THE SASKATCHEWAN RATE REVIEW PANEL

SASKPOWER 2016 AND 2017 RATE APPLICATION

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Transcript of Proceedings of
A PUBLIC MEETING
held by the
Saskatchewan Rate Review Panel
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APPEARANCES:

Saskatchewan Rate Review Panel:
Albert Johnston (Chairperson)
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SaskPower Panel:
Mike Marsh
Sandeep Kalra
Darren Foster

THE CHAIRPERSON: Good evening and welcome to the SaskPower rate application public meeting. My name is Albert Johnston. I'm the Chair of the Saskatchewan Rate Review Panel. We are the body charged with reviewing rate applications from the three major crowns in Saskatchewan, and tonight we'll be hearing from SaskPower about their rate application for 2016/2017.

This process is part of our review of the application, and we seek public input in many ways, from our website and as well as e-mails. You can follow us on Twitter and so on, and we welcome public participation.

This public meeting, which is also being streamed on your computer, will be recorded, and ultimately you'll be able to go to our website and view any or part of the presentation.

We will hold all questions until the end, and you will be able to type questions into your computer as we go, and we will deal with those. If you are on the phone, your phone -- phone lines are muted, but we will open them up at the end if there are any questions at that time, and we will deal with those.

As I said, we certainly encourage public participation in this process. It is important, from the Panel's point of view, that we hear from the public. We need to know what people are thinking, and we hope that you're able to do that.

We also have one presenter besides SaskPower tonight, and I'll introduce him later.

With that, I'll now turn it over to SaskPower, and we have today three people from SaskPower, and I'll -- the first speaker will be Mr. Mike Marsh, who is the president and CEO.

MR. MARSH: Good evening. I'm pleased to be here tonight along with Sandeep Kalra to my left, SaskPower's chief financial officer, and Mr. Darren Foster, manager of corporate planning.

First of all, we'd like to say that we appreciate the work of the Saskatchewan Rate Review Panel and the opportunity to update our customers on a variety of fronts related to our 2016 and 2017 rate application. I'd like to thank all of those who made time in their busy schedules to participate in the rate review process whether tonight or through correspondence with the Saskatchewan Rate Review Panel.

We value the views of our customers and stakeholders and recognize the importance of ongoing two-way dialogue. In a few minutes, you will hear more detail about our 2016 and 2017 rate application. In the meantime, I'd like to begin by telling you that we take any potential rate increases very seriously. We recognize that any increase in electricity cost for our customers is a stress for Saskatchewan's households, farms and businesses. However, we also have the responsibility to ensure that our company maintains a strong financial foundation so that we can continue to provide a reliable and sustainable supply of electricity for our customers in the province.

SaskPower is requesting a system average rate increase of 5 percent effective July 1st, 2016, and 5 percent effective January 1st, 2017.

Our company's requirement for rate increases is driven primarily by its need to make investments in aging infrastructure and new capacity to support Saskatchewan's growing demand for electricity. SaskPower continues to set records for the total amount of power needed by customers at one time. The most recent record was a peak load of 3,640 megawatts in January of this year, and the demand for new electrical services has continued to remain strong. We have added an average of 9,500 customer accounts each year over the past 5 years. Meanwhile, the province has seen a 16-percent increase in load growth over the past 5 years, and increased demand is expected to continue into the foreseeable future.

While the demand for power grows, SaskPower is also facing the pressing need to renew its aging electrical infrastructure. Much of the province's electrical system was built 30 to 50 years ago and has reached the end of its productive life. In response, SaskPower is making historic investments. In the past five years our company has spent over six billion dollars on capital investments and power purchase agreements. Going forward, we are forecasting the need to keep making capital investments of approximately one billion dollars each year. These investments are part of SaskPower's ongoing commitment to renew and improve the system.

In recent years, the requirement for capital spending has increased substantially from 280 million dollars in 2007 to 990 million dollars in 2015. Within last year's capital program, SaskPower invested nearly 590 million dollars on growth and compliance initiatives and nearly 390 million dollars to sustain existing infrastructure.

