debt is down $1 billion, EBITDA Interest Coverage Ratio is up 0.15 to 1.73, and the Capital

Coverage Ratio is up 0.05 to 1.38. The debt ratio has unfavourably increased to 87.9%, but this is expected to occur in a drought.

Manitoba Industrial Power Users Group submitted that customer interests for rate stability, predictable transitions, and avoidance of rate shock support a movement on rates towards the levels previously anticipated to be required in the future, as the existing rate deferral accounts become depleted. The last rate increase to the majority of Manitoba Hydro's customers was on December 1, 2020, and the next fully-reviewed rate increase is not expected to occur before a full General Rate Application is completed in 2022. However, to maintain a normal schedule of rate increases, this Intervener submits a 2.5% average rate adjustment should be implemented on an interim basis for January 1, 2022.

This Intervener maintained that, of a 2.5% increase, 0.8% should be credited to MH's operating revenues while the revenue from the 1.7% balance of the overall increase be held in a deferral account until a full General Rate Application has been conducted in 2022. This Intervener submitted the revenue from a 0.8% increase is reasonable as a bridge to a full General Rate Application.

Manitoba Industrial Power Users Group further indicated a 2.5% rate increase as of January 1, 2022 would still result in an estimated loss of between $201 million and $206 million in 2021/22 but a Net Income of between $147 million and $162 million in 2022/23. With such a rate increase, most of the loss in 2021/22 would be recovered by Manitoba Hydro's positive Net Income in 2022/23.

The Assembly of Manitoba Chiefs submitted that First Nations customers are particularly negatively affected by electricity rate increases because of their increased electricity usage due, in part, to the lack of access to natural gas for heating. First Nations customers are also more negatively affected by rate increases due to higher levels of energy poverty as seen in previous proceedings before the Board.

The Assembly of Manitoba Chiefs further submitted that a 5% increase in electricity rates will have a significant negative impact on the customers who were previously in the First

Nation On-Reserve Residential class and that Manitoba Hydro has not balanced the interests of these customers with its corporate financial health.

The Assembly of Manitoba Chiefs submitted that, in determining the balance between Manitoba Hydro's financial health and the interests of its ratepayers, the principle of reconciliation should be considered. As an agent of the Crown, this Intervener maintained Manitoba Hydro also has a mandate to advance reconciliation. The Assembly of Manitoba Chiefs submitted that aside from some general statements made by Manitoba Hydro, including that it considered the interests of all customers including First Nations customers, there is no evidence on the record of the Interim Application about the impact of a 5% rate increase on former First Nations On-Reserve Residential class customers in light of the rate increases they have faced since the fall of 2020.

According to this Intervener, a 5% increase is not just and reasonable through the Interim Application process because the requested amount is not just related to the costs of the drought. Furthermore, the costs of drought should be addressed through mechanisms other than a rate increase. If the next rate increase is not until Apr 1, 2023, the Assembly of Manitoba Chiefs is concerned that it may explain why Manitoba Hydro is asking for a 5% increase now. A 5% rate increase would amount to rate shock for First Nations customers.

According to the calculations of this Intervener, the impact of the drought is more appropriately considered to be $250 million due to reduced hydraulic generation, with the remainder being the impact of changes in electricity export prices and the cost of electricity imports and natural gas needed for Manitoba Hydro's thermal generating station. If 1.5% of the rate increase is related to the cost of the drought (being the portion of 5% that is not the 3.5% related to major capital projects), this amount can be reduced further given the cost of the drought is $250 million, not $398 million as stipulated by Manitoba Hydro.

Where rate increases are necessary, the Assembly of Manitoba Chiefs advocated for lower rate increases over a longer period of time because it provides predictability and stability for customers.

Board Findings

In Order 137/21 and relying on the evidentiary record of Manitoba Hydro's Interim Application, the Board found that it was just and reasonable to vary Manitoba Hydro's requested 5% increase in General Consumers Revenue and approve a 3.6% increase through interim rate increases, effective January 1, 2022, that were differentiated by customer class.

In this Order, the Board varies its finding in Order 137/21 and in Order 140/21 and now finds that this interim 3.6% General Consumers Revenue increase will be recovered through rates that remain in effect only until November 30, 2022, unless Manitoba Hydro has filed, by November 15, 2022, a General Rate Application to confirm the 2021/22 interim rate increases and seeking rates for 2022/23 and, if it so chooses, for 2023/24. If Manitoba Hydro does not file a General Rate Application by November 15, 2022, the rates will revert to those in effect prior to Order 140/21. The General Rate Application to be filed in 2022 by Manitoba Hydro may be for up to three test years, including the confirmation of the 2021/22 test year interim rates.

In this Interim Application, the Board did not find sufficient evidence to allow it to divide the awarded increase into separate categories of "drought rate increase" and "base operations rate increase". This is a matter that the Board will consider further at the 2022/23 General Rate Application when Manitoba Hydro seeks to finalize the 2021/22 interim rates.

In Order 140/21, the Board approved rate increases differentiated by customer class, to allow Manitoba Hydro to realize a 3.6% increase in annual General Consumer Revenues. For the balance of the 2021/22 fiscal year, which ends March 31, 2022, the rate increases are expected to generate approximately $20 million of additional revenue. On a full 12 month basis, the interim rate increases will realize $64 million of additional revenue for Manitoba Hydro.

The Board directs Manitoba Hydro to provide, by February 28, 2022, schedules showing the approved revenue requirements for the 2021/22 and 2022/23 fiscal years reflecting the decisions in Order 137/21 and 140/21, in a similar format as it provided in Minimum Filing Requirement 3.

