

1 (9:30 a.m.)

2 MR. NOSEWORTHY, CHAIRMAN: Good morning. A fine
3 crowd gathered here this morning by the looks of things.
4 Looks like we're close to the end hopefully.

5 COMMISSIONER SAUNDERS: (inaudible).

6 MR. NOSEWORTHY, CHAIRMAN: It is, yeah. A
7 beautiful winter morning out there. I was thinking this
8 morning and reflecting back that this is the third season of
9 this hearing. (laughter) We (inaudible) at the pre-hearing
10 conference during the summer and most of the hearing in
11 the fall, in the autumn, and we're into the, pretty well the
12 dead of winter now, so hopefully we won't see the spring
13 with this. We'll get it over with before then. Welcome to
14 the, I guess the final two days of this regulatory marathon
15 and I trust, like me, you're looking for a sprint to the finish
16 here over the next two days. I don't have anything by way
17 of preamble to say this morning. I'll ask Counsel indeed to
18 review our schedule for the next two days first of all. Good
19 morning, Mr. Kennedy.

20 MR. KENNEDY: Good morning, Chair, Commissioners.
21 There's just one change to the schedule that was forwarded
22 around to all counsel late Friday, and the schedule as is
23 now proposed is unchanged for today and that being for
24 oral submissions to be led off by Hydro, and upon
25 completion then Newfoundland Power, then counsel for the
26 industrial customers, then the argument of 5-Wing. That
27 should fill out the full day and then commencing Tuesday
28 morning would be Lab City, then the Consumer Advocate,
29 then myself as Board counsel and then Hydro has been
30 allotted a half an hour for rebuttal, so that would hopefully
31 round out Tuesday, so that's the schedule, Chair, with the
32 approval of the panel.

33 MR. NOSEWORTHY, CHAIRMAN: Thank you very much.
34 I would note that we have allotted timeframes, I guess, and
35 particular time limits to the arguments and the
36 presentations and I'd like you to strongly adhere to those.
37 If they're not adhered to, I think I'll be invoking some sort
38 of five-minute flexibility, but that will be about it, so I'd like
39 you to bear that in mind, please, if you would. Good
40 morning, Mr. Lockyer, and welcome back. I think you're
41 probably the only particularly new face at the table, so
42 welcome here this morning.

43 MR. LOCKYER: Thank you.

44 MR. NOSEWORTHY, CHAIRMAN: Are there any other
45 particular items before we begin this morning? Okay,
46 having heard none, good morning, Ms. Greene. I'd ask you
47 to begin, please.

48 MS. GREENE, Q.C.: Good morning, Mr. Chair and
49 Commissioners. You mentioned it's been three seasons.
50 Well for the Hydro team it's five seasons. We started a

51 year and a half ago in September of 2000 and ... 2000. It has
52 been a long process and we are very happy to be here
53 today for the end of the process.

54 Hydro filed the application now before the Board
55 that you must consider on May 31st of 2001, seeking
56 approval for the, for increases in the rates that we charge
57 our largest customer, Newfoundland Power, and our island
58 industrial customers. The increase proposed for
59 Newfoundland Power as of the October 31st revision is 6.4
60 percent, which is approximately 3 1/2 percent at the end
61 consumer level. The increase proposed for industrial
62 customers is 10 percent. Also Hydro seeks approval for the
63 continuation of the existing policies for charging it's rural
64 customers with one change at this time, which is the
65 commencement of the implementation of full cost recovery
66 rates for Government departments and agencies in isolated
67 rural areas. As well, Hydro is proposing the
68 implementation of uniform rate structures for customers on
69 the Labrador interconnected system.

70 Before getting into the specific issues, and there
71 are many of them, I would like to make some general
72 comments to place our application in some sort of context.
73 These comments relate to five considerations which I think
74 we should bear in mind when we are looking at the
75 application generally.

76 They are the period of time that has elapsed since
77 rates were last changed; the impact of the price of No. 6
78 fuel on Hydro's rates; the actions taken by Hydro to
79 mitigate or reduce the required increase; the fact that
80 Hydro's proposals are dependent on one another; and,
81 number five, the legislative changes that have occurred
82 since Hydro's last rate hearing.

83 As I mentioned, the first consideration that I think
84 that is important relates to the period of time which has
85 elapsed since Hydro's last rate increase. The base rate
86 increases which are now being proposed by Hydro are the
87 first since July of 1990, some 11 1/2 years ago. While the
88 Board did review rates in 1991 and issued a report in early
89 1992, the actual rates were not changed from those that had
90 been implemented on July 1, 1990.

91 Evidence filed at this hearing indicates that the
92 rates charged by Hydro, including the annual RSP
93 adjustments that have occurred in the past ten years, have
94 tracked well below the rate of inflation since the last
95 hearing, plus Hydro's customers have had the benefit of a
96 real decline in the price of electricity over the past ten
97 years. In fact, industrial customers' rates have actually
98 decreased in this period. The current base rate paid by
99 industrial customers is 82 percent of the rate that was
100 charged in 1992, and even with the proposed 2002 increase,
101 the rates will be 92 percent, or 90 percent of the '92 rate. In

1 fact industrial rates are the lowest in Atlantic Canada and
2 compare favourably with those in the rest of Canada, so
3 Hydro's customers' experience in the past ten years with
4 electricity pricing has been stable, as I've just
5 demonstrated, and that is to be contrasted with the
6 experience with other products such as the purchase of
7 fuel.

8 However, no one likes an increase and there have
9 been a number of events which have transpired which now
10 require that rates be reviewed, which leads me to the
11 second point or the second overall consideration, and that
12 is the price of No. 6 fuel at Holyrood which Hydro believes
13 is one of the primary drivers. It's not the only one but it's
14 one of the primary drivers for this rate application.

15 The Holyrood plant now accounts for 30 percent
16 of the generation requirements for the province and burns
17 on average three million barrels of oil a year. At the time
18 the rates were last set in 1992, the amount that was included
19 in base rates for No. 6 fuel was \$12.50 Canadian a barrel.
20 The amount included in the 1992 cost of service for No. 6
21 fuel was \$37.9 million. There has been a significant
22 increase in the prices paid for No. 6 fuel with significant
23 sustained increases, particularly in the last 12 to 15 months.

24 (9:45 a.m.)

25 The amount forecast for 2002 for No. 6 fuel is \$92.1
26 million. The difference in the price in base rates for No. 6
27 fuel and actual prices has also, of course, impacted the
28 balance in the Rate Stabilization Plan. Hydro's current
29 forecast for the price of fuel for 2002 is \$25.90 Canadian per
30 barrel. The need to reflect a more realistic price for No. 6
31 fuel in base rates is in our view one of the primary drivers
32 for this application.

33 The third comment, or general comment, relates to
34 the action that Hydro has taken to keep the required
35 increases as low as possible. Hydro in preparing for this
36 application was concerned about the impact of the
37 increases that would be required and the impact it would
38 have on their customers, so consequently Hydro proposed
39 a number of measures to moderate what the rate increase
40 would otherwise would have had to be if Hydro didn't take
41 this action. The two primary ones listed in the application
42 were, number one, asking for a lower profit than Hydro
43 would otherwise be entitled to, and, number two, asking if
44 the price for No. 6 fuel included in base rates be set lower
45 than the forecast price with the difference between the
46 forecast price and the actual price being accounted for
47 through the Rate Stabilization Plan.

48 If a normal profit had been asked, so I'll use the
49 11.25 percent because that is what had been used for
50 illustrative purposes in our application, then the rate
51 increases would have been higher by another six percent

52 other than the ones I referred to earlier. Similarly, if the
53 price of No. 6 fuel had been set at the forecast price of \$28
54 at the time we filed, the rate increase required for
55 Newfoundland Power would have been 16 percent instead
56 of 6 1/2 and for industry the increase would have been 23
57 percent.

58 In addition to the two specific measures which I
59 just outlined, Hydro has taken a number of actions over the
60 past ten years to enhance efficiency in its operations. I
61 won't go through all of these now. They have been
62 outlined in the evidence and throughout the hearing but
63 they include such initiatives as reducing staffing by 16
64 percent, the introduction of an integrated suite (phonetic)
65 of financial products, improved operational efficiency such
66 as the online efficiency monitoring system at Holyrood, the
67 introduction of the diesel system representative category
68 in diesel plants, the realignment of staffing including our
69 line crews, and technical improvements such as the runner
70 replacement at the Bay d'Espoir plant. Other examples have
71 been provided throughout the hearing.

72 The fourth comment of a general nature on the
73 context is that Hydro's proposals are generally dependent
74 on one another. This is what I call the package deal. What
75 I mean by this is that Hydro's proposals regarding the
76 return on equity it is requesting for 2002 and its proposal
77 on the price of No. 6 fuel to be used in base rates are based
78 on the facts as Hydro understood them at the time they
79 filed the application. If any significant change is made by
80 the Board which was not contemplated by Hydro at the
81 time of filing, it would significantly change the whole
82 picture and other factors would have to be considered.

83 For example, if the Rate Stabilization Plan is
84 eliminated and nothing replaces it as proposed by the
85 Consumer for 2002 and 2003, then the risks that Hydro
86 faces would materially change. There is no doubt that this
87 would have affected Hydro's proposal for a three percent
88 ROE. The fact that the RSP materially affects Hydro's risk
89 was recognized by all of the cost of capital experts,
90 including the Consumer Advocate's cost of capital expert,
91 Dr. Kalymon, so Hydro's proposal for a three percent ROE
92 was made in the light of the risks as Hydro understood
93 them at the time of filing the application. If the Board
94 makes a decision which materially increases the risk, then
95 the impact of the increase on the risk has to be considered
96 with respect to return on equity.

97 The fifth and final comment on the overall context
98 of the application is the legislative changes that have
99 occurred in the past ten years. Hydro became fully
100 regulated under *The Public Utilities Act* in early 1996.
101 These amendments were set out in our final argument and
102 in Schedule A to that argument. As well, the island
103 industrial customers summarize the legislative changes.

1 The only comment I would have is that the effective date
2 for the amendments was not December 1995 as stated by
3 the industrial customers but in fact it was early 1996. The
4 Act which contains the amendments said it would become
5 effective when proclaimed. The amendments were
6 proclaimed January 16th and they were gazetted on January
7 19th, so the amendments became effective in January of
8 1996.

9 Many complex issues were raised throughout this
10 hearing. The positions of all of the parties on the various
11 issues have been summarized in our final arguments. In
12 preparing for oral argument this morning, it was a challenge
13 to try to decide what issues needed to be addressed in the
14 hour and a half that's been allotted. I have many
15 suggestions from many of the people at Hydro as to what
16 should be covered. It was impossible to cover them all, so
17 I would point out that all of the main points have been
18 covered in our final argument. If I don't ... I will not refer to
19 all of those arguments here because time does not permit,
20 but we will be commenting on those issues that we feel
21 need additional comment as a result of the final
22 submissions of the other parties.

23 For the purpose of the oral argument, I have
24 grouped the issues under eight main headings, the revenue
25 requirement, number one; number two, financial issues, and
26 of course most of those are related to the revenue
27 requirement; Rate Stabilization Plan; cost of service
28 methodology; rates issues, rural deficit, 2002 capital
29 budget, miscellaneous.