As an example of how SaskPower's capital funds are spent, the past fiscal year saw a number of projects completed including the on-budget commissioning of a 510-million-dollar expansion of Saskatoon's Queen Elizabeth Power Station, which added about 204 megawatts to the grid; the on-budget completion of the 327-million-dollar I1K transmission line, a 300-kilometer project in the far north which offers improved service and reliability to the people of northern Saskatchewan; and the completion of over 9,800 new customer account connections at a cost of nearly 200 million dollars. These are just a few examples of the kind of work that is required today and into the future.

We are continually looking for efficiencies to mitigate the impact of our capital program on rates. We want to make sure that we are using our customers' money wisely. In 2015 alone, SaskPower reduced its budgeted operating maintenance and administration spending by 38 million dollars. This was done by freezing management salaries, reducing spending on training, travel and contract services and reducing the budgeted number of employees by not filling vacancies as people retire or leave the company. This rate application proposes additional OM & A cuts of 53 million dollars over the next three years. In 2015 SaskPower also cut 210 million from its capital program by eliminating or deferring capital projects. This rate application proposes further cuts of 790 million dollars to capital spending over the next three years.

Our efforts to streamline our operations will continue throughout all areas of our business. Efficiency and quality will become even more important as we balance the need to minimize rate increases with the need to sustain and grow Saskatchewan's electricity system.

Throughout this rate application process, we look forward to working in a timely, open and collaborative manner with our customers, with our stakeholders and the Saskatchewan Rate Review Panel, and as we look ahead to Saskatchewan's future, we look forward to continue to deliver on our mission, which is ensuring reliable, sustainable and cost-effective power for our customers. Thank you very much.

MR. KALRA: My name is Sandeep Kalra. I'm chief financial officer for SaskPower, and I'll take you through a detailed -- a more detailed rate application. I have roughly 20 -- 20 slides to cover.

As Mike mentioned, we are requesting a rate increase of 5 percent effective 1st of July 2016 and a second rate increase effective 1st of -- 1st of January 2017 of 5 percent. We are requesting a flat-rate increase, which means that most classes are getting the same rate increase. The primary driver for rate increase, as Mike mentioned, is increase in our capital program. We have been and plan to continue to invest roughly a billion dollars a year to maintain and expand our infrastructure. This rate increase will enable us to meet our ROE target of 8.5 percent for the first time since 2011 in 2017/2018 and keep our debt ratio to around 75 percent.

The customer impact is

shown on this slide, our revenue to revenue requirement measure, R/RR measure. It measures revenue that is generated from each customer class against the cost of providing the service to that class. An R/RR ratio less than 1 means that the customer class is paying less than what it cost to service them while an R/RR ratio greater than 1 means customer class is paying more than the cost to service them. Because of contract class with some lengthy contracts, every other class was required to take a 5.1 percent rate increase while the contract class gets an increase of 3.9 percent. An R/RR ratio will remain fairly tight within the industry accepted norm of 0.95 to one oh five with the exception of rural residential rate. We are planning of -- planning on implementing rate simplification in our next rate application, and the lower R/RR ratio for the rural group means there will be less of an adjustment when we rebalance.

This slide shows a summary which Hydro Quebec puts together. It studies the electricity rates in Canada and the United States. This report is off -- dated April 1st, 2015, and that's the latest results we have. We benchmark our rates against other thermal utilities that are similar to SaskPower and rely largely on fuel sources such as natural gas, coal and nuclear to produce their electricity. Our rates are now on aggregate at about on par with the rates of other thermal utilities in Canada. However, not all the classes are the same. The residential rates are about 7 percent higher in Saskatchewan than the rest of Canada. On the other hand, large industrial customers pay about 11 percent lower than thermal Canadian average. The higher rates for residential customers is largely due to the cost of distribution to transmit electricity to customer homes, and I'll follow that up in a future slide.

The primary driver for our investment and our rate increase is aging infrastructure. Our infrastructure is quite old by industry standards and requires significant investment to maintain it. Our coal assets were largely built in the seventies and eighties, are coming to the end of their useful life. Hydro generation is even older. Some units go back to 1929, and the latest one was built in 1980s.

Our distribution poles have a mean average of about 38 years. The industry average and recommended average is 25 years. Our transmission system is in somewhat better shape, but it's still quite old by industry standard. We are looking to spend from 400 to 400 (sic) million dollars a year just to maintain these assets.