8.0 Cost Allocation and Customer Bill Impacts

A cost of service study ("COSS") is used to determine each customer class's share of Manitoba Hydro's revenue requirement. A COSS is an established and industry-accepted method to evaluate whether each customer class is contributing, through revenues from the approved rates, its fair share based on the cost to Manitoba Hydro to provide electric service to each class.

The results of the COSS indicate the degree to which each customer class's allocated costs are recovered through revenues collected from the class through Board-approved rates. The ratio of class revenues to class costs is referred to as Revenue to Cost Coverage ("RCC"). In Manitoba, to the extent that a customer class's RCC falls within a range of 95% to 105%, known as the Zone of Reasonableness ("ZOR"), it is accepted that its revenues are recovering the allocated costs.

Manitoba Hydro relies on its most current COSS – Prospective Cost of Service Study PCOSS21 – to guide the rate increases being proposed for each customer class. Reflective of Board direction in Orders 59/18 and 69/19, Manitoba Hydro proposed differentiated rate adjustments to continue the migration of customer class RCCs into the ZOR. The required class differentiation has been calculated in the table below by Manitoba Hydro assuming a seven-year remaining timeframe, consistent with the Board's direction to move all classes within the ZOR over a ten-year timeframe as contemplated in Order 59/18:

Customer Class	Proposed Rate Increase	Annualized Additional Revenue (millions)
Residential	5.2%	$40.4
General Service Small – Non-Demand	3.9%	$6.4
General Service Small – Demand	5.0%	$9.2
General Service Medium	5.2%	$11.2
General Service Large 750V – 30 kV	5.2%	$6.0
General Service Large 30 – 100 kV	5.2%	$5.0
General Service Large >100 kV	5.2%	$8.9
Area & Roadway Lighting	2.6%	$0.7

Source: Manitoba Hydro's Interim Application page 43

Manitoba Hydro's Interim Application proposes no rate increases to the Diesel - Government and First Nation Education energy charge or the tail block energy charge for Diesel – General Service. However, Manitoba Hydro seeks PUB approval to apply the same increases awarded to grid-connected Residential and General Service customers to the equivalent Diesel rate components. Manitoba Hydro's proposal reflects its consideration of:

- maintaining the long-standing practice of charging grid-equivalent rates on the basic monthly charge, and energy charge for the first 2,000 kWh per month for General Service Customers; and,
- current rates for Diesel Residential customers are 9.6% lower than rates of all other residential customers. In Order 100/20, the PUB found that "the Diesel Zone Residential rate should be maintained at the approved August 1, 2017, Residential rate pending the Board's review of a Diesel Zone-specific rate application and Diesel Zone Cost of Service Study filed by Manitoba Hydro. While a Diesel Zone Cost of Service Study has not yet been filed, Manitoba Hydro is proposing to limit further divergence between the Diesel Residential and grid Residential rates given the much higher cost to serve customers within the Diesel Zone.

Manitoba Hydro Position

Manitoba Hydro proposes rate increases differentiated by customer class based on prior Board direction. Manitoba Hydro is of the view that rates differentiated by customer class are entirely within the Board's purview. Manitoba Hydro would not oppose rate increases that were different among the customer classes, and different to the increases it has proposed, so long as Manitoba Hydro was afforded the opportunity to fully recover its revenue requirement.

Manitoba Hydro further states that the proposed rates for Diesel Zone Residential customers are just and reasonable even though there is no new Diesel Zone COSS. The Residential rates are just and reasonable as supported by Manitoba Hydro's Prospective Cost of Service Study PCOSS21, and there is a long-standing policy to maintain the same or similar rates for Diesel Zone Residential customers as for grid-connected Residential customers.

Intervener Positions

The Consumers Coalition recommends no rate differentiation until the COSS can be tested in a full General Rate Application. PCOSS21 was not tested in this interim rate proceeding. PCOSS21 presents an incomplete picture of class cost responsibility because PCOSS21 only reflects the revenue requirements of Keeyask Generating Station partially being in service. When Keeyask is fully in service, additional costs will be allocated to the customer classes and will affect the Revenue to Cost Coverage ratios.

This Intervener further noted that the Board paused rate differentiation in the 2019/20 General Rate Application pending a review of the Prospective Cost of Service Study.

Manitoba Industrial Power Users Group recommends rate increases differentiated by customer class following the methodology proposed by Manitoba Hydro, but with the reduced revenue from the below-average rate increase contributed only by customer classes whose Revenue to Cost Coverage ratio is below 100%.

Manitoba Industrial Power Users Group considers it inappropriate to give above-average increases to customer classes which already have a Revenue to Cost Coverage ratio above 100%. When classes are above 105%, below-average increases are merited, but the reduced revenue from the below-average rate increase should be recovered from the classes benefitting from underpaying their allocated costs (i.e. those customer classes with a Revenue to Cost Coverage below 100%), rather than those already overpaying their allocated costs (i.e. those customer classes with a Revenue to Cost Coverage above 100%).

Manitoba Keewatinowi Okimakanak states former First Nations On-Reserve Residential class customers experienced a 6.5% rate increase on September 1, 2020, following the Manitoba Court of Appeal decision. This was followed by a Government-imposed 2.9% increase on December 1, 2020. In opposing the requested rate increases, this Intervener submitted that a 15.1% increase in rates in 16 months – which is what former First Nations On-Reserve Residential customers would experience if Manitoba Hydro's requested 5% increase is approved - is rate shock.

According to Manitoba Keewatinowi Okimakanak "*A land and territorial acknowledgement has to have some meaning…if it has no meaning, then it's just empty words.*"

In its submissions, Manitoba Keewatinowi Okimakanak quoted the Path to Reconciliation Act: "*To advance reconciliation, the government must have regard to the following principles. No. 4: Reconciliation is furthered by concrete and constructive action that improves the present and future relationships between Indigenous and non-Indigenous peoples.*"

In Manitoba Keewatinowi Okimakanak's view, the affirmed land and territorial acknowledgement and the enactment of the *Path to Reconciliation Act* are more important than a technical concept such as a desire to have all customer classes' Revenue to Cost Coverage ratios within the Zone Of Reasonableness.