30 The first main category, the revenue requirement,
31 will take me the longest period of time, and here, I wonder,
32 Mr. O'Rielly, if you could bring up Schedule 1(A) to the
33 evidence of John Roberts. The first general step in
34 determining rates to be charged to customers is to
35 determine the regulated expenses that are approved for
36 recovery from customers. This is referred to as the revenue
37 requirement. What I've shown here on the screen is
38 Schedule 1 and as it was revised in Schedule 1(A) to the
39 evidence of John Roberts, and this lists all the categories
40 of expenses that are included in the revenue requirement,
41 and I will have to deal with each of these because there
42 were significant issues raised by the other parties with
43 respect to most of the categories.

44 On the screen you will see two expenses,
45 depreciation, line three, and power purchased, line 15. No
46 other party raised any issue with respect to these two
47 categories of expenses and Hydro therefore submits that
48 these two categories of expenses should be approved by
49 the Board as proposed by Hydro.

50 The next major category of expense listed there on
51 Schedule 1(A) is fuel. In the fuel category there are two

52 major components, diesel fuel and No. 6 fuel. No issues
53 were raised by the other parties with respect to Hydro's
54 proposed forecast for diesel fuel for 2002. As Hydro
55 pointed out in its final argument, the diesel fuel forecast of
56 October 31 should be reduced by \$300,000 to reflect the
57 revised fuel forecast presented in the second
58 supplementary evidence of Rob Henderson, so the total
59 amount for diesel fuel on line 11 for 2002 should be reduced
60 by \$300,000 to \$6.5 million. There were no other issues ...
61 there were no issues raised with respect to diesel fuel. That
62 change arises from the revised forecast, and that was
63 pointed out in our final argument.

64 The other major component of fuel is No. 6 fuel
65 burnt at Holyrood, and here the other parties have raised
66 four issues: the forecast price to be used in setting base
67 rates; the hydraulic production forecast to be used in
68 determining the forecast thermal generation for 2002; the
69 efficiency factor for No. 6 fuel burnt at the Holyrood plant;
70 and Hydro's fuel management practices.

71 With respect to the first issue, which is what price
72 should be used for No. 6 fuel in setting base rates, it should
73 be noted that both Newfoundland Power and the Industrial
74 Customers agree with Hydro's proposal that \$20 Canadian
75 a barrel should be used in base rates. They both have
76 agreed that that is a reasonable approach.

77 The Consumer Advocate's position on the price of
78 No. 6 fuel is related to his position on the Rate Stabilization
79 Plan. He is recommending, as we all know, that that plan be
80 eliminated. He is further proposing that the price for No. 6
81 fuel used in base rates be set at the forecast price, which is
82 \$25.90 a barrel. This position by the Consumer Advocate
83 would of course result in higher rates for all consumers
84 than that proposed by Hydro. Only the Consumer
85 Advocate is recommending the elimination of the Plan,
86 both Hydro and Newfoundland Power are recommending
87 continuation of the Plan, and Industrial Customers are
88 proposing changes that are significant, and I will deal with
89 the issue of the RSP later.

90 But on the first issue of price it seems clear or it is
91 clear that no party has suggested a lower price and
92 therefore Hydro proposes that the price of \$20 Canadian a
93 barrel should be the one used in setting base rates.

94 The second issue with respect to No. 6 fuel is the
95 appropriate forecast of Holyrood thermal generation for
96 2002. This forecast depends on two factors, one is the
97 amount of hydraulic generation which would be available
98 to meet the load, and the other is the efficiency of
99 conversion factor to be used per barrel of No. 6 fuel.

100 The determination of the forecast hydraulic
101 production has to Hydro's surprise been one of the
102 contentious issues in the hearing. Hydro proposes, as it

1 has in all previous rate referrals, to use the long-term
2 average hydraulic production for each plant to determine
3 the hydraulic generation of the test year. Newfoundland
4 Power proposes that Hydro use a 30-year moving average
5 of historic (inaudible) rather than the full historic record.
6 This position is supported by the Consumer Advocate,
7 while the argument of the Industrial Customers states that
8 while they're not opposed to the 30-year average, they're
9 not opposed to using the longest, reliable historic record
10 available either.

11 In taking their positions, both Newfoundland
12 Power and the Industrial Customers suggest that certain of
13 the data is unreliable. Hydro doesn't agree. The argument
14 of Newfoundland Power and Industrial Customers raises
15 three issues to support their contention of unreliability.
16 One is that the older gages used were inherently less
17 accurate than new gages; number two, while data on the
18 major rivers were included, not all the rivers were included;
19 and, number three, that the use of data prior to an in-
20 service date of a plant is unreliable.

21 With respect to the first point, it must be noted
22 that there was no evidence presented to indicate that the
23 gages were inaccurate or that any other utility disregards
24 data on the basis of the age of the gage. On the second
25 point, the rivers that were excluded were so minor that they
26 would have no impact on the inflows.

27 The third point raised by Newfoundland Power
28 relates to the use of data prior to a plant's in-service date.
29 If this position is to be taken, then data for Cat Arm pre-
30 1985, Hines Lake pre-1980, and Paradise River, pre-1989,
31 would have to be disregarded, as well as data prior to the
32 in-service date for Bay d'Espoir. This would add significant
33 variability to the 30-year average. Either you must accept
34 the validity of the gage data prior to the project
35 development to get a 30-year average or you use an
36 averaging period that starts only with the project in-service
37 date and that would result in less than 30 years. You can't
38 have it both ways. The data is either reliable or it isn't, and
39 if the data is unreliable, it would be unreliable for any
40 purpose, whether it's for rate making or whether it's for
41 engineering purposes. Newfoundland Power suggests that
42 it's okay to use the data for engineering purposes but it's
43 not appropriate for rate-making purposes. We think this is
44 inconsistent.

45 We would point that every other Canadian utility
46 that has significant hydro generation uses the full historic
47 record that's available. No utility that we are aware of
48 disregards any data, including data prior to the in-service
49 date of a plant.

50 The impact of using a shorter period of 30 years
51 would increase the average hydraulic production forecast

52 and thus reduce the forecast thermal generation with a
53 consequent reduction in the revenue requirement for 2002,
54 however, as Hydro has pointed out in its final argument,
55 the difference between the actual production and the
56 forecast production goes into the RSP and will be
57 recovered over time, with the end result being that
58 customers will pay what the actual production is, so the
59 real question is what is the most reasonable forecast to use
60 to set base rates.

61 Hydro still believes, after having gone through the
62 hearing and reviewing all of the issues, that the best
63 forecast of what can be produced on average from hydro
64 facilities is that determined from the longest data record
65 available. This position has been accepted by the Board in
66 all previous rate referrals. Newfoundland Power did not
67 provide any precedent for any other utility using a 30-year
68 average as proposed by them, nor did they provide any
69 regulatory precedent where the regulator reduced the
70 record to be used for determining hydraulic production as
71 proposed by a utility.

72 *(10:00 a.m.)*

73 I will point out that from a financial perspective,
74 Hydro is revenue neutral with respect to this because of
75 the operation of the Rate Stabilization Plan.

76 We are taking the position that the full historic
77 record should be used to determine hydraulic production
78 because we believe it's the best approach. The use of a 30-
79 year average does not produce a more accurate forecast.
80 For example, 2001, which was the seventh driest year on
81 record, followed eight relatively wet years and it would not
82 have been appropriately forecast if a 30-year period had
83 been used. If 2002 is like 2001, Hydro's approach will in fact
84 produce a closer forecast than Newfoundland Power's for
85 2002.

86 In summary on this point, I would like to point out
87 that Newfoundland Power's recommendation is not
88 supported by the practice of any other utility that has any
89 hydro, significant amount of hydro generation, that Mr.
90 Brockman who made the recommendation has no
91 experience in operating a hydro system or determining
92 hydraulic forecasts, and that it is inconsistent with Hydro's
93 and the Board's past practice.

94 The second issue on the price of fuel is the
95 conversion factor which is to be used for a barrel of No. 6
96 fuel oil. Hydro is proposing that the current conversion
97 factor of 605 kilowatt hours per barrel be increased to 610.
98 Newfoundland Power and Industrial Customers are
99 proposing that it be set at 633 kilowatt hours per barrel,
100 which is the highest efficiency factor ever for Holyrood.

101 As pointed out in our final argument, the

1 conversion factor selected by the Board to be used in the
2 determination of thermal generation can have a dramatic
3 impact on Hydro's net income. If 633 kilowatt hours per
4 barrel is used to set base rates, and our experience as it was
5 in 1999, just two years ago, when the actual conversion
6 factor was 577, Hydro's net income would be wiped out. In
7 fact we would be in a negative position of \$1 million. This
8 significantly increase Hydro's risk.

9 A dramatic increase in the conversion factor to 633
10 would be an extreme risk for Hydro. It will be picking the
11 highest efficiency ever achieved and saying that it can be
12 achieved on a continuous basis, on a go-forward basis.
13 Hydro submits that this is not reasonable. Hydro will point
14 out that it would be necessary to assess the additional
15 risks imposed by setting such a high conversion factor to
16 determine what that impact should be for the return on
17 equity.

18 In conclusion, Hydro states that it cannot live
19 with a conversion factor of 633 kilowatt hours per barrel.
20 Hydro is proposing that it be set based on a reasonable
21 estimate of what the plant can achieve over a period of time
22 and that Hydro is proposing that the conversion factor be
23 increased from 605 to 610 kilowatt hours per barrel to reflect
24 our recent experience. A 610 strikes a balance from the
25 extremes of 633 and the 577, both of which have been
26 experienced in the past five years.

27 The fourth and final issue with respect to fuel cost
28 is Hydro's management of its fuel practices, or fuel
29 purchases. Two specific recommendations remain in this
30 regard. The Consumer Advocate in Recommendation No.
31 7 recommended that the Board require Hydro to implement
32 an oil hedging program. The Industrial Customers
33 recommended that the Board should direct Hydro to
34 develop an integrated strategic approach to fuel purchases.
35 Both these parties rely on evidence submitted by Abitibi
36 Consolidated Inc. with respect to its fuel purchases.

37 Hydro submits that it is not appropriate to use the
38 purchasing practices of Abitibi for its Stephenville
39 operations to draw any conclusions with respect to
40 Hydro's practices. Abitibi purchases only 180,000 barrels
41 a year. It doesn't even purchase the same type of fuel as
42 Hydro. Hydro purchases an annual amount of about three
43 million and it can be as high as five million barrels a year,
44 depending on the type of year we're having. One shipment
45 for Hydro is double Abitibi's entire annual consumption.
46 What might be appropriate for the purchase and storage of
47 180,000 barrels, cannot be applied to purchase and storage
48 of a different product at volumes in excess of three million
49 barrels per year.

50 I would also point out that Hydro's practices on
51 its contract and the prices obtained for No. 6 fuel were

52 reviewed by the Board's consultant, Quetta in 1999, and
53 were found to be reasonable.

54 With respect to the last issue, which is hedging,
55 Hydro would point out that it had been proactive in
56 assessing the implications of hedging for Hydro and its
57 customers. Mr. Osmond explained in his evidence that
58 Hydro has established a committee to review the
59 implications of the implementation of an oil hedging
60 program. This committee sought the advice of financial
61 advisers and tracked what hedging would have resulted in
62 over a period of time if it actually had been employed. The
63 results of this analysis were provided in U-Hydro-31.