This chart shows the number of customers that pay for per kilometer of line. SaskPower has one of the largest service areas. We have roughly 150,000 kilometers of wires. We have 3 customers that pay for that line, and if you look at the other extreme, Hydro Quebec has 28 customers paying for that line, so as a result, our distribution charges per customer tend to be a little bit higher, and that's why I mentioned our residential rates are higher as compared to the other utilities in Canada.

Our rates historically have tracked inflation at roughly 3.4, 3.5 percent over the last 20, 30 years. There are periods where the rate increases outstrip the inflation when we are investing significantly, and then there are other periods when the investment holds -- we hold back on investment and its normal sustainment period where the rate increases have been lower than the inflation rate, but we have tracked over this period on average very close to the rate of inflation.

Turning to our financials, this slide shows our operating income, the blue bars, and the operating ROE, which is the green line. With the approved rate increases, we are expected to return to running an ROE of 8.5 percent in 2017/2018, which would require an operating income of 208 million. This level of income is what we need to earn to be able to afford to invest roughly a billion dollars of annual capital investment.

Our operating cash flow tends to be around 400, 450 million dollars.

200 would be -- out of that would be profits, and the rest would be non-cash, items like depreciation, etc. Without these additional earnings, our debt load will become unmanageable. More on that later.

This slide shows return on equity. Our return on equity in the last few years has been the lowest of any utility in Canada. We were around 2 percent in 2014, which is, as I mentioned, the lowest in Canada. At 4.7 in 2014/2015, we would also be the lowest in Canada. The line across this chart shows our target return of 8.5 percent, and then it shows how are the other utilities doing as compared to that.

This chart shows the sales growth. The higher load in 2016/'17 is due partly to the warm weather, warmer than normal weather in 2015. This understates the growth in 2015 and overstates the growth in 2016/'17, which is about 1 percent. The blue line at the top, that shows the peak demand which is -- which we expect in these years. That continues to grow, and our system is built to meet that demand. Even if that demand is, you know, one day of the year or two days of the year, our system has to be capable to be able to meet that demand.

In the past there was some criticism of our forecasting of our -- the load forecasts. Over the last few years we have improved that substantially. What this is showing is that in 2012, the actual 2011 forecast, we have a variance of 6.5 percent. We started using, besides the customer information, other information which comes from the Ministry of Economy and other sources as well, and over time we have improved the accuracy of our forecast and, as a result, accuracy of our load -- accuracy of our application -- information in our application as well, and over the last few years, you will see the variance was only 0.7 percent and 0.2 percent from what we had put in the load forecast.

Now, on to other revenues. Exports and trading margins used to be relatively high 'til 2011, 2013. Economy in Alberta is soft. The margins are low. The price of electricity has come down, so we do not expect to make the same margins and export the same amount to Alberta. This used to contribute quite significantly to the bottom line. It still does, but the amounts have moderated quite a bit.

This chart shows other revenues, and this has, I think, like CO2 sale, CCTF revenues and other miscellaneous revenues and customer inspection revenue and customer contributions. They peaked in 2015. We expect them to moderate as the customer activity, new connect activity is moderating a little bit, but it's still at a quite -- quite a healthy level of 130, 135 million dollars.

Now, on to the cost drivers now, and the first one is fuel and purchased power. The blue bars show increase of -- increase, you know, from 485 in 2011 to up to 700 million dollars. This is largely driven by yields of more and more natural gas in our generation mix. That is -- that is the fuel that we use in the margin. Also this is affected by hydro availability in any given year. In good years we can back off natural gas and use more hydro. In the rate application and the forecast, we normally use the median hydros. This year our hydro will be significantly lower than median.

The second big cost category for us is operating maintenance and administration expense. This shows in 2015 we actually had an actual reduction of cost from 656 million dollars to 634. That was due to deferral. That was due to cost containment, not hiring, keeping a lot of positions open and cutting down on, you know, travel and consulting and training and a lot of other costs.