According to this Intervener, because the Manitoba Court of Appeal has ruled that there cannot be a First Nations On-Reserve Residential customer class, the only way to provide the necessary relief to First Nations customers is to provide the same relief to all residential customers. The resulting recommendation by Manitoba Keewatinowi Okimakanak is a 0% rate increase for all residential customers.

Assembly of Manitoba Chiefs recommends there be no rate increase to diesel residential customers as there is no evidence to support deviation from current Diesel Zone Residential rates. This Intervener also quantifies the impact of its recommendation as $42,000.00 based on the evidence in the Interim Application.

Board Findings

In order to continue the gradual movement of customer class Revenue to Cost Coverage ratios into the Board-approved Zone of Reasonableness, the Board finds it just and reasonable to approve interim rate increases differentiated by customer class. The Board finds that the differentiated rate increases permit the principled approach approved in Order 59/18 to be continued.

As detailed in Order 140/21, the resulting average rate increases by customer class are as follows:

Customer Class	Average Increase
Residential	3.8%
General Service Small – Non-Demand	2.5%*
General Service Small – Demand	3.6%*
General Service Medium	3.8%*
General Service Large 750V – 30 kV	3.8%
General Service Large 30 – 100 kV	3.8%
General Service Large >100 kV	3.8%
Area & Roadway Lighting	1.3%
Diesel Zone – Residential	0%

* With the exception of the General Service Small and General Service Medium classes, each rate component is increasing by the percentage specified in the table above. Therefore, each rate component increase is equal to the average increase. However, for the General Service Small and General Service Medium classes, the individual rate components are increasing by varying amounts as shown in the rate schedules appended to Order 140/21.

Customers in the Residential class without electric heat using an average of 1,000 kilowatt-hours per month will see an increase of approximately $4 per month. Residential customers with electric heat using an average of 2,000 kilowatt-hours per month will see an increase of approximately $7 per month.

The Board directs that a new Prospective Cost of Service Study be filed with the 2022/23 General Rate Application. This COSS should include revised costs for Manitoba Hydro's major capital projects, including the revenue requirement related to all seven units of the Keeyask Generating Station being in service.

Based on the Interim Application evidence, the Board finds it just and reasonable to maintain the Diesel Zone Residential rates, the Diesel Zone Government and First Nation Education energy charge, and the tail block energy charge for Diesel Zone General Service rates at their current levels. Diesel Zone rates are currently interim rates and are pending finalization based on a 2004 Settlement Agreement that includes Manitoba Hydro, Canada, and First Nations. The Board finds that to consider and finalize the existing interim Diesel Zone rates, a current Diesel Zone Cost of Service Study needs to be prepared by Manitoba Hydro. This topic will be included in the discussions respecting the 2022/23 General Rate Application.

9.0 Payments to Government

Pursuant to *The Water Power Act*, water rentals are paid by Manitoba Hydro to the Province for Manitoba Hydro's use of water resources for its hydroelectric generation. Land rentals are annual payments for the use of Manitoba Crown lands used for water power purposes.

The debt guarantee fee is an annual fee payable to the Province in exchange for the Government's guarantee of Manitoba Hydro's debt (with the exception of Manitoba Hydro-Electric Board Bonds). The fee is calculated using a rate of 1% multiplied by the applicable outstanding debt at March 31st of the previous fiscal year. On new capital projects, the debt guarantee fee is capitalized to the capital project to which the payment of the fee relates, and forms part of the total cost of a capital project.

Manitoba Hydro pays capital tax to the Province at a rate of 0.5% which is applied to the taxable paid-up capital of Manitoba Hydro. The only corporations that pay a capital tax to the Province are Crown Corporations and financial institutions.

Payroll tax is based on a tax rate of 2.15%, which is applied to the Utility's gross payroll.

Business taxes are paid with respect to commercial space occupied by Manitoba Hydro in both leased and owned properties. The Utility pays property taxes to the landlords of leased premises as part of the required lease payments.

Based on the above formulas and information, and as shown in the following table, Manitoba Hydro's Payments to Government have increased based on Manitoba Hydro's capital assets, the total debt incurred to construct its capital assets, and the installed generating capacity of its capital assets.

Payments to the Province ($Millions)

Year Ending	Capital Tax	Payroll Tax	Water Rentals	Debt Guarantee Fee	Total Payments to Province	Total Payments as a Percentage of MH's Gross Revenue
2021	112	12	117	218	459	20%
2020	112	12	115	207	446	20%
2019	101	12	113	186	402	19%
2018	92	12	116	154	374	19%
2017	80	12	122	132	346	18%
2016	69	12	117	118	316	17%
2015	62	12	117	105	296	16%
2014	60	11	118	96	285	15%
2013	55	11	110	90	267	15%
2012	52	10	111	82	256	16%
2011	48	10	114	77	249	15%
2010	46	9	114	72	242	15%
2009	44	9	115	70	239	14%
2008	39	8	117	70	237	14%
2007	37	8	106	68	219	13%
2006	36	7	124	66	235	13%
2005	35	7	104	68	228	15%
2004	35	6	62	67	175*	14%
2003	33	6	95	70	405*	30%
2002	30	5	107	68	211	15%

Source: Manitoba Hydro's Annual Reports

* Manitoba Hydro made one-time special distributions to the provincial Government of $200 million in 2003 and $4 million in 2004.