64 That analysis shows that in some cases you win
65 and in other cases you lose when you engage in a hedging
66 program. In addition, there are costs associated with
67 hedging. The primary purpose of any hedging program is
68 to protect consumers from adverse or unexpected and
69 random price fluctuations that are short-term in nature, but
70 there's no guarantee that hedging will always result in
71 savings. There is an equally probable chance that there
72 will be losses. What Hydro proposes is that we continue
73 to monitor the implications of a hedging program until our
74 next rate hearing. This will allow Hydro to assess whether
75 the additional risks associated with hedging are offset by
76 benefits. Hydro proposes that it will report to the Board on
77 the merits of a hearing (*sic*) program at the time of its next
78 rate application, which it is anticipated to be in 2003 for rate
79 change in 2004.

80 The next category of expense shown on Schedule
81 1(A) that I'd like to talk about is interest expense, which is
82 found on line 39. Three issues have been raised by the
83 other parties relating to the calculation of interest expense.
84 The first issue relating to interest expense concerns the
85 adjustment to the interest expense arising from recall
86 revenue and was raised both by Newfoundland Power and
87 Industrial Customers.

88 This issue is dealt with in our final argument on
89 page 21, and it seems to be what Hydro has done with the
90 revenue from re-call sales is to eliminate all impacts that it
91 has on Hydro's regulated revenue as well as its regulated
92 expenses. Hydro's requirement for borrowing is reduced
93 because of the availability of the recall revenue, and thus
94 Hydro avoids interest because of the availability of the
95 recall revenue. However, recall revenue must be excluded
96 from the determination of regulated revenue requirement as
97 it relates to a non-regulated activity. Therefore, the interest
98 expense also has to be adjusted to ensure there's no
99 impacts from this unregulated activity.

100 As noted in our final argument, this issue has
101 been reviewed by the Board's external financial
102 consultants, who recommended that the Board approve the

1 adjustment to the interest expense as Hydro proposes. If
2 the adjustment is not made as Hydro proposes, then in
3 effect a non-regulated activity, which is the sale of recall
4 energy to Hydro-Quebec, will be subsidizing Hydro's
5 regulated activities. This was recognized by the Industrial
6 Customers on page 118 of their final argument where they
7 say to treat the interest, the recall expense, as suggested by
8 them, results in Hydro's customers benefitting from Hydro's
9 use of this money, but Hydro submits that's not
10 appropriate. A non-regulated activity must be totally
11 eliminated so there is no impact, positive or negative, on
12 the regulated activities, so Hydro submits that this
13 treatment of interest expense should be approved by the
14 Board as found appropriate by the Board's own financial
15 consultant.

16 The second issue relating to interest expense is
17 Newfoundland Power's suggestion that the interest
18 expense should be decreased to reflect what it calls an
19 excessive dividend for the 2002 test year. The issue of the
20 appropriateness of the dividend proposed for 2002 and
21 how the Board should deal with the dividend is dealt with
22 in Hydro's final argument on pages 45 to 46.

23 There we point out that the cost of capital experts
24 who testified for Hydro and for the Consumer Advocate
25 had no difficulty with the amount of the proposed dividend
26 payment for the test year. They recognize that the
27 Government as Hydro's shareholder is entitled to a return
28 of dividends and that there was nothing so unusual about
29 the proposed payment for 2002 or that any adjustment
30 needed to be made in Hydro's return on equity. If this is
31 the case, then the same thing applies to the interest
32 expense.

33 Ms. McShane did point out that even with the
34 amount of the proposed dividend for 2002, the amount of
35 dividends that could have been paid to the Government
36 from 1975 to 2002 would have been 40 percent of Hydro's
37 net income for the entire period, this in effect being a catch-
38 up of Government's right to receive dividends during the
39 period that dividends were not paid. Hydro submits,
40 therefore, that the interest expense should not be reduced
41 as submitted by Newfoundland Power to reflect any
42 adjustments as a result of the dividend proposed for 2002.

43 The third and final issue with respect to interest is
44 whether there needs to be an adjustment to the interest
45 expense to reflect interest on overdue accounts of rural
46 customers as suggested by Newfoundland Power. Hydro
47 in the application did not forecast any lag in receiving
48 payments from its customers which would have increased
49 the interest expense. Hydro submits, therefore, it wouldn't
50 be appropriate to offset the interest expense by the interest
51 on overdue accounts, so that concludes all of the issues
52 raised on interest.

53 The next category in revenue requirement that I
54 have to address is the margin of return on equity, which is
55 line 40. Under Section 80 of *The Public Utilities Act* the
56 Board must set what is a just and reasonable return on
57 Hydro's rate base. Hydro is proposing that the Board set
58 and fix the return on its rate base for 2002 at 7.2 percent or
59 \$98.3 million, and this is shown in Schedule 7(A) to John
60 Roberts' evidence.

61 The return on common equity is one of the factors
62 that's used to determine the allowed return on rate base and
63 thus the appropriate return on equity must also be
64 considered. Hydro is proposing a return on equity for 2002
65 of three percent. This has been recognized by all the cost
66 of capital experts as being below what would normally be
67 reasonable. The Board need not therefore in this
68 proceeding determine the precise level of an appropriate
69 return on common equity for Hydro. That decision can be
70 made at the time of Hydro's request for a full return in light
71 of the economic and capital market conditions prevailing at
72 that time. However, as we've stated before, we do believe
73 it is essential that through the decision of the Board the
74 financial markets be aware that the acceptance of three
75 percent is a temporary measure, short-term in nature, to
76 reflect the current circumstances.

77 The Consumer Advocate in his final submission
78 has suggested that the return on common equity should be
79 expressed in terms of a range between two and a half and
80 three percent. We believe this is totally inappropriate. I
81 just said that the three percent was viewed as being below
82 the compensatory return by all of the experts. If three
83 percent is too low, how can we even go lower at two and a
84 half percent? The more appropriate way to look at it is
85 whether there should be a cap on Hydro's earnings.

86 As pointed out by Ms. McShane, Hydro does not
87 agree that a cap is necessary, given the fact that the return
88 being requested is so much below what would be normal.
89 In light of the spread between what Hydro is asking for and
90 what a reasonable upper end of the range would be, the
91 probability of getting to the range is virtually non-existent.
92 However, Ms. McShane did suggest that if the Board were
93 to consider a cap, it should be in the range of 9.25 percent
94 on rate base.

95 The Board needs to reflect on what a reasonable
96 return on rate base for Hydro would be and not the return
97 asked for by Hydro in the current application in
98 considering whether there needs to be a cap on the
99 earnings.

100 The last main category of cost included in the
101 revenue requirement, which I have not yet addressed, is
102 that of other costs, and that is shown on Schedule 1(A)
103 before you on lines 17 to 28. A number of specific issues

1 have been raised by the other parties on certain
2 components of this category, and, as well, three of the
3 parties, Newfoundland Power, the Consumer Advocate and
4 Industrial Customers, have raised the issue of the
5 application of a productivity allowance to this category of
6 expense.

7 First I'm going to deal with each category of
8 expense that has been questioned, primarily by
9 Newfoundland Power, and here I wonder, Mr. O'Rielly, if
10 you could turn to page C-34 of Newfoundland Power's
11 submission? On this page Newfoundland Power sets out
12 the specific reductions to this category of expense and I
13 need to deal with each one.

14 The first one is the vacancy allowance.
15 Newfoundland Power has suggested that the vacancy
16 allowance in the test year should be increased from two
17 and a half percent to four percent. Hydro does not agree.
18 Mr. Roberts explained that over the past four years, ending
19 in 2000, the average vacancy reduction achieved was 3.8
20 percent which was then rounded to four percent in the
21 Grant Thornton Report of 2001.

22 Mr. Roberts further explained that for the year
23 2000 permanent positions had been deliberately left vacant
24 in light of the fact that Hydro knew there were going to be
25 restructurings coming early in 2001, thus the actual
26 vacancy factor was higher than 2 1/2 percent because of
27 that planned deliberate restructuring in that way. In 1999
28 the actual vacancy factor was only 1.6 percent.

29 *(10:15 a.m.)*

30 Mr. Roberts further explained that the vacancy
31 reduction factor used for 2002 is the best estimate Hydro
32 has, taking into account the complement (phonetic) of
33 positions that it has and its experience with filling
34 vacancies when there is a vacancy. The average of the
35 past four years, which are unique to those four years, are
36 not a true test of what it would be on a go-forward basis,
37 and this was taken into account by Hydro in coming up
38 with its best estimate for 2002, so Hydro submits that the
39 best estimate to use is the 2 1/2 percent and it is based on
40 the current, Hydro's current understanding of what 2002
41 will bring.

42 The second specific reduction Newfoundland
43 Power has suggested there relates to the issue of employee
44 future benefits. No other party has raised this issue nor did
45 any other party raise the issue of the vacancy allowance.
46 We deal with the issue of employee future benefits on page
47 32 of our final argument, and there we point out that the
48 accrual method is preferable to the cash method as the cost
49 of the employee future benefit are expensed in the period in
50 which the services giving rise to the obligation are
51 performed, and that's consistent with the principle of inter-

52 generational equity.

53 With respect to the transitional obligation which
54 was the liability for benefits earned up to the end of 1999,
55 Hydro has charged its retained earnings for the entire
56 amount of \$22.8 million. Mr. Brushett, the Board's financial
57 consultant, in his testimony has concluded that Hydro's
58 proposed treatment of employee future benefits is
59 acceptable. It should be pointed out that the impact on the
60 2002 revenue requirement is not material and is less than .3
61 of a percent.

62 So Hydro submits that it is prudent to recognize
63 this liability in accordance with the recommendations of the
64 Canadian Institute of Chartered Accountants and that its
65 proposal, in light of what it has done with respect to its
66 transitional obligations, is prudent, it is reasonable and it
67 should be approved by the Board. It recognizes the
68 liabilities as they arise.

69 The next category on this category of other costs
70 raised by Newfoundland Power is the issue of capitalized
71 expense. Again, it was not raised by any other party. As
72 noted by Mr. Roberts in his evidence, the amount of
73 Hydro's capitalized expense is dependent on the actual
74 capital program. Where a capital program is more internally
75 intensive, then the capitalized expense will be higher.

76 For example, in the years in which the P-2000
77 Project was underway, the capitalized expense was higher
78 because of the number of the internal people that had to be
79 assigned to the teams to fully implement the new software.
80 However, in another year when there is a large component
81 of contracted-out projects, the capitalized expense would
82 be lower, so the capitalized expense is determined by the
83 type of capital program that occurs. It cannot be looked at
84 by looking at simple averages without looking at the type
85 of programs that were associated with that average.

86 Hydro's estimate for 2002 is based on its
87 knowledge of what the actual program would be as
88 proposed. That could be changed by the Board when it
89 approves the 2002 capital program for Hydro because there
90 are issues arising with respect to that as well.