Costs are going up as the volumes -- as the size of our business grows, as we have more fleet to maintain, but what the bar -- what the lines are showing is we are trying to keep the rate of growth of our operating maintenance, admin. expense to the level of rate -- to the level of increase in the volumes of sale, so that is the green bar, and the blue bar -- so blue bar is our OM & A growth. Green bar is the growth in our volumes. The orange bar -- it's not the bars. The orange line at the top shows the impact of inflation, so what we're doing is we are managing -- we are able to kind of manage the OM & A growth to below the inflation and growth rate.

The last driver and the most significant driver -- cost driver for us is capital-related expenses. This includes depreciation, finance, capital taxes and some of the other expenses. Every one billion dollar in capital spend results in roughly 70-to-80-million-dollar increase in -- increase in depreciation and finance charges. These costs have doubled since 2011, and we expect them to become even more significant as we continue to invest in our systems.

This slide shows the drivers of the rate increase for the last three, four years. The single biggest one, as I mentioned, is capital-related expenses, 62 percent. Fuel and purchased power is the next one, 25 percent, and that is because we're using more natural gas, and it also depends on what the price is and also, as I said, the mix in any given year, and the smallest part of that increase is the OM & A increase of 13 percent.

Capital spend over the last few years, so in 2013 it was two billion dollars including the IPP. Since that we have invested or plan to invest over seven billion dollars to the end of 2018/2019, and as a part of this rate application, we have gone through our capital spending through a fine-tooth comb and have deferred capital spending of roughly a billion dollars, and I'll show you that in a -- in a slide, and this results into a savings of roughly 30 to 40 percent on our rates.

This slide provides more information as to what that capital spend is. We've broken that down into three buckets. Sustainment investment, so that is on our existing assets. These assets already are there. We need to maintain them. The second is growth and compliance. This is mainly to add new capacity and to connect the customer, and the third one is anything else that doesn't fall into those buckets, and those tend to be IT investments and, you know, buildings and things of that nature.

So you would see the sustainment capital is roughly -- run rate is 400 million to 450 million. Growth depends on any given year. If we have high customer connects like 740, 750, once the customer connects start moderating, the numbers are in 500 and change. It also depends on the timing of when major projects are coming to fruition and when we're spending money on that, so it fluctuates quite a bit. Our capital budget rough -- run rate roughly a billion dollars a year.

This slide provides an example -- further example of what these projects are that we've kind of worked on, sustainment capital, wood pole replacement, circuit breaker replacement, rural rebuild, E.B. Campbell life extension, and the growth ones are Pasqua to Swift Current transmission line, many transmission lines mentioned over here. Tazi Twe hydroelectric station, we haven't started working on it, but that would be another significant project that we would take on.

This slide shows our debt-to-debt ratio. Our long-term range is 60 to 75 percent. When we started in 20 -- 2009/2010, the ratio was 60 percent. We have taken advantage of our very low debt ratio at that point in time and let it run up a little bit to roughly 75 percent, and the reason for that was we wanted to invest heavily in the system but at the same time wanted to kind of moderate the impact, the rate impact, so we have let it run, but unfortunately this has run its course. We are at a point of that we are touching the top threshold of our debt ratio. As I mentioned, the rate is 60 to 75, and we would need further rate increases from now on to be able to maintain it at this level.

This slide shows our -- comparing our debt with the rest of the industry. We have the fourth-highest debt ratio in the country. As I said, we're getting close to the top of the range for our company, and we would like to kind of maintain it at this level or slightly below this level.

This is some of the steps we have taken to reduce the rate impact on OM & A. We reassessed the budgets. We saw the slowdown. We saw the impact on the customers, and we've been able to defer or eliminate OM & A of roughly 90 million dollars from our original estimates for the four years. We've done the same thing for our capital spending, and we have deferred. These cannot be eliminated, but these can be deferred, our capital budget of a billion dollars, to future years.

We have also -- we have also been working on improving efficiency and effectiveness of our business operation since 2009. We have worked on many many initiatives and saved half a billion dollars or avoided additional costs of half a billion dollars since then. This is in overhaul maintenance, procurement, changing our capital structure a little bit and in new connect, and on the conservation program, we have helped our customers save energy of 303 gigawatt hours and, from our point of view, the total capacity savings is roughly 107 megawatts.

