PUB-IC-3 **On pgs. 11-12 Ms. Lee states that Hydro, by restating the original cost of its assets to net book value in January 1, 2011 as part of implementing IFRS, and moving to the remaining life technique, understates the depreciation rate and resulting depreciation expense. She recommends that Hydro be required to recalculate the reserve using a recalculated depreciation rate. Describe in detail the analysis and level of effort that would be required to implement this recommendation.**

RESPONSE: There would be minimal effort required to implement Ms. Lee's recommendation. Ms. Lee notes that in RFI IC-NLH-66, Hydro states that the original cost of its assets as shown on Exhibit 1, Schedule 1, pages III-4 and III-5 of Hydro's 2009 depreciation study was restated to net book value on January 1, 2011 as part of the implementation of IFRS. The restatement "put the reserve of each asset to zero." Ms. Lee's recommendation would simply require a recalculation of the proposed remaining life depreciation rates on Exhibit 1, Schedule 1, pages III-4 and III-5 to reflect the restatement of cost and reserve that has occurred.

For example, please refer to Account A01, Aircraft Landing Strip on Exhibit 1, Schedule 1, page III-4. The investment as of December 31, 2009 before the restatement is $394,805; the book reserve is $217,451 or 55% (reserve percent = investment $/reserve $). Hydro's proposed remaining life rate is 7.5% [(100%-55%)/6]. Assuming this depreciation rate is approved by the Board, the resulting annual depreciation expenses are about $29,659 (multiplying the depreciation rate by the account investment).

Let's now restate the investment to net book value and the reserve to zero as Hydro did as of January 1, 2011. The restated investment is $177,354. The approved 7.5% remaining life rate will result in annual expenses of about

$13,301. Clearly, the same remaining life rate produces different expenses if applied to different bases (original cost or net book value).

However, if the remaining life rate is recalculated to reflect the January 1, 2011 restatement by using a zero reserve, the rate produced is 16.7% [(100%-0%)/ARL]. This rate multiplied by the account restated investment yields annual depreciation expenses of about $29,659, the same as that illustrated by the Company on Exhibit 1, Schedule 1, of the depreciation study.

This exercise simply shows that if the depreciation rates proposed by Hydro are approved, all things remaining equal, they will result in annual expenses that are actually lower than those reflected on Schedule 1 of the depreciation study.