91 Hydro submits it is not appropriate to make an
92 arbitrary adjustment to the capitalized expense as
93 suggested by Newfoundland Power. The program has to
94 be looked at in context of what are the components of the
95 program and that is what Hydro did when it came up with
96 its estimate of capitalized expense for the test year, so
97 Hydro submits that Newfoundland Power's position on this
98 should be rejected.

99 The next issue raised by Newfoundland Power,
100 and again by no other party, was the issue of the hearing
101 costs. In our October 31st revision, Hydro requested that

1 the hearing costs which were incremental internal costs as
2 well as the cost of third parties which Hydro must pay,
3 should be deferred and recovered over a two-year period.
4 The total amount that Hydro propose be deferred was \$2
5 million. Included in this estimate was the cost of Hydro, as
6 I just mentioned, the internal incremental costs, and the
7 estimated costs of the Board and the Consumer Advocate,
8 which was consistent with Hydro's past practice. No costs
9 were included for the cost of other parties such as the
10 industrial customers.

11 Newfoundland Power has suggested that the
12 amount of the deferral should be limited to external costs
13 only. Hydro reviewed all of these issues again in
14 preparation for final argument, and with respect to this
15 issue Hydro has agreed to, not to ask for the deferral of the
16 costs. We are changing our position on the issue of the
17 rate hearing costs. In order to keep the revenue
18 requirement for 2002 as low as possible, we are saying that
19 we will not ask for a deferral of any of those costs into the
20 test year, but those costs include, as I just mentioned,
21 Hydro's incremental internal costs and the estimated cost
22 of the Board and the Consumer Advocate. This is
23 consistent with Hydro's past practice where it never asked
24 for it to be treated as a recoverable regulatory expense.

25 However, if an order for costs is made for other
26 parties, as is also an issue at this hearing, this decision will
27 need to be revisited and I will address this later, so in order
28 to reduce the revenue requirement for 2002, Hydro has
29 determined that it will not ask for the deferral of the rate
30 hearing costs which were primarily incurred in 2001.

31 The next issue raised is the Bay d'Espoir street
32 lighting and communication plan costs. As pointed out in
33 the original application, inclusion of \$60,000 for the Bay
34 d'Espoir street lighting costs and the regulated revenue
35 requirement was based on historical precedent. It had
36 always been approved before. However, this is one issue
37 where we again further considered it where we thought that
38 it is not appropriate to continue to treat the Bay d'Espoir
39 street lighting costs as a regulated expense. We are
40 therefore proposing to exclude the \$60,000 for Bay d'Espoir
41 street lighting costs from the 2002 revenue requirement,
42 however, we do not agree with respect to the
43 communication plan costs. We believe that those are
44 appropriate costs to improve communications among
45 Hydro's employees and stakeholders and we do not agree
46 that they should not be allowed. That covers the specific
47 issues that were raised with respect to the category of other
48 costs.

49 The last issue on the category of other costs
50 raised by three of the other parties was whether the Board
51 should consider imposing a productivity allowance. This
52 category of other costs we generally refer to as Hydro's

53 controllable costs. It includes such things as salaries,
54 equipment maintenance, fringe benefits, travel, etcetera.

55 Mr. Brushett first raised the issue of the
56 productivity allowance in his December 13th evidence and
57 stated that if the Board considered it appropriate, a range of
58 one to one and a half percent would be appropriate.
59 Having, giving a range, of course Newfoundland Power
60 and Industrial Customers picked the top end of the range
61 and they've suggested one and a half. The Consumer
62 Advocate has gone further and wants two percent. Hydro
63 doesn't agree that any productivity allowance factor should
64 be applied and I'll explain why.

65 In their final submission, Newfoundland Power
66 focused on the period '97 to 2002 with respect to the
67 history of Hydro's controllable costs. What I'd like the
68 Board to look at this morning is Hydro's history in the past
69 ten years since the last rate hearing. As shown in Schedule
70 1 to John Roberts' pre-filed evidence, the actual amount for
71 the category of other costs in 1992, the last test year on
72 which rates were based, was \$86.7 million. The revised
73 amount for 2002, which we filed on October 31st, was \$99.3
74 million. However, the \$99.3 million includes the amount of
75 \$2.2 million for employee future benefits which were not
76 accounted for back in 1992. I think you will have to
77 eliminate the issue of employee future benefits to look at,
78 to truly look at what the true controllable operating costs
79 have been in that ten-year period, so if employee future
80 benefits are eliminated, the \$99.3 million that was in the
81 October 31st filing becomes \$97.1 million.

82 What I'd like to do is compare the actual costs for
83 1992 in this category, which were \$86.7 million, to \$97.1
84 million for 2002. That percentage change is 12 percent, so
85 the change from what actually happened in '92 when base
86 rates were last set to what we're proposing for 2002, without
87 considering employee future benefits, that change is 12
88 percent. If inflation and using the same inflation factor that
89 we used when we filed our application and when
90 Newfoundland Power did its submission on this in their
91 final argument, I'm using the same inflation factor, if
92 inflation had been applied to that category of costs from '92
93 to the present, (inaudible) would have been much more
94 than that, so the actual change from '92 to 2002 is 12
95 percent. If inflation had been applied to it, it would have
96 been 16.4 percent, so that has been below the rate of
97 inflation over the ten-year period.

98 That comparison I just gave you did not include
99 the proposed adjustments that I've given you this morning,
100 which are the reduction of the rate hearing costs and the
101 elimination of Bay d'Espoir street lighting. If you take that
102 off the 2002 revenue requirement, then the percentage
103 change drops to 11 percent, so Hydro's controllable costs
104 would have increased by 11 percent in 10 years. Inflation

1 alone would have brought the increase to 16.4 percent, so
2 Hydro has tracked (phonetic) well below the rate of
3 inflation over the 10-year period for this category of
4 controllable costs. We believe that that demonstrates that
5 Hydro has taken action where appropriate with respect to
6 the category of operating costs. Moreover, as pointed out
7 in Hydro's final submission, the Board's financial
8 consultant does review each year what the expenditures
9 have been. In each of these reviews no expenditures were
10 found to be unreasonable or imprudent with two
11 exceptions, one with the spousal travel we've talked about
12 and the other was the suggestion with respect to
13 communication costs which I've already referred to today.

14 So Hydro believes that it has demonstrated
15 through its evidence a number of initiatives that have been
16 undertaken to improve efficiencies and that has been
17 demonstrated in the way this category have (phonetic)
18 costs below the rate of inflation in the past ten years. We
19 therefore submit that it is not appropriate for the Board to
20 apply a general productivity allowance as suggested.

21 The last issue to be dealt with under the category
22 of other costs is the issue raised by the Consumer
23 Advocate with respect to a potential duplication of costs
24 between the two utilities. We did cover this on pages 32 to
25 33 of our final argument and I'll only summarize it here.
26 Hydro submits that the evidence throughout this hearing
27 has demonstrated that Hydro's and Newfoundland Power's
28 operations are very different. Hydro is primarily a
29 generator and a transmitter of power. It owns only limited
30 distribution assets and then they are in more remote areas
31 of the province. On the other hand, Newfoundland Power
32 is primarily a distribution utility operating in more urban
33 areas of the province. There are not the opportunities for
34 savings that the Consumer Advocate suggests. The nature
35 of our business are, they're too (inaudible) and the service
36 areas are as well not adjacent enough to lead to potential,
37 significant potential savings. To the extent possible the
38 utilities do coordinate their activities, and there was
39 evidence given on this throughout the hearing as well, so
40 it's Hydro's submission as set out in its final argument that
41 there's not sufficient evidence before the Board to support
42 the recommendation that a third party should be hired to
43 come in and do yet another report on the issue.

44 There is another minor issue, other heading of
45 costs that I hope to deal with briefly and that was raised
46 only by the Industrial Customers and it kind of came out of
47 the blue, on page 119 of their final submission. There is
48 one recommendation that the supply of inventory should
49 be reduced by \$600,000. There is no explanation provided
50 for the recommendation and Hydro submits it should not
51 be approved. Hydro filed an undertaking, U-Hydro-25,
52 which tracked the supply of inventories from December of

53 2000 until October of 2001, which was an 11-month average,
54 and not the 13-month average used in the calculation of the
55 rate base. This 11 months show \$20.8 million versus the
56 \$21.1 million used in the rate base calculation, however, Mr.
57 Roberts did point out in the transcript of November 16th at
58 page 21 that Hydro normally increases its inventory in the
59 fall after the heavy construction season to ensure that there
60 are adequate supplies on hand and he further testified it
61 would not be appropriate to reduce the amount used in the
62 rate base calculation for inventories.

63 (10:30 a.m.)

64 Hydro therefore submits on the evidence before
65 the Board that there's no basis to reduce the inventories
66 used in the calculation of the rate base as suggested by the
67 Industrial Customers, so that concludes the first major
68 category of issues, which were the revenue requirement
69 issues, and as you can see from what I just went through,
70 there were a number of issues raised in the various
71 categories of expenses by the Industrial Customers.

72 The second main topic that needs to be addressed
73 in this final argument is that of financial issues, and these
74 are closely related to some of the revenue requirement
75 issues. The first topic that I wanted to talk about under
76 this general heading of financial issues is the appropriate
77 return on rate base. As has been mentioned already this
78 morning, under Section 80 of *The Public Utilities Act*,
79 Hydro is entitled to earn a just and reasonable return on its
80 rate base. Hydro is proposing that its return on rate base
81 be only 7.2 percent or \$98.3 million for 2002. This return on
82 rate base has been acknowledged to be lower than the
83 normal compensatory return and again (inaudible) Hydro's
84 approach to this application, which was to accept a lower
85 profit level in order to keep rate increases as low as
86 possible.

87 There was extensive pre-filed evidence with
88 respect to the rules to be applied in the determination of
89 Hydro's rate base and the appropriate return for 2002. The
90 only issue that has been raised with respect to that was
91 raised by Mr. Drazen and it concerns the calculation of
92 cash working capital and the treatment of interest expense
93 in that calculation.

94 The Towns of Labrador City and Wabush in their
95 final submission have supported the recommendation of
96 Mr. Drazen and submit that the collection of interest
97 expense prior to (inaudible) by Hydro should be included
98 as an offset or a negative in the calculation of the cash
99 working capital. Hydro doesn't agree with this and our
100 position is set out on pages 48 to 49 of our final
101 submission. To summarize on this point at this time, Hydro
102 states that the method it proposed is a method that has
103 been approved by the Board for Newfoundland Power. No

1 provision is made in the calculation of cash working capital
2 allowance for interest expense. It is also clear in the one
3 jurisdiction that Mr. Drazen was able to refer to, which is
4 Alberta, which use, includes interest expense in the
5 calculation, but other things are also included in the, in that
6 calculation as well, so this is not a true picture, just to look
7 at the interest and not to look at the other items that are
8 taken into account in Alberta. It's quite clear from Mr.
9 Drazen's direct testimony as well as the response we finally
10 received on January 18th to the undertaking that had been
11 given on December 12th that there is no regulatory
12 precedent in Canada to support the calculation exactly as
13 suggested by Mr. Drazen. In these circumstances, Hydro
14 feels that it's not appropriate to follow this
15 recommendation.