Manitoba Hydro provided updated information in its Interim Application related to its recent Payments to Government in comparison to other jurisdictions.

Being a capital-intensive utility and reflecting the recently increased capital asset and debt levels, Manitoba Hydro's payment of the Provincial Debt Guarantee Fee and Capital & Other Taxes (excluding municipal grants in lieu of taxes and business taxes) is increasing from the prior fiscal year while the drought has reduced the amount to be paid in 2021/22 to the provincial Government for Water Rentals.

The actual 2020/21 fiscal year payments made by Manitoba Hydro to the Province compared to other Crown-owned electric utilities for the most currently available fiscal year financial information were as follows:

Payments to Governments

($Millions)	Manitoba Hydro (2020/21 Actual)	British Columbia Hydro (2021/22)	Hydro-Quebec (2020)	Newfoundland Labrador Hydro (2020)	SaskPower (2021/22)	New Brunswick Power (2021/22)
Water Rentals	117	295	716	-	25	-
Debt Guarantee Fee	218	-	217	9	-	32
Capital & Other Taxes	124	254	422	-	50	49
Other	-	-	-	-	29	-
Payments to Gov't	**459**	**549**	**1,355**	**9**	**104**	**81**
Gross Operations Revenue	2,353	6,414	13,594	651	2,771	1,834
Payments to Gov't as Percentage of Gross Revenue	***19.5%***	***8.6%***	***10.0%***	***1.4%***	**3.8%**	**4.4%**
Dividends	-	-	1,727	-	48	-
Total Payments to Gov't (with dividend)	**459**	**549**	**3,082**	**9**	**152**	**81**
Total Payments to Gov't (with dividend) as Percentage of Gross Revenue	*19.5%*	*8.6%*	*22.7%*	*1.4%*	*5.5%*	*4.4%*

Source: Interim Application Exhibit PUB-8

Manitoba Hydro Position

Manitoba Hydro testified it is in regular dialogue with the Government as to the revenues paid by the electric utility to the Province. Manitoba Hydro has not made a formal request of the provincial Government to reduce or suspend the payment of water rental fees, capital taxes, or provincial debt guarantee fees. However, Manitoba Hydro testified that it is aware that similar recommendations in this regard by the Brad Wall Commission and in prior Orders of the Board are with the Government for its consideration and review.

Recommendation 2.6 from the Economic Review of Bipole III and Keeyask by the Wall Commission states:

> *Manitoba Hydro's ratepayers should not bear the risk associated with new generation projects that will, for an extended period of time, be commercial in nature, used for exports, and not needed to serve domestic demand. In other words, they should not be used as involuntary equity investors for projects to serve export demand in a risky market. Since it is the Government that approves export contracts and new generation projects like Keeyask, not ratepayers, and the Government that benefits (through water rentals, capital taxes and debt guarantee fees from Manitoba Hydro) even if such projects do not turn out well financially (as discussed in Chapter 4), it is the Government that should bear this risk. Accordingly, if a Government in the future approves a generation project that is, for an extended period of time, primarily for export and not needed for domestic demand, then the Government should bear the risk if this commercial plant is not successful during that period. If the market plan fails and export revenues do not cover the costs of operating the plant during that period and the proportion of capital costs for that part of the plant's operating life, then the Government should reduce or suspend its collection of transfers from Manitoba Hydro until those cost shortfalls are made up. This will have the effect of putting government's budget at risk for decisions that are made by Government, rather than ratepayers.*
>
> *The Commissioner believes that this recommendation will add accountability that will improve decision making at the government level and will provide a proper incentive to the Government of Manitoba to provide greater oversight and accountability with respect to any future major capital projects.*

To implement this recommendation, Government may wish to legislate a reduction or suspension in the transfers that Manitoba Hydro is required to pay to the Government in the circumstances set out above.

Intervener Positions

No Parties took a position in this proceeding with respect to payments made by Manitoba Hydro to the provincial government.

Board Findings

The Board recommends that the Government continue to review the amount and the basis for calculation of the transfer payments from Manitoba Hydro to the provincial Government, particularly in light of the $398 million reduction in Manitoba Hydro's Net Extraprovincial Revenue due to the 2021/22 drought. Despite this revenue reduction, Manitoba Hydro plans to make payments to Government of $438 million in 2021/22 that include $88 million of water rental fees.

According to Manitoba Hydro, it has been forced to borrow $348 million of additional debt to fund its core business operations in 2021/22 due to the drought. While water rental fees paid to the provincial Government declined due to the drought, Manitoba Hydro made increased payments to the Government related to this additional debt on account of the debt guarantee fee paid on Manitoba Hydro's borrowings.

Other utilities in Canada make payments to their respective provincial governments based on the profitability of the utility in a given year. Manitoba Hydro's payments to government are not related to Manitoba Hydro's profitability or financial performance. Instead, the majority of Manitoba Hydro's payments to Government are based on the amount of debt and capital assets, with only water rental fees decreasing with reductions in Manitoba Hydro's annual hydraulic generation, which is a strong determinant of extraprovincial revenue and Net Income.

The Board recommends Government consider amending the criteria and structure of payments made by Manitoba Hydro to the Government to reflect the profitability of Manitoba Hydro. In the Board's view, electricity ratepayers are disadvantaged when Manitoba Hydro is required during a drought to make substantial payments to Government for the benefit of taxpayers, as electricity ratepayers face increased electricity rates to mitigate the substantial financial losses incurred by Manitoba Hydro due to the same drought.

10.0 Manitoba Hydro's Next General Rate Application

Long-Term Financial Forecasts

The September 22, 2021 directive from the Minister of Crown Services to the Manitoba Hydro Board of Directors contained the following two specific directives:

- Manitoba Hydro is directed to take all steps necessary to proceed with submission of an interim rate application to The Public Utilities Board (or other application as determined by The Public Utilities Board); and
- Manitoba Hydro is directed to engage with The Public Utilities Board on submitting multi-year general rate applications.