So summary once again. The rate increases are required primarily to fund our capital investments. We expect to meet our ROE target of 8.5 percent not this year but the year after that, 2017/2018. The rate increase will permit us to maintain our debt ratio to stabilize at 75 percent. Without the rate increase, the financial health of the corporation could be at risk, and this request is consistent with the corporation's strategy of capping annual rate increases at 5 percent or less.

So that's all we had for presentation. Thank you.

THE CHAIRPERSON: Thank you, Sandeep. I would now like to call on Kent Smith-Windsor, who is here representing the Saskatoon Chamber of Commerce, to make his presentation.

MR. SMITH-WINDSOR: Thank you very much. I didn't realize I had to present in public, but I'm happy to -- in terms of the on-line component, but I'm happy to do so, and I want to thank the Panel and SaskPower for giving us the opportunity to express our views.

I expect that some of the Panel members and certainly SaskPower would be aware that we made presentations in the past. The presentation today has got a very similar theme.

Our greater concern is competitiveness in the long term, so one of the pieces that we do in the comparisons are to look at most recent data on a regional comparative basis. The data that we have in the graph as presented is developed from the KPMG competitive alternatives report. It's updated every second year. It is able to define on a sample business in a number of categories -- I believe about 20 categories -- and about 144 jurisdictions in the United States and Canada, and what this particular graph demonstrates is where SaskPower's current rate is in 2016 comparing to Billings, Montana, and Fargo, North Dakota.

Those comparisons are important to us because many of our businesses find themselves in competition with similar businesses in those jurisdictions. This one is on the agri-food, food-processing industry. The other elements of Montana or North Dakota are that they are more dependent on thermal energy than SaskEnergy in that they're virtually a hundred percent coal. I believe they probably have some natural gas today, and we're able to see what the rates will look like for this sample plant in Saskatoon or Saskatchewan in any jurisdiction in 2016 today, post the 2016 proposed increase and the increase as proposed in January of 2017, and we can see that the gap is growing, and that will have a material impact on the ability for our businesses to compete.

When we look at the operations, maintenance and administration components of the SaskPower request, we note that the rate of increase is well in excess of the rate of inflation, something in the order of four times that rate. That's even after the reductions that are proposed as part of this submission, and the future overhead maintenance and administration costs are continuing again at a rate well in excess of either the Bank of Canada target inflation rate or the currently-experienced CPI rate in Canada and Saskatchewan.

The last piece on this has to do with fuel purchased power. It's more than likely, based on our analysis, that the amount of hydro that will be drawn in the market today may well be less than what we've experienced over the previous few years. However, there had been a pattern where the predicted amount of fuel expenditures were substantially lower than that which was contained in previous submissions, so we were suggesting that that be monitored by the Panel, and in the event that they are, in fact, materially lower than those that are forecast within this report that we consider a future rebate or rate reduction.

The last point is is that we do assert both for this submission and for the SaskEnergy submission that our comparative analysis start to include the information from the KPMG competitive alternatives because it does provide an excellent comparator against nearby competing jurisdictions that have very similar attributes in terms of customer dispersion and generation.

THE CHAIRPERSON: Thank you, Kent. I would now like to ask if someone from SaskPower would like to respond to Kent's presentation.

MR. KALRA: We have just received this, so we would like to take our time and, you know, review these numbers and then respond appropriately.

THE CHAIRPERSON: Okay.

MR. KALRA: Yeah.

THE CHAIRPERSON: There's no questions that we have received on-line, so if there is someone out there who is waiting to ask a question, please type it in and get it sent to us, and we'll see if we can get it answered. In the meantime, we will also now un-mute the phones, so if there's anyone on the phone who would like to ask a question, they are welcome to do so.

It appears there are no questions, so that will end our presentation. Thank you for watching and listening, and, as

I said, you can always go to our website and you can review the material that's on-line including this presentation. If you have questions that you would like to pose, you're certainly welcome to do so on our website or by phone, and we will see that they get answered and considered in our process of reviewing these applications. Thank you very much.

(Concluded at 7:37 p.m.)

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I, Shawn Hurd, CSR, Certified Court Reporter, hereby certify that the foregoing pages contain a true and correct transcription of my stenograph notes taken herein to the best of my knowledge, skill and ability.

Shawn Hurd, CSR

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