Appendix 5.11
November 30, 2018

CENTRA GAS MANITOBA INC.
2019/20 GENERAL RATE APPLICATION

DEPRECIATION AND AMORTIZATION EXPENSE CHANGES

INDEX

1.0 DEPRECIATION STUDIES

Existing CGAAP Average Service Life (“ASL”) depreciation and amortization rates used by Centra for rate setting purposes are based on the 2010 depreciation study that was approved by the PUB for rate setting purposes in Order 85/13 (directive #6) as part of Centra’s 2013/14 GRA.

As discussed in Appendix 3.4, Centra performed an updated depreciation study for asset values as of March 31, 2014. Centra adopted the CGAAP ASL depreciation rates (including negative salvage) from the 2014 study for financial reporting purposes under CGAAP for its 2014/15 fiscal year only. An updated depreciation rate for gas meters was adopted by Centra in its 2015/16 fiscal year. Centra has established regulatory deferral accounts to eliminate the impact of the 2014 Depreciation Study and the subsequent change in the gas meter depreciation rate on net income and customer rates, until PUB approval of these depreciation rate changes is received. For more information on the respective regulatory deferral accounts, please refer to Appendix 3.4 of this application.

2.0 TRANSITION TO IFRS

Centra’s 2015/16 transition to IFRS resulted in several changes to the manner in which Centra determines depreciation and amortization expense for financial reporting purposes. Such changes included the transition from the CGAAP ASL to the Equal Life Group (“ELG”) method of depreciation, the elimination of a provision for asset removal costs (i.e. negative salvage) in depreciation rates, and the immediate recognition of asset removal costs on terminal asset retirements and asset retirement gains/losses in depreciation expense. In addition, under IFRS Centra is required to move the classification of the amortization of the regulatory deferral accounts from depreciation expense to the Net Movement account and to move the recognition of the revenue from non-refundable customer contributions in aid of construction from depreciation expense to Other Income.

Centra implemented these changes for financial reporting purposes starting in its 2015/16 fiscal year, and as required by the accounting standards, applied these changes retrospectively to its 2014/15 fiscal year for comparative purposes.

2.1 Change to ELG Method of Depreciation

Centra's change from the CGAAP ASL to the ELG method of depreciation was implemented by Centra for financial reporting purposes only to comply with the requirements of IFRS as it pertains to determining depreciation. The change to the ELG method of depreciation resulted in an annual increase in depreciation expense of approximately $2 million.

Centra has established a regulatory deferral account to eliminate the impact on net income and customer rates of the change to the ELG method for rate setting purposes. For more information on the impact of the change to the ELG method, please refer to Appendix 3.4 of this application.

2.2 Elimination of Negative Salvage in Depreciation Rates

As discussed in Appendix 3.4, IFRS does not permit the inclusion of a provision for negative salvage (asset removal costs) in depreciation rates. In Order 73/15 (Directive 8) arising from Manitoba Hydro's 2014/15 & 2015/16 GRA, Manitoba Hydro received endorsement from the PUB to eliminate negative salvage from depreciation rates for rate setting purposes.

To be consistent with the depreciation rates used by Manitoba Hydro for rate setting purposes, Centra eliminated negative salvage from depreciation rates starting with its 2015/16 fiscal year, applied retrospectively to its 2014/15 fiscal year. This change results in an annual reduction in depreciation expense of approximately $4-$5 million for Centra.

The following figure presents the impact on depreciation expense of the elimination of negative salvage in depreciation rates:

Figure 1: Impact on Depreciation Expense from Eliminating Negative Salvage

Impact of Removing the Provision for Negative Salvage from Depreciation Rates						
($000'S)	2014/15 Actual	2015/16 Actual	2016/17 Actual	2017/18 Actual	2018/19 Forecast	2019/20 Test Year
Transmission	(312)	(321)	(350)	(423)	(440)	(458)
Distribution	(4 077)	(4 227)	(4 414)	(4 615)	(4 792)	(4 977)
General Plant	77	75	74	74	74	74
Annual Increase (Decrease)	(4 312)	(4 474)	(4 689)	(4 963)	(5 158)	(5 361)

2.3 Immediate Recognition of Asset removal Costs and Retirement Gains and Losses in Income

Centra deferred asset removal costs and asset retirement gains and losses on retired assets in accumulated depreciation under CGAAP. Under IFRS, the costs to remove an asset from service are to be added to the cost of the replacement asset, or in situations when an asset is terminally retired (i.e. no replacement is installed), removal costs are to be expensed as incurred. In addition, IFRS requires that asset retirement gains and losses are to be recognized in income in the period incurred. Following its transition to IFRS, Centra now records these amounts in depreciation expense in the year incurred. Notably, the value of this account can fluctuate significantly from year to year depending on the nature and age of the assets retired.

Centra has established a regulatory deferral account to eliminate the impact of this change on net income for rate setting purposes. For more information on the impact of this change, please refer to Appendix 3.4 of this application.

2.4 Reclassification of Amortization of Regulatory Accounts from Depreciation Expense to the Net Movement Account

Previously under CGAAP, the amortization of regulatory account balances were recognized in depreciation and amortization expense in the income statement. *IFRS 14* requires all net income impacts of regulatory deferral accounts to be recognized through the Net Movement account so as to isolate the impacts of rate regulated accounting in one section of the income statement.

Please see Figure 5.20 of Tab 5 for the details of the regulatory deferral accounts that are recognized in the net movement account.

2.5 Reclassification of Amortization of Customer Contributions to Other Income

Under CGAAP, non-refundable contributions received from customers as part of capital projects were included in contributions in aid of construction and subsequently amortized on a straight-line basis to income as a reduction to depreciation expense over the remaining service life of the asset group for which the contribution related to. Under IFRS, the standards for revenue recognition require the recognition of the amortization of non-refundable customer contributions in aid of construction in Other Revenue.

Please see Figure 5.8 of Tab 5 for the actual and forecast amounts of customer contributions recognized in Other Income.