In response to the first directive, Manitoba Hydro filed its 2021/22 Interim Rate Application with the Board on November 15, 2021, to address the financial effects of the current drought and the financial health of the corporation.

In response to the second directive, Manitoba Hydro provided evidence at the hearing that it will file a General Rate Application in 2022.

While not within the scope of this Interim Application, Manitoba Hydro briefly explained that it has developed a new long-term vision known as 'Strategy 2040' to identify future opportunities and challenges in serving its customers. Manitoba Hydro maintains the energy sector worldwide has seen unprecedented change in recent years due to the key trends of decarbonization, digitalization, and decentralization which are increasingly reshaping the energy landscape. Manitoba Hydro sees the pace of these trends being driven by: government policy interventions, technological advancements, economics, customer preferences, and climate change.

In order to implement Strategy 2040 and translate strategy into action, Manitoba Hydro is developing a range of initiatives that will create the foundation of future work. One of the key initiatives under Strategy 2040 is Manitoba Hydro's development of an Integrated Resource Plan ("IRP"), first recommended by the Board in its 2014 NFAT Report to Government. An IRP is a long-term roadmap to guide decisions in response to the evolving energy landscape, its impacts on Manitoba Hydro's customers, and changes in energy supply and delivery systems. Manitoba Hydro presented evidence that it initiated the process to begin preparing for the development of an IRP with the release of a general customer survey with respect to customers' electricity and natural gas needs. Manitoba Hydro further stated that the IRP planning process will evolve over the following year and a half with targeted completion by the summer of 2023. It is expected that, when completed, the IRP will inform Manitoba Hydro's future rate applications to the Board and Manitoba Hydro's investment decisions on both gas and electric system assets.

According to Manitoba Hydro, a significant outcome from the development of the IRP is that it will help build a more comprehensive and informed long-term financial forecast that will support future General Rate Applications to the Board. The IRP will provide critical input to the long-term financial forecast with respect to underlying assumptions that need to be considered in the context of the evolving energy landscape, anticipated impacts to Manitoba Hydro's system, and how Manitoba Hydro will need to respond to these. Given this critical input, until such time as the IRP development is complete, any long-term financial forecasts developed will be less robust and may not include the full ramifications or revenue requirement impacts of the potential energy sector changes on Manitoba Hydro's future financial position.

Manitoba Hydro Position

Manitoba Hydro's President & CEO testified in the hearing that Manitoba Hydro has completed Strategy 2040 and it has now been approved by the Manitoba Hydro Board of Directors. The President & CEO indicated that she was looking forward to sharing Strategy 2040 now that it was formalized and stated Strategy 2040 has "…come out of the oven fully baked and ready to serve".

Work to develop Manitoba Hydro's first IRP, and other foundational strategic initiatives including the development of disciplined planning and risk frameworks, will still be underway throughout calendar 2022 when Manitoba Hydro will begin preparing its next General Rate Application to the Board.

On the topic of long-term financial forecasts, Manitoba Hydro's evidence is that it is unable to prepare a meaningful long-term financial forecast because there are two key missing components: an Energy Policy by the Province of Manitoba (which is expected to define the role of Manitoba Hydro in such an Energy Policy) and an IRP by Manitoba Hydro (which is expected to define how Manitoba Hydro will serve the Manitoba load in recognition of the Province's Energy Policy). Manitoba Hydro testified that, ideally, it would not work on these two projects in parallel, however both were commenced in the fall of 2021. The Energy Policy process is expected to conclude in 2022 while the IRP will take 18 months to complete. Only after these documents are completed does Manitoba Hydro envision a long-term financial forecast being prepared that could be utilized in the Board's rate-setting process.

Manitoba Hydro recognizes the challenges placed on the Board by not having a longer-term view of Manitoba Hydro's financials when considering rate applications before it. Manitoba Hydro indicated that it will work with the Board on the filing requirements for the 2022/23 General Rate Application which will allow the Board to complete its review while Manitoba Hydro's foundational work is underway.

In the interim, according to Manitoba Hydro's evidence, its Enterprise Planning Group is currently working on a 2-3 year financial forecast.

Having testified that it does not have a long-term financial plan prepared for rate-setting purposes, Manitoba Hydro acknowledges it has prepared long-term financial plans to demonstrate to debt-rating agencies a scenario where Manitoba Hydro achieves certain financial metrics from the now-withdrawn Bill 35.

With respect to the next General Rate Application, Manitoba Hydro indicated it will engage with the Board on a path to achieving annual rate increases, including options that would allow the utility to seek an increase in 2022/23. In addition, Manitoba Hydro will engage with the Board on ways to ensure the regulatory process is as efficient and effective as possible and in the best interest of Manitoba Hydro's customers. Manitoba Hydro respectfully requested that the Board not provide any specific directives related to the timing and parameters of the upcoming General Rata Application in its Order.

Intervener Positions

To restore ratepayer trust and confidence in the rate-setting process, the Consumers Coalition recommends any rate increase be time-limited and expire on January 1, 2023. This Intervener further recommends conditions on the rate increase, including reactivation of the Status Update proceeding if Manitoba Hydro has not provided the Board with a firm timetable for filing a General Rate Application by June 1, 2022. Furthermore, as Manitoba Hydro's lack of transparency has undermined consumer confidence, the Consumers Coalition recommends Manitoba Hydro should be directed to engage with stakeholders about rate-setting strategy prior to filing its next rate application in order to begin to restore confidence in Manitoba Hydro's rate-setting process.