16 The only other party that addressed this issue in
17 their final submission was the Industrial Customers. On
18 page 116 they state that they agree with the
19 recommendation and that it would reduce the revenue
20 requirement by \$10 million. That is incorrect. The actual
21 impact on the revenue requirement, even if you accept the
22 recommendation, is \$720,000 and not \$10 million as stated
23 by the Industrial Customers, however, for the reasons
24 we've stated, we think the Board should not accept this as
25 it has not been accepted by any other regulatory board in
26 Canada to do like Mr. Drazen has suggested.

27 The other topic under the heading of financial
28 issues that needs to be addressed is that of the appropriate
29 financial targets for Hydro. In the application Hydro
30 proposed that the appropriate short-term target should be
31 a debt equity of 80/20 with a 2002 debt equity ratio being
32 83/17, an ROE of three percent and a return on rate base of
33 7.2. The issue of the appropriate return on equity of three
34 percent in the test year and the appropriate return on rate
35 base has already been commented on this morning, leaving
36 only the issue of the appropriate capital structure to be
37 addressed at this time.

38 No party in their final argument took exception to
39 the short-term target of 80/20. With respect to the long-
40 term target proposed by Hydro of 60/40, I would like to say
41 that Hydro believes that it should be viewed as a
42 commercial entity and that the capital structure of Hydro
43 should be consistent with its business risks and that Hydro
44 should on a stand alone basis be able to achieve an
45 investment grade debt rating of Triple B or better, which
46 the experts have indicated requires a capital structure of
47 60/40. However, as with the ROE, Hydro is not requesting
48 that the Board approve this as a target that Hydro must
49 achieve immediately. However, as with the ROE, it is
50 Hydro's position that the financial markets need to be
51 aware through the decision of the Board that the target of
52 80/20 is short-term in nature and that the Board agrees with

53 the principle that Hydro is entitled to earn a return and to
54 have a capital structure which is consistent with a utility on
55 a standalone basis.

56 The last issues to be dealt with on the topic of
57 financial issues are under the heading of regulatory
58 reporting and they arise as a result of the recommendations
59 contained in Section H of Newfoundland Power's final
60 argument. On page H-2 Newfoundland Power made three
61 recommendations. The first is that the Board shall order
62 Hydro to maintain separate accounting records. I will point
63 out that we dealt with this on page six to eight of our final
64 argument.

65 We agree that we must demonstrate what
66 revenues and costs are associated with regulated activities
67 and that's kind of basic. We must be able to demonstrate
68 that to the Board. However, we don't believe that we need
69 to keep separate financial records to do that. Within the
70 existing system we can track the costs and the revenues
71 and report on an appropriate basis to the Board. We would
72 also point out that the Board's own financial consultant has
73 agreed with this position as well, so we don't agree with
74 that first recommendation that you actually need separate
75 financial records.

76 The second recommendation Newfoundland
77 Power made was that there should be a clear definition of
78 what is included in regulated operations, and again we've
79 covered this on pages six to eight of our final submission.
80 Again, obviously the Board and all the parties must know
81 what are the regulated operations. However, our
82 submission is that this has already been, already
83 understood by the Board and the parties to the
84 proceedings and it was clearly defined throughout the
85 hearing. The Board's financial consultant has said he has
86 no difficulty with respect to this issue.

87 The third recommendation made by Newfoundland
88 Power relates to intercorporate transactions. They
89 recommended we file a policy and we thought we had done
90 that when we responded with response to NP-11(B). The
91 policy was reviewed by the Board's financial consultants
92 for charging other subsidiaries and was found to be
93 appropriate by the Board's financial consultant. It was
94 available for all parties at this proceeding to ask questions
95 on and there were many questions on it, so in Hydro's view
96 we've already complied with this recommendation. The
97 issue is before the Board and the Board can deal with it in
98 the context of this hearing.

99 The third major category of issues that I need to
100 talk about this morning is the Rate Stabilization Plan.
101 Unlike (phonetic) the fuel and the use of the hydraulic
102 records for determining hydraulic generation, this turned
103 out, to our surprise, to be one of the most contentious

1 issues in the hearing. In the final submissions the
2 Consumer Advocate recommended that the plan be
3 immediately eliminated. Newfoundland Power
4 recommended no substantive change in the actual
5 mechanics of the plan but did make recommendations with
6 respect to the cap, and the Industrial Customers while
7 agreeing with the basic principles underlying the Rate
8 Stabilization Plan, have suggested significant changes for
9 immediate implementation. The Consumer Advocate is
10 further recommending, following the elimination of the plan,
11 that Hydro's revenue requirement be established based on
12 the actual forecast, not the actual but the current forecast
13 price, forecast system load and hydraulic production.

14 Hydro dealt with the issues surrounding the Rate
15 Stabilization Plan at pages 50 to 59 of our final submission,
16 so I will only summarize that here this morning. First, I
17 think as is quite obvious now, Hydro does not agree with
18 the elimination of the Rate Stabilization Plan. All of the
19 parties have recognized, including the Consumer
20 Advocate, that Hydro must have some mechanism for
21 recovering the true cost of fuel which is burnt to supply
22 customers' loads. The Consumer Advocate has suggested,
23 while the RSP be implemented immediately, that nothing
24 replace it until at the time of our next rate hearing when
25 there should be consideration of a fuel adjustment charge.

26 I would point out that before the RSP was
27 implemented in 1986, Hydro did have two mechanisms to
28 recover with respect to fuel and hydraulic variations. We
29 had the fuel adjustment charge and we had the water
30 variation provision, and this has been acknowledged by
31 the Industrial Customers who recommends similar types of
32 provisions on a go-forward basis, while the Consumer
33 Advocate recommends one but not for another three years,
34 so while the parties agree that there should be some
35 mechanism with respect to recovery of fuel cost, it doesn't
36 seem to make a lot of sense to throw it out now and wait for
37 another three years to deal with it. That's simply too big a
38 risk for Hydro to assume and it would affect the three
39 percent ROE that Hydro has asked for in this application.
40 The elimination of the RSP would dramatically impact the
41 rate of return that Hydro would require to recover the risk
42 associated with it, and this was the position as well of the
43 Consumer Advocate's own expert, Dr. Kalymon.

44 It is Hydro's position that the RSP has worked well
45 to smooth the impact for customers arising from wide
46 variations in fuel price, hydraulic conditions and load
47 variation. It is Hydro's view that the RSP strikes an
48 appropriate balance between the competing interests of
49 allowing the Utility to recover the appropriate regulated
50 expense and rate stability for customers.

51 In our view, the real issue with the RSP at this time
52 is how the balance in the plan should be dealt with, and

53 here there's two issues, the cap and the recovery period.
54 When it filed its application initially, Hydro suggested a
55 cap of \$100 million. In our final submission we agreed to
56 reduce that cap to \$85 million. As pointed out, the cap that
57 is forecast in PUB-81 of \$65 million on retail is only a
58 forecast and like any forecast is not precise. It's based on
59 average hydraulic conditions and Hydro's forecast of the
60 price of No. 6 fuel. If 2002 is another low water year like
61 2001 or if the price of No. 6 fuel is higher than used in the
62 forecast, the RSP balance will be significantly higher. Also
63 the fact that new rates will be implemented later in 2002
64 than January will also increase the retail RSP balance. The
65 amount of the increase for that will depend on the actual
66 date of implementation, so the amount of the cap cannot be
67 precisely determined. In Hydro's judgement, a cap of \$85
68 million will be appropriate.

69 Hydro also stated in its final argument that it
70 accepted that the increase in the cap would be temporary
71 and that it would be reviewed at the earlier of the next rate
72 application or three years, but I'm pretty sure we're going to
73 see you before three years' time.

74 The other issue with respect to the RSP balance is
75 the recovery of the current balance as well as future
76 balances. Both the Consumer Advocate and Industrial
77 Customers suggest that the current balance should be dealt
78 with a different way and should be recovered, in the
79 Consumer Advocate's case, over 15 years, and the
80 Industrial Customers', over five. We believe both these
81 timeframes are too long and they exacerbate the issue of
82 inter-generational equity which has been raised by the
83 Consumer Advocate as one of the reasons for the
84 elimination for the RSP to begin with.

85 Hydro is not adverse to the options for the
86 recovery of the balance as outlined in Mr. Brushett's
87 supplementary evidence of December 31st and as we've
88 gone through in our final submission on pages 55 to 56, nor
89 are we adverse to the changes recommended by Mr.
90 Brushett with respect to the recovery of future balances,
91 also as outlined on page 56 of our final submission.

92 The Industrial Customers have suggested
93 significant changes to the RSP on a go-forward basis. We
94 don't believe that it's the right time to implement these, any
95 such changes at this time without further consideration and
96 discussion by all of the parties. Hydro's preliminary review
97 of the suggested changes is that they would be even more
98 complex than the current arrangement, and, to be quite
99 honest, we didn't fully understand how the plan proposed
100 by Industrial Customers would work. We don't believe that
101 the improvements, the changes suggested are an
102 improvement and we believe that the Board shouldn't
103 consider them further at this time and that it be deferred
104 until the, Hydro comes back for its next rate hearing.

1 The Industrial Customers have also raised an
2 issue with respect to the RSP, and that is how the plan
3 balances have been allocated between Hydro's customers
4 from the date of implementation of the plan to present.
5 Hydro totally rejects this position put forward by the
6 Industrial Customers. We dealt with this issue on pages 56
7 to 58 of our final submission. I'll only deal with it in a
8 summary way now.

9 Hydro has allocated the balance in the RSP
10 between Industrial Customers and Newfoundland Power in
11 a consistent way since the plan was introduced in 1986.
12 The rules applicable to the allocation were set out in a 1986
13 letter to the Board, which was then filed in the 1989
14 hearings, hearing. The RSP was reviewed at the 1989
15 hearing and again at the 1990 hearing. The rules were made
16 known to island industrial customers, by the latest 1993.
17 Industrial customers did participate in Hydro's rate referrals,
18 as clearly outlined by Mr. Dean in his evidence, and took
19 a very active part in all issues in the proceedings before the
20 Board where the RSP was reviewed in 1990. In its
21 submission the Industrial Customers state that the way the
22 allocation occurs results in retroactive rate making. This is
23 not correct. The plan was established by the Board with
24 defined rules and it is acceptable practice for there to be
25 adjustments to rates following actual experience. That's
26 exactly the way a fuel adjustment charge works.

27 On page 74 of their final submission the Industrial
28 Customers suggest that the balance in the plan should be
29 re-allocated from 1985 to present and they go further and
30 suggest, however, that no additional charge should flow
31 through to Newfoundland Power because Newfoundland
32 Power relied on the method of allocation. If Industrial
33 Customers are relying on the doctrine of estoppel to
34 suggest that Newfoundland Power shouldn't be affected by
35 the issue because they relied on the application of rules, I'd
36 have to point out the very same facts apply to Hydro.

37 (10:45 a.m.)

38 Hydro submitted the rules to the Board, have
39 consistently followed the rules, the rules have been
40 reviewed in two rate hearings, they've been reviewed in
41 annual reviews since by the Board's consultant. We've
42 certainly relied on the fact that the rules for the allocation
43 have been approved by this Board. We've relied on it and
44 how it's been allocated to Newfoundland Power and
45 Industrial Customers every year since 1986 and this is the
46 first time the issue has been raised, so if as suggested by
47 the industrial customers, Newfoundland Power shouldn't
48 be affected because of its reliance on the way the balance
49 was allocated, the same argument would apply to Hydro.