The Consumers Coalition notes that Manitoba Hydro has the ability to seek rate relief in 2022/23 if unfavourable water conditions continue.

Manitoba Industrial Power Users Group maintains that, contrary to the submission of Manitoba Hydro, the Board should not remain silent on a date or content for Manitoba Hydro's filing of a General Rate Application in 2022.

Manitoba Industrial Power Users Group submits that given Manitoba Hydro is able to produce a long-term financial forecast for debt-rating agencies, it is not credible for Manitoba Hydro to now assert that it cannot produce a similar forecast for the Board with all the details of the short-term and long-term assumptions used by Manitoba Hydro.

The Assembly of Manitoba Chiefs notes that pursuant to a Ministerial Directive, Manitoba Hydro has been ordered to work with the Board on a General Rate Application hearing in 2022/23, yet has budgeted a 0% increase in its 2022/23 financial forecast. This Intervener states that this is contrary to Manitoba Hydro's oral testimony that it will be seeking a rate increase for 2022/23.

The Assembly of Manitoba Chiefs cautions that granting a 5% increase effective January 1, 2022 would give Manitoba Hydro more leeway to operate longer without appropriate regulatory oversight.

Board Findings

The Board notes that Manitoba Hydro presented evidence that it intends to seek new rates in 2022/23, even though its 2022/23 Plan budget reflects no rate increase in 2022/23.

In Order 128/21, the Board found long-range financial targets to be out of scope for this Interim Application. Besides being a controversial issue that ought not to be addressed in an Interim Application, any evidence on this topic will not be complete without a current long-term financial forecast. However the Board finds that long-range financial forecasts will be essential for the upcoming GRA.

The Board finds that the regulatory world cannot stand still while Manitoba Hydro waits to develop a long-term financial forecast pending completion of the provincial Energy Policy and its own Integrated Resource Plan. The Board is not prepared to wait until the provincial Energy Policy and Manitoba Hydro's Integrated Resource Plan are complete before the Board sees Strategy 2040 and a long-term financial forecast. Considering Manitoba Hydro has now confirmed that Strategy 2040 is ready to be 'served', the Board directs Manitoba Hydro to file Strategy 2040 with the Board as soon as released to stakeholders and by no later than November 15, 2022, and be included in the documents discussed with the Board for inclusion in the 2022/23 General Rate Application.

For purposes of the 2022/23 General Rate Application in which January 1, 2022, interim rates are examined, the Board directs Manitoba Hydro to include a long-term financial forecast which is to extend more than the two to three years that Manitoba Hydro indicated it is currently constructing. The long-term financial forecast that Manitoba Hydro is to provide shall be a forecast out at least 20 years – the same period as Manitoba Hydro's forecast provided to debt rating agencies – with all assumptions explained in similar form to what has previously been presented by Manitoba Hydro.

In Order 137/21, the Board established November 15, 2021 as the deadline for the filing of Manitoba Hydro's next General Rate Application. This date recognizes that interim rates ought not remain in place any longer than is reasonably necessary. By that date, the Board expects a new proceeding to have been commenced, to examine whether the interim rates approved in Order 140/21 should be varied or finalized.

Therefore, recognizing the precise timing and content of Manitoba Hydro's 2022/23 General Rate Application has not been finalized and will be the subject of further discussion, and recognizing the Board finds it reasonable that the interim rates approved in Order 140/21 should be further examined as soon as reasonably possible, the Board has determined and now varies its prior decision such that the interim rates will remain in effect only until November 30, 2022, (not November 15, 2022 as indicated in Order 137/21 and Order 140/21) unless Manitoba Hydro has filed a General Rate Application by November 15, 2022 seeking rates for 2022/23, and for 2023/24 should it so decide, and to confirm the 2021/22 interim rate increases in Order 140/21. The November 30 date reflects Manitoba Hydro's long-standing policy of adjusting rates on the first day of the month.

Even though water flow conditions are its single largest risk factor when it comes to earnings, Manitoba Hydro has no reliable long-term precipitation forecasting capability. Without reliable long-term forecasting, Manitoba Hydro must use its judgment as to when to switch its operations from seeking to maximize its extraprovincial revenues to preserving water for energy reliability purposes for domestic and firm export customers. As seen in this Interim Application, there are significant financial consequences to Manitoba Hydro ratepayers due to a drought that Manitoba Hydro is unable to forecast. The Board finds that additional expert evidence at the 2022/23 General Rate Application that examines the 2021/22 interim rates is required to determine what, if any, additional drought forecasting options may exist to mitigate Manitoba Hydro's drought risk.

In this Interim Application, Manitoba Hydro advised the Board that it discontinued the use of 108 years of water flow data to forecast Net Extraprovincial Revenue for the current and next fiscal years. Instead, Manitoba Hydro uses the most recent 40 years of water flow data to model its reservoir and generation operations and translate that information into its short-term financial projections. However, Manitoba Hydro plans to continue using the 108 years of water flow data for its long-term financial forecasting.

While Manitoba Hydro indicated the 40 years of data improve the quality of the data for its modeling purposes, the Board notes that the average Net Extraprovincial Revenue, and therefore Net Income, is $19 million less using the 40-year average compared to the 108-year average. The Board further notes that the median (or P50) result of the 40 years of data is $36 million less than the median result using 108 years of data. The Board finds that this issue should be further explored, including comparisons with other jurisdictions and industry best practices, in the 2022/23 General Rate Application when the 2021/22 interim rates are reviewed. Manitoba Hydro should consider conducting a retrospective analysis that investigates whether the 40 year water flow record provides more reliable financial forecasts than the long-term (100+ year) water flow record.

Financial Metrics

While citing that contentious financial metrics ought not to be considered or debated in its Interim Application, Manitoba Hydro provided evidence for 2021/22 on this topic to provide a full financial “status update” to the Board and to demonstrate that its proposed interim general revenue increase and resulting rates are just and reasonable.

The following is a list of financial metrics Manitoba Hydro is tracking and considering as part of its ongoing internal Key Performance Indicator review while acknowledging that Manitoba Hydro does not presently have targets for each of these metrics.

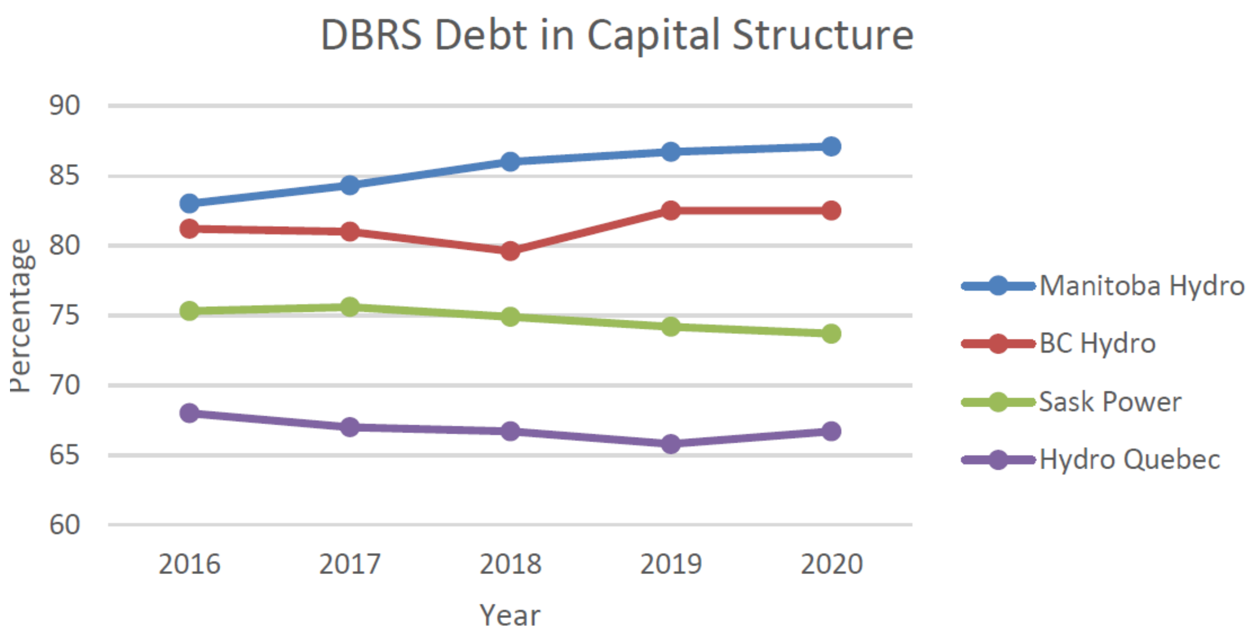
- Debt Ratio: the portion of assets that are financed by debt rather than equity. Related to the debt ratio are the debt-to-equity ratio and equity level referred to in prior Orders such as 59/18.
- EBITDA Interest Coverage Ratio: the number of multiples of earnings before interest, taxes, depreciation and interest can cover interest payments on the outstanding debt.
- Cash Surplus/(Deficiency) for Core Business Operations: a deficiency indicates borrowings are required to fund business activities other than the major capital projects.
- Interest Paid as a Percentage of Total Revenue: the portion of every dollar of revenue that is needed to service the interest payments on the outstanding debt.

Manitoba Hydro supports, as a general and reasonable roadmap to gradually reducing the utility’s leverage over a 20-year timeline, the debt ratio targets embedded in the now-withdrawn Bill 35 of:

- 87% by March 31, 2025
- 84% by March 31, 2030
- 78% by March 31, 2035

- 70% by March 31, 2040

Manitoba Hydro provided a comparison of its debt ratio with the debt ratios of other Crown-owned electricity utilities, as shown in the graph below.



Manitoba Hydro's initial 2021/22 Budget, which assumed a range of 40 possible water flow conditions for the year and a 3.5% rate increase effective October 1, 2021, projected Net Extraprovincial Revenue of $509 million and Net Income of $177 million. The initial 2021/22 Budget projected sufficient earnings and cash flow to avoid borrowing to fund core business activities, an EBITDA Interest Coverage Ratio just under 1.7, it maintained the debt ratio at 86%, and prevented interest paid as a percentage of total revenue from exceeding 40%.

However, the 2021/22 Forecast financial position, approved November 10, 2021 by the Manitoba Hydro Board of Directors, projects Net Extraprovincial Revenue of $111 million, a $190 million net loss, and $348 million of additional borrowings to fund core business activities. This update results in a 1% deterioration (increase) of the debt ratio to 87%, an EBITDA Interest Coverage Ratio of 1.36 (down from 1.68), and interest paid as a percentage of total revenue increases to 42% (from 40%).

Electric Segment	**2021/22 Forecast**	**2021/22 Budget**	**Change**
Proposed Rate Increase	5.0%	3.5%	1.5%
Net Income (Loss)	($190)	$177	($366)
Net Export Revenue	$111	$509	($398)
Cash Surplus/(Deficiency) to Fund Core Operations	($348)	$62	($410)
EBITDA Interest Coverage Ratio	1.36	1.68	(0.32)
Interest Paid as a % of Total Revenue	42%	40%	2%
Debt Ratio	87%	86%	1%

Source: Manitoba Hydro's Interim Application page 24

Even with a 5% revenue increase commencing January 1, 2022, Manitoba Hydro calculates that it will borrow approximately 90% of the projected $398 million of lost Net Extraprovincial Revenue resulting from the current drought.

<u>*Board Findings*</u>

In Order 59/18, the Board made findings on Manitoba Hydro's financial metrics:

> *The Board accepts Morrison Park Advisors' evidence that debt-to-equity is a questionable metric for a vertically integrated monopoly Crown utility with a debt guarantee from the provincial government. The equity level target does not have the prominence suggested by Manitoba Hydro given the context in which the Utility operates. The concern regarding the value of the equity level target is compounded when Manitoba Hydro is going through an unprecedented major investment period to more than double the value of its assets in the next four years. As noted by Manitoba Hydro's external consultant KPMG, there is a "practical recognition that this target will not be met during a period of large capital expenditures when newly constructed assets are placed in service. Accordingly, the 75/25 could remain the long-term objective." The Board supports this view. The Board agrees with the evidence that there is a cost associated with equity as equity is provided by ratepayers who could otherwise use those funds. As such,*

the Board is not prepared to look at the issue of pacing to achieve a particular equity level target at least until the current phase of major capital construction is completed, now projected by Manitoba Hydro to be in 2024.

…

The Board finds that, while important, care must be taken to avoid placing too much weight on reports by credit rating agencies. The Board accepts that credit ratings and capital markets are related, but are not the same thing.

The Board is of the view that these findings remain valid and relevant.

With respect to the comparison of Manitoba Hydro's debt ratio to the debt ratio of other Crown-owned electricity utilities, the Board finds that context is required to properly understand the comparisons. For example, there was a suggestion that BC Hydro's current debt ratio reflects the completion of the Site C hydroelectric generating station. However, that $16 billion project has not yet been completed. Hydro Quebec's debt ratio reflects its mature asset base. SaskPower's debt ratio reflects its primarily fossil fuel-based generation fleet as opposed to higher-capital hydroelectric generating stations. These are in contrast to Manitoba Hydro's situation where it has doubled its assets since commencing construction of Keeyask Generating Station and Bipole III. Any comparisons of financial metrics among Canadian Crown energy utilities at the 2022/23 GRA will require context for the Board to consider the information.

11.0 Recommendations to Government

The Board makes the following recommendation to the Government of Manitoba:

1. The Government of Manitoba should consider amending the criteria and structure of payments made by Manitoba Hydro to the Government to reflect the profitability of Manitoba Hydro. In support of this recommendation, the Board cites the $398 million reduction in Manitoba Hydro's Net Extraprovincial Revenue due to the 2021/22 drought and the increase in debt guarantee fee paid by Manitoba Hydro to the Government due to the additional $348 million of borrowings resulting from the drought.

12.0 IT IS THEREFORE ORDERED THAT:

1. Directive 3 in Order 137/21 and Directive 2 of Order 140/21 **BE AND ARE HEREBY VARIED** such that the interim rate increases approved in those Orders will remain in effect only until November 30, 2022, unless Manitoba Hydro files a General Rate Application by November 15, 2022, to confirm the 2021/22 interim rate increases, to seek rates for 2022/23, and for 2023/24 should it so decide. If Manitoba Hydro does not file a General Rate Application by November 15, 2022, the rates will revert to those in effect prior to Order 140/21.

2. Manitoba Hydro file, by February 28, 2022, updated electronic schedules of its revenue requirement for the 2021/22 and 2022/23 fiscal years reflecting the decisions and rates approved in Orders 137/21 and 140/21.

3. Manitoba Hydro file, as soon as released to stakeholders and by no later than November 15, 2022, a complete copy of Strategy 2040.

4. Manitoba Hydro include in its 2022/23 General Rate Application its long-term financial forecast of at least 20 years together with its underlying assumptions.

5. Manitoba Hydro include in its 2022/23 General Rate Application its updated Prospective Cost of Service Study which includes revised costs for Manitoba Hydro's major capital projects, including the Keeyask Generating Station.

6. At the 2022/23 General Rate Application, Manitoba Hydro demonstrate the savings in Business Operations Capital that are found by showing the updated Business Operations Capital spending compared to the spending proposed at this interim proceeding.

7. At the 2022/23 General Rate Application, Manitoba Hydro demonstrate the savings in O&A expenses that are found by showing the updated O&A expenses compared to the O&A expenses proposed in this interim proceeding.

Board decisions may be appealed in accordance with the provisions of Section 58 of *The Public Utilities Board Act*, or reviewed in accordance with Section 36 of the Board's Rules of Practice and Procedure. The Board's Rules may be viewed on the Board's website at www.pubmanitoba.ca

THE PUBLIC UTILITIES BOARD

"Robert Gabor, Q.C."
Chair

"Darren Christle, PhD, CCLP, P.Log., MCIT"
Secretary

Certified a true copy of Order No. 9/22
issued by The Public Utilities Board

Secretary

Appendix A: Appearances

PARTY	LEGAL COUNSEL
The Public Utilities Board	Bob Peters
Manitoba Hydro	Brent Czarnecki, Jessica Carvell, Odette Fernandes
Assembly of Manitoba Chiefs	Carly Fox, Emily Guglielmin
Consumers Coalition	Byron Williams, Katrine Dilay, Chris Klassen
Manitoba Industrial Power Users Group	Antoine Hacault
Manitoba Keewatinowi Okimakanak Inc.	Marcus Buchart

Appendix B: Hearing Witnesses

PARTY	WITNESSES
Manitoba Hydro	Jay Grewal, President & Chief Executive Officer;
	Aurel Tess, Vice President & Chief Financial Officer;
	Alistair Fogg, Director, Enterprise Risk Management;
	Kevin Gawne, Manager, Energy Supply Planning;
	Shannon Gregorashuk, Director, Rates & Regulatory