50 Section 71(B) and Section 17(5) of *The Hydro*
51 *Corporation Act*, are relevant here as well. Section 71(B)

52 states, "That Hydro is to adopt and maintain the RSP on
53 the basis effective in the audited financial statements of
54 December 31, 1994." The RSP as reflected in those
55 statements reflected the allocation of the balances now
56 raised by industrial customers. Section 17(5) of *The Hydro*
57 *Corporation Act* states, "That the rates and the rules that
58 were in effect prior to Hydro becoming fully regulated
59 continued until altered under *The Public Utilities Act*, and
60 this is the first time there would be an alteration. It goes on
61 further to provide, "That no alteration shall have a
62 retroactive effect, including by providing for refunds or
63 credits." So there is an expressed prohibition against
64 refunds.

65 The last point raised by Industrial Customers on
66 the Rate Stabilization Plan is with respect to the operation
67 of the plan in the event an industrial customer ceases
68 operation. This has already been dealt with by Hydro in its
69 final submission on page 58 to 59. We would reiterate that
70 the industrial customers as (phonetic) treated as a class, the
71 RSP was set up with respect to two classes, and it is not
72 appropriate, in fact it would be extremely cumbersome to try
73 and to break it out by individual customers.

74 The fourth of the eight broad categories of issues
75 that I said I needed to talk about this morning was the cost
76 of service methodology. In its 1993 report, following the
77 generic hearing on the cost of service methodology, the
78 Board recommended that Hydro use an embedded cost of
79 service. This was confirmed in Order No. PU-25 2000/2001.
80 Hydro has complied with this recommendation and Order
81 in the cost of service that was submitted with the
82 application, but there are only a limited number of issues
83 arising with respect to the cost of service methodology.
84 Two of these have been dealt with in Hydro's final
85 submission, which is the allocation generation demand
86 costs and the treatment of non-firm load, and I will make no
87 further comment here as I believe they're adequately
88 covered.

89 However, there was one issue raised by the
90 Consumer Advocate relating to the allocation of
91 distribution demand costs which we didn't address in our
92 final submission. The Consumer Advocate in
93 Recommendation 2 recommended that distribution demand
94 costs be allocated on the basis of non-coincident peak
95 rather than the coincident peak as Hydro proposes. Hydro
96 submits that for the reasons outlined by its expert, Mr.
97 Brickhill, in his first supplementary evidence at pages 12 to
98 15, that coincident peak is the more appropriate basis for
99 allocation, and in the interest of time I'll say nothing further.
100 Hydro would point out that it does not have available non-
101 coincident peak demand data for each level of service that
102 would be required if the NCP method were approved.

103 The next issue under the cost of service heading

1 that needs to be addressed is the issue of the system load
2 factor raised by the Industrial Customers beginning on
3 page 42 of their final submission. There they suggested
4 that Hydro in its cost of service has made a mistake in
5 calculating the annual system load factor when it
6 (inaudible) off Newfoundland Power's load. However,
7 Hydro states that its treatment of Newfoundland Power's
8 capacity, which can be supplied at the time of system peak,
9 is consistent.

10 If there were no demand credit given to
11 Newfoundland Power, then Newfoundland Power would
12 forecast its own generation (unintelligible) peak, thereby
13 reducing its demand required from Hydro. Therefore, the
14 reduced demand is used for both costing to Newfoundland
15 Power as well as for the system load factor, since if
16 Newfoundland Power used its own generation at peak the
17 adjusted demand is all that would be required to be
18 produced on Hydro's system.

19 The last issue under the cost of service
20 methodology that I need to address this morning is the
21 assignment of plant which was dealt with at great length in
22 the Industrial Customers' submission. On page 20 of its
23 submission the Industrial Customer suggests that Hydro's
24 guideline that all production facilities be treated as common
25 does not correspond to Hydro's definition in previous
26 hearings. Hydro totally disagrees with this statement.
27 Guideline A set out on page 16 of Mr. Budgell's pre-filed
28 evidence is the same as proposed by Hydro in the 1992
29 hearing. In all previous hearings Hydro has always
30 recommended that production facilities be assigned as
31 common. If a particular generation facility, be it on the GNP
32 or elsewhere, were not available to meet loads then that
33 load would have to be found elsewhere. It is Hydro's
34 position that all generation facilities are of benefit to all
35 customers on the system. Hydro states that this has been
36 its position in all previous rate referrals and always been
37 accepted by the Board.

38 The second issue taken by Industrial Customers
39 is whether certain transmission facilities which connect
40 generation to the grid should be classified as common. Our
41 position on the guideline we've developed to determine
42 whether a transmission line connecting remote generation
43 is of benefit has been set out in our final argument, and
44 there was great length of cross-examination on this issue
45 during the hearing.

46 Applying Hydro's guideline would result in the
47 Great Northern Peninsula line as well as the transmission
48 lines for the Port aux Basques area and the Burin Peninsula
49 being classified as common as they are of benefit to all
50 customers served on the grid. As we pointed out in our
51 final submission, once the revenue requirement has been
52 determined, the cost of service study deals with how the

53 costs should be recovered from customers. Hydro will
54 receive its approved regulated cost and the question is
55 which customer should pay these costs. In trying to
56 determine the issues related to the cost of service
57 methodology, Hydro proposed what it believes is the most
58 reasonable and fairest treatment for customers. We are
59 revenue neutral essentially with respect to this or generally.
60 We will get our approved costs. The question is which
61 customer should pay those costs. It's Hydro's view that
62 the transmission lines in question are of common benefit
63 and all customers should share in the cost of paying for
64 them.

65 The other issue raised by the Industrial Customers
66 on the assignment of plant is the assignment of the
67 frequency converters. Hydro will point out that its position
68 has been explained in its final submission, however, we
69 really felt we had to make one comment this morning. At
70 page 40 of their submission the Industrial Customers say
71 that it borders on scandalous to think that Hydro would
72 suggest a change in the assignment of plant given the
73 historical reason for the converters.

74 In Hydro's view a single comment can be made on
75 the Industrial Customers' current position. In Hydro's view
76 it is inexplicable that the Industrial Customers expect all
77 customers in Newfoundland to pay for an asset that now,
78 after April 30th, will only be of benefit to one customer, one
79 industrial customer. Why should the rest of Hydro's
80 customers pay for an asset required by one industrial
81 customer when the rest of Hydro's customers receive no
82 benefit from that asset?

83 The final issue to be dealt with under the cost of
84 service methodology are the comments of Board counsel
85 on page 22 of his final submission relating to marginal cost
86 methodology. I believe this is one area where Mr. Kennedy
87 may have strayed over the line with respect to the
88 appropriate comments of Board counsel and I don't, again
89 in the interest of time, I would suggest that the Board
90 should take into account whether it was appropriate for
91 Board counsel to have taken what is an adversarial position
92 to support his own expert when there are three other
93 experts on the record who did not support a marginal cost
94 study.

95 The fifth of the eight broad categories is rates
96 issues, and most of these issues fortunately were covered
97 in Hydro's final submission and don't require any additional
98 comment here. These include the issue of the demand
99 energy rate structure for Newfoundland Power, the
100 interruptible rate with Abitibi and the industrial contracts.
101 It also includes the issue of the appropriate rates for the
102 Labrador interconnected system and the appropriate rates
103 for the secondary supply to CFB Goose Bay. All of those
104 issues were dealt with at fairly great length in our final

1 submission and require no additional comment today.

2 There is one issue though with respect to this that
3 needs to be addressed, and that's the Industrial Customers'
4 position that the phase-out of the rural subsidy should
5 have been done in equal amounts from 1996 to 1999. Hydro
6 states that *The Electrical Power Control Act, Section*
7 *3(A)(4)*, while it states, "It is to be gradually reduced,"
8 does not provide for equal amounts as suggested by the
9 Industrial Customers, so we do not agree with their
10 interpretation of the section of the Act.

11 Also Mr. Wells explained that the Government in
12 the period 1996 to 1999 were reconsidering the policy to
13 eliminate industrial customers' contribution to the rural
14 subsidy and did not give direction to Hydro to proceed
15 with it until 1999. We also refer again to Section 17(5) of
16 *The Hydro Corporation Act* which states that, "No ruling
17 by the Board in this hearing is to have a retroactive effect
18 on the rates including providing for refunds or credits."

19 The final issue under the heading of rates that I
20 think we need to address as a result of the submissions is
21 that of transformer losses. The Industrial Customers' final
22 submission, pages 51 to 55, dealt with that and
23 unfortunately we don't think they set out the facts
24 accurately. We believe that their description of the
25 treatment of the losses is incorrect. We would refer you to
26 the response to IC-227 where we believe the proper
27 explanation for the treatment of losses is given. On page 54
28 the Industrial Customers state that our proposal will result
29 in additional revenue flowing to our bottom line. This also
30 is not correct. As we state in the response to IC-31(3), the
31 proposed adjustment was specifically assigned and
32 customer-owned transformers are not reflected in the
33 forecast losses. These losses are included in the sales to
34 customers, not the losses, as stated by Industrial
35 Customers. Hydro gets no additional revenue from the
36 proposed change in treatment.

37 The last comment on losses again is to correct a
38 statement of the Industrial Customers. On page 55 they
39 state that they estimate the increased cost to Stephenville
40 to be \$75,000 to \$100,000. The response to IC-227 indicates
41 that the estimate of the additional charge for 2002 is
42 \$29,531.

43 The next category of issues is the rural deficit and
44 here we believe all of the issues have been covered in our
45 final submission. There is only one that had been raised
46 that we hadn't addressed and that was the recommendation
47 of the Consumer Advocate for the increase in the lifeline
48 block of 900 kilowatt hours.

49 To increase the lifeline block would increase the
50 amount of a subsidy associated with serving rural
51 customers. No evidence is before the Board as to the exact

52 impact on the subsidy of an increase to 900, however, the
53 issue of increasing it to 1,200 was considered by the Board
54 in the 1996 rural inquiry where the Board refused to
55 increase it and where they pointed out at page 140 of the
56 '95 report that the present level was sufficient, so if the
57 Board is to consider increasing the lifeline block, it must
58 take into account the impact that this will have on the rural
59 subsidy.

60 The next major issue relates to the capital budget
61 and this was dealt with extensively in ... this was dealt with
62 extensively in Hydro's final submission. We pointed out in
63 the final submission that in reviewing the capital budget in
64 preparation for today we have agreed to defer two
65 associated with Harbour Deep, one associated with
66 compressors for Buchans. Harbour Deep, the deferral
67 arrives from the uncertainty on the status of the community
68 and in our review of all of our capital projects again we
69 determined that one which was already approved by the
70 Board probably should be deferred, and we are asking for
71 an amendment to that Project B-47, which was the
72 replacement of a diesel unit in Petites, be deferred. Again
73 the load in the community is declining. We have reviewed
74 it again and believe we can get through with the existing
75 diesels.

76 Hydro's position with respect to the capital budget
77 has been set out in detail. We have described each one of
78 the projects that the other parties have objected to in
79 Schedule B and we refer the Board to that for why we
80 believe each one of these projects, other than the three that
81 I just mentioned, should, four actually that I just
82 mentioned, should proceed.

83 (11:00 a.m.)

84 In submitting its 2002 capital budget Hydro
85 complied with existing processes that it has followed for
86 the past five years. If there are to be changes in the rules,
87 Hydro submits that they must be made on a go-forward
88 basis, that it would not be appropriate for the Board to
89 arbitrarily change the rules as suggested by the Industrial
90 Customers and impose it on Hydro until there's time for
91 consultation between the Board and both utilities as to
92 what might be appropriate changes on a go-forward basis
93 for justification of a capital project, so Hydro would refer
94 the Board to its submission on the capital budget in its final
95 argument where these issues have been dealt with in detail.

96 The only other issue on the capital budget relates
97 to the reduction of interest and depreciation expense in the
98 2002 revenue requirement and there again our position is,
99 yes, we acknowledge there should be an adjustment for the
100 historic under-spending. We have said we should be
101 treated the same as Newfoundland Power. Our under-
102 spending has been roughly the same as theirs. They were

1 set at four percent when (phonetic) they were at 12 percent.
2 If you exclude the year we were not regulated, our under-
3 spending is 13 percent, so we believe we should be treated
4 in a similar way and that four percent would be appropriate.

5 The last issue that I need to address is the issue
6 of costs and this is my last major category of issues, which
7 I ...

8 MR. NOSEWORTHY, CHAIRMAN: Excuse me, Ms.
9 Greene, it's 11:00. I think you're entitled to roughly another
10 15 minutes. Oh, okay. I guess we got ...

11 MS. GREENE, Q.C.: My time keeper here has told me
12 (unintelligible). That's why I've had (unintelligible).

13 MR. NOSEWORTHY, CHAIRMAN: Okay.

14 MS. GREENE, Q.C.: You know, when you practice this it
15 takes ... I can say it more quickly when I was practicing
16 than I can ... (*laughter*)

17 MR. NOSEWORTHY, CHAIRMAN: I must say you can
18 read faster than I can write. (*laughter*)

19 MS. GREENE, Q.C.: The good news is you have a
20 transcript.

21 MR. NOSEWORTHY, CHAIRMAN: Thanks. Thank God
22 for that. You have about ten minutes left. I'd suggest, it's
23 after 11:00, I think we're ... at no point in time are we going
24 to be able to allow these hour and a half's and get them
25 fully in. I think we're going to have to allow for breaks and
26 what have you, so with your indulgence I think we'll break,
27 give you a little bit of a respite for a little while and return
28 with your ten minutes later.

29 MS. GREENE, Q.C.: That's ten minutes, is it? I can get the
30 direction as to what I've got done, if they felt it was
31 essential, as I skipped my pages ...

32 MR. NOSEWORTHY, CHAIRMAN: Okay, thank you.
33 We'll break now until 20 after.

34 (*break*)

35 (*11:20 a.m.*)

36 MR. NOSEWORTHY, CHAIRMAN: I'm going to have to
37 reset the clock up there.

38 MS. GREENE, Q.C.: That's what I was telling Mr. O'Rielly,
39 I couldn't see the time, I'm going to need my bifocals
40 checked again here. That's much better, thank you, Terry.

41 MR. NOSEWORTHY, CHAIRMAN: Ms. Greene, if you
42 could continue. It's around ten minutes you have. I don't
43 think, somebody suggested the other day, the way these
44 things go in the States, is that the, when the time is over
45 the microphones go silent, but I don't think we'll do that at
46 this point in time, but I'd ask you to at least be a few

47 minutes around the ten minute mark, please.

48 MS. GREENE, Q.C.: Oh, I will, I will.

49 MR. NOSEWORTHY, CHAIRMAN: Thank you.

50 MS. GREENE, Q.C.: Having reviewed where I was over the
51 break, I believe I need to make comments on the
52 submission of 5-Wing Goose Bay, and the issue of costs,
53 so those are the two issues that I will deal with in the
54 remaining time that I have available. And 5-Wing Goose
55 Bay arises because of their submission and the fact that
56 there wasn't a lot of evidence on that issue during the
57 hearing. In his submission, Mr. Lockyer had raised the
58 issue in paragraph 10 of compensation for interruption for
59 the supply of secondary energy. We would like to point
60 out that in the electrical industry, the whole basis of
61 secondary is that it is not firm, that is the basis on which it
62 is supplied.

63 In paragraph 12, Mr. Lockyer states there is a
64 typographical error in the formula and we agree with that.
65 I just wanted to point that out to the Board that that is
66 correct, we made a mistake in the formula. The other thing
67 that we must point out is that with respect to the revenue
68 to cost ratio is not necessarily the best thing to look at, as
69 these are non-firm sales. The costs assigned to a cost of
70 service study are very low and it tends to make the revenue
71 to cost ratio seem out of line with other rate classes.
72 However, with respect to secondary energy, the issue of
73 the value to the supplier and to the purchaser is often used
74 to determine the appropriate rate for secondary energy.

75 My last point with respect to their submission is
76 a suggestion that somehow the subsidy paid previously by
77 industry has been shifted to 5-Wing Goose Bay. That is
78 absolutely not correct. There has been no change in how
79 the secondary energy rate has been set with the exception
80 of the floor that has been imposed tied to the price paid by
81 Hydro Quebec, and that is because if secondary energy is
82 only available, if Hydro has it available, it would not have
83 it available to sell it at a lower cost that it could make from
84 a sale to Hydro Quebec.

85 The last issue I needed to deal with is the issue of
86 costs which has been raised by the Industrial Customers
87 and by the Towns of Labrador City and Wabush. Under
88 Section 90(1) of the *Public Utilities Act*, the Board does
89 have the discretion to award costs in appropriate
90 circumstances. Hydro would point out that in all its past
91 referrals, Hydro has not sought to cover the costs of
92 referrals from its ratepayers as regulated expenses.
93 Similarly, as a result of the decision we've made earlier
94 communicated to you this morning, we have agreed not to
95 defer and recover as a regulated expense the cost of the
96 Board and the Consumer Advocate. In coming up with our
97 estimates that we had previously used and asked be

1 deferred, we had considered, as was consistent with past
2 practice of this Board, only the cost of the Board and the
3 Consumer Advocate. It has not been the practice of this
4 Board to award costs to intervenors of the same type as the
5 Island Industrial Customers. No costs were awarded to
6 such a customer with respect to the hearings in which one
7 or more of those customers had been represented by
8 counsel and have actively participated, including the 1990
9 and '92 general rate applications of Hydro, the Rural Rates
10 Inquiry, and the 1993 cost of service hearing. Moreover,
11 costs were not awarded to Abitibi or Irving in their
12 interventions in Newfoundland Power's general rate
13 applications in 1996 and 1998, so the past practice of this
14 Board has been not to award costs to industrial customers.

15 Hydro submits that the Island Industrial
16 Customers have adequate financial resources to cover their
17 own costs. Given that Hydro's own costs, and the costs of
18 the Board and the Consumer Advocate are not going to be
19 passed on to ratepayers, Hydro doesn't believe that it will
20 be appropriate that the cost of industrial customers be
21 ordered to be paid by Hydro. Newfoundland Power, it is
22 my understanding, is not seeking its costs of this hearing
23 either.

24 If the Board does order costs are to be paid, as I
25 said, we would need to look at the issue of what costs, if
26 any, need to be included in the test year revenue
27 requirement. Hydro's decision not to include the costs was
28 made on the basis of the knowledge of the costs it had at
29 the time of that decision. If there is to be an order of costs,
30 we submit that there should be something included in the
31 2002 test year revenue to recover those, because we have
32 not provided for that in our analysis.

33 In any event, Hydro submits that it is within the
34 discretion of the Board and based on past practice, it is not
35 appropriate that this type of customer who is a special
36 interest group would have its costs paid by the utility and
37 the utility's customers.

38 With respect to the Towns of Labrador City and
39 Wabush, I would point out that the Consumer Advocate
40 was appointed by the Lieutenant Governor in Council to
41 represent all domestic and general service customers,
42 including those in those two towns. Under Section 117 of
43 the *Public Utilities Act*, the costs of the Consumer
44 Advocate are paid by the Board who in turn pass them on
45 to Hydro. As the Consumer Advocate has been appointed
46 to represent all consumers, we don't think it's appropriate
47 to ask Hydro to pay for a third lawyer to represent
48 consumers, seeing that the Consumer Advocate has been
49 represented by two here at this hearing.

50 So Hydro submits on the issue of costs that the
51 Board should not grant the order sought by the Industrial

52 Customers and the Towns of Labrador City and Wabush.
53 That concludes my oral comments. I thank you for your
54 attention this morning, and as I said, it was a challenge to
55 try to fit in the time period I had, with all of the helpful
56 suggestions I was receiving from my team, those are the
57 issues I needed to cover, so thank you very much, and as
58 I said earlier, I would refer you to my final argument for our
59 position on all of the main issues which were set out, as
60 luckily we had anticipated what most of the main issues
61 were. Thank you.

62 MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms.
63 Greene, and thank you for adhering to the timeframe. Good
64 morning, Ms. Butler.

65 MS. BUTLER, Q.C.: Good morning, Mr. Chairman.

66 MR. NOSEWORTHY, CHAIRMAN: Could I ask you to
67 proceed please with your oral presentation?

68 *(11:30 a.m.)*

69 MS. BUTLER, Q.C.: Mr. Chairman, thank you. Before I do
70 that, there was an order of the Alberta Energy and Utilities
71 Board circulated by us to all other parties on Friday and the
72 covering note indicated that one of the staff members at
73 Newfoundland Power actually had stumbled upon this in a
74 completely unrelated request for information, so I wonder
75 if we just couldn't table it and perhaps consider it as part of
76 our submission. The only reference, of course, that's
77 relevant in it addresses the issue of hydraulic forecasting,
78 is at page 116 under the Board Findings. I won't be dealing
79 with it in my verbal argument.

80 MR. NOSEWORTHY, CHAIRMAN: Thank you, sure.

81 MR. KENNEDY: I believe, Chair, that all counsel are
82 agreeable to that with the permission of the panel.

83 MR. NOSEWORTHY, CHAIRMAN: Thank you, do we
84 need to mark that then?

85 MR. KENNEDY: No Chair, it's a decision, so that's fine.

86 MS. BUTLER, Q.C.: Thank you, and good morning Mr.
87 Chairman and all Commissioners. Newfoundland Power
88 does not intend to repeat what's in the 96 pages of
89 argument. I had intended to use the time allotted to us this
90 morning to respond to the written briefs of my learned
91 friends and answer any questions that you might have at
92 the end of our submission. I will, however, close on the
93 topic of test year costs just to highlight some points that
94 are made in our written argument on that substantial issue.

95 Mr. Chairman, this hearing was headlined to be
96 about the cost of No. 6 fuel burned at Holyrood, over
97 which Hydro admittedly had limited control.
98 Newfoundland Power submits that it was in reality about
99 costs including fuel to the extent possible that can be

1 controlled, approximately \$17 million of which Hydro seeks
2 to pass on to customers. The customers are the true focus
3 of this hearing, Mr. Chairman, retail and industrial, and
4 Newfoundland Power hopes that its argument assists you
5 in finding the means to reduce those costs to the benefit of
6 all customers and in doing that, to reduce the rates which
7 ultimately the customers will pay. This hearing is about
8 least cost reliable service.

9 You heard 16 weeks of evidence on the cost of
10 service, cost of capital, operating and capital expenditures,
11 the Rate Stabilization Plan, and hydrology as some sample
12 issues, and for the most part, Hydro's written argument
13 suggests that it continues to support the position
14 maintained in its original application filed in May. Now we
15 acknowledge that there were some revisions made in Ms.
16 Greene's oral submission this morning, but given 16 weeks
17 of evidence, Mr. Chairman, the evidence heard before you
18 has to be addressed, and the concessions made by Ms.
19 Greene this morning are not as large as what I would have
20 expected following the 16 weeks of evidence.

21 Let me cite two examples. Hydro remains against
22 the deeming of a capital structure for rate making purposes,
23 but Mr. Wells admitted to you that the \$70 million dividend
24 to the Province of Newfoundland may not be paid, and is
25 contrary to Hydro's dividend policy.

26 Hydro remains against any change in the basis for
27 either the hydraulic production forecast or efficiency factor
28 at Holyrood, but Newfoundland Power submits to you that
29 the evidence on those two issues are substantial and must
30 be addressed, and again I will leave the details of that to
31 the end of my argument.

32 Since, for the most part, Hydro's position in
33 written argument is identical to that to which
34 Newfoundland Power responded in the evidence by cross-
35 examination of their witnesses and calling of our own, we
36 do not have a whole lot to add in our oral argument in
37 relation to Hydro's written argument. However, I think
38 there are three points worthy of comment, and the first
39 arises at page 18 of Hydro's argument, lines 4 to 11. Here
40 you will recall Hydro discusses the fuel efficiency factor
41 and the effect on Hydro's margin if Mr. Brushett's
42 recommendation of a factor of 633 kilowatt hours per barrel
43 is accepted. Now Mr. Chairman, what we want to point out
44 here is that Hydro's mathematics may be correct but the
45 concept is not correct because what was put to Mr.
46 Brushett in this example was, he was asked hypothetically
47 what would occur, or what would be the result on Hydro's
48 margin if you took the fuel efficiency factor from 1999
49 which was 577 kilowatt hours per barrel, and applied it to
50 the thermal production forecast for 2002, which was 2,207
51 gigawatt hours. Let's think about the result for a moment.
52 It is a given, as a result of the evidence before you, that the

53 efficiency factor ... I'm sorry, the efficiency increases as
54 production increases. The efficiency factor which was put
55 to Mr. Brushett of 577 from the year 1999 resulted ... sorry,
56 was related to thermal production of 919 gigawatt hours.
57 You cannot take an extremely low efficiency factor from an
58 extremely low thermal production year and apply it to a
59 high thermal production forecast. The result would not be,
60 Mr. Chairman, as Hydro suggests, an elimination of
61 Hydro's margin of \$5.6 million.

62 The second issue arises at page 16, lines 5 to 11,
63 and here Hydro is suggesting that using a 30 year record
64 for hydraulic forecasting could impact the RSP balance.
65 Mr. Chairman, I think we all accept that the hydraulic
66 forecast you use will affect the RSP balance. That is not,
67 however, the appropriate approach for this Board to
68 determine what is the most accurate hydraulic production
69 forecast. The Board must first determine what is the most
70 accurate means of forecasting the overall production
71 forecast for Hydro. And within that you will determine
72 what is the most appropriate hydraulic production forecast,
73 and by default, therefore, the thermal production forecast.
74 Having made your decision on that point, you will then
75 eventually work your way towards the operation of the RSP
76 and determine how the RSP, what effects the RSP will have,
77 and what modifications, if any, the Board is going to make
78 to the RSP, but the exercises are completely independent,
79 and you cannot determine the most accurate production
80 forecast simply by focusing on what the end result will be
81 on the Rate Stabilization Plan.

82 Related to this point at pages 10 through to 19 of
83 its argument, and we don't need to go to it, Hydro
84 addresses fuel, and specifically the forecast Holyrood
85 thermal generation. They state the real question at page 15,
86 and we will take a peak at that, Terry, if we can, lines 21 to
87 24. The real question, therefore, is what is the most
88 reasonable forecast of hydraulic generation that should be
89 used for setting base rates. Mr. Chairman, that is, in fact,
90 the real question, but in the discussion that you will see
91 looking at your own hard copy of Hydro's argument that
92 follows from the posing of that question, Hydro did not
93 refer you to the exhibit known as U-Hydro-17(revised).
94 This is the exhibit produced in direct response to Vice-
95 Chairman Whalen's question on the method which would
96 yield the most accurate forecast. The Vice-Chair asked for
97 the information, the information is provided, and Mr.
98 Brockman, as an expert, testified before you as to what that
99 exhibit said. It says that Newfoundland Power's proposed
100 means of forecasting yields more accurate results. You
101 cannot ignore that most singularly important piece of
102 evidence. Hydro obviously felt in their written argument
103 they did not have to deal with it, but the Board has to deal
104 with it, and Hydro's written argument does not assist you
105 in how to deal with it.

1 The third point I make from Hydro's written
2 argument arises at page 29, and here, Mr. Chairman, at lines
3 8 to 16, Hydro suggests that the total cost of energy per
4 kilowatt hour excluding fuel has shown a declining trend
5 since 1998, and Hydro is relying on the fact that the total
6 costs have reduced, but Mr. Brushett's exhibit that's
7 referred to, which is 5(b), does not suggest that
8 productivity has increased. The total costs reduced
9 because interest rates dropped and interest reduced.
10 Newfoundland Power maintains that the more accurate and
11 appropriate comparison appeared in Mr. Brushett's exhibit
12 5(d)(1), which was discussed during his cross-examination
13 on January 8th, and here he admitted that the cost per
14 kilowatt hour did represent a measure of efficiency, and
15 that if Hydro had maintained in 2002 the productivity it had
16 in 1997, it would reduce the 2002 revenue requirement by
17 approximately \$9 million. There is considerable money to
18 be saved, Mr. Chairman, to Hydro's customers. The Board
19 has a duty to find those savings. You now have the
20 evidentiary basis to assist you in calculating those
21 savings, and you have the legislative power to disallow
22 any costs that you accept to the benefit of Hydro's entire
23 operation, and to the benefit of the customers of the
24 province, and we think that Newfoundland Power's
25 argument assists you in that task.

26 I turn now to the brief filed by Mr. Kennedy. This
27 brief is, as we expected, and as is totally appropriate,
28 focused on the underlying law, the process, and the
29 procedure, and I will refer several times during my oral
30 argument to the rules and standards which Mr. Kennedy
31 has told you should be applied. I want to draw a couple of
32 examples from the evidence to his principles, and the first
33 deals with the topic of weight. Mr. Kennedy told you at
34 page 12 of his submission that it is your duty to identify
35 the relationship between the evidence you heard and the
36 issues you must address, and also explain why certain
37 evidence was accepted, rejected, or afforded more or less
38 weight. On the weight to be given to the evidence of any
39 witness, but particularly expert witnesses, we submit that
40 on issues that are fundamental to your decision and on
41 which the experts disagree, it is extremely important to
42 review the facts on which the expert based his or her
43 opinion, and ask yourself if the opinion had a solid
44 foundation.

45 A prime example of this arises on the multiple
46 recommendations you had on the appropriate CP allocator
47 to be used in allocating generation demand costs. The
48 Board will recall that Mr. Brickhill had based his opinion for
49 2-CP on the LOLH study prepared by Hydro dated 2001 but
50 which report omitted unbeknownst to Mr. Brickhill, data for
51 '95 to 2000. This is an excellent example of evidence that is
52 admissible and relevant, but which has to be afforded less
53 weight because the factual basis for it has been challenged.

54 Mr. Kennedy addressed for you the test known as
55 the burden of proof, which in this forum is the balance of
56 probabilities, and on this I ask only that the Board bear in
57 mind the scales of justice. When faced with two options,
58 all the balance of probabilities really means to me is that the
59 scales are tipped on one side in favour of the other.
60 Consider this as you weigh the evidence, and it will put the
61 term in perspective, and I will be suggesting to you how
62 this can be applied specifically in the area of the hydraulic
63 forecasting evidence later in my argument.

64 Aside from what Mr. Kennedy has said about the
65 general rules of process and procedure, however, there are
66 four specific points in his argument to which we wish to
67 respond, and the first, if we might, Mr. O'Rielly, is at page
68 18, and here Mr. Kennedy makes two specific suggestions
69 in the one sentence. The apportionment of demand related
70 energy costs between Newfoundland Power and the
71 Industrial Customers, he says, is dependent upon the
72 relative forecasts of demand for the test year as estimated
73 by each party. These forecasts were revised during the
74 hearing and he submits that the issue could have
75 benefitted from having Newfoundland Power give direct
76 evidence on the issue. He says that this would have
77 avoided the situation of Hydro relying on the hearsay
78 evidence of Newfoundland Power or the Industrial
79 Customers.

80 Now earlier in Mr. Kennedy's argument, we don't
81 need to go back to it, he does refer you to both the hearsay
82 evidence rule and the documentary evidence business
83 records rule, acknowledging that hearsay evidence is
84 acceptable before you. As such, Mr. Chairman,
85 Newfoundland Power's forecast, and each of the Industrial
86 Customer's forecasts are submitted to Hydro in the form of
87 business records, and they are admissible documents
88 without further proof. This is Hydro's rate hearing. The
89 documents are relied upon by Hydro. If Hydro questions
90 their legitimacy, that is the evidence that the Board would
91 require in order to assess whether on a balance of
92 probabilities the information is reliable. Hydro did not
93 question the load forecast of either of the customers,
94 including Newfoundland Power.

95 Also, let me clarify what forecast Hydro used,
96 because of the suggestion that ours was revised during the
97 hearing. The Board will know that on August 15th, 2001,
98 Newfoundland Power presented its capital budget
99 application, and in that Newfoundland Power's annual sales
100 forecast forms part of the record. Subsequently,
101 Newfoundland Power's forecast is given to Hydro, as it is
102 every year. The sales forecast that was in the hands of the
103 Board quite independent of this general rate application is
104 the basis for the information that Hydro referred to in its
105 amended or revised evidence in October. It does not

1 represent a revision of Newfoundland Power's forecast
2 during the hearing. The methodology of Newfoundland
3 Power's forecast is well known to you and its accuracy has
4 been tested by this Board on a regular basis. As a practical
5 matter, therefore, the sales forecasts of Hydro's customers,
6 notwithstanding that they are hearsay evidence are
7 admissible and reliable, and Newfoundland Power submits
8 that nothing would have been served by Newfoundland
9 Power or any of the Industrial Customers calling evidence
10 on the point at this hearing, it would just simply add
11 unnecessary time.

12 (11:45 a.m.)

13 On the same page 18, Mr. Kennedy refers to the
14 possibility of combining Hydro's GRA with the flow-
15 through application of Newfoundland Power. Mr.
16 Chairman, the relationship between Hydro's rates to
17 Newfoundland Power, and Newfoundland Power's rates to
18 its customers are a matter of record. Hydro's sales to
19 Newfoundland Power represent approximately 58 percent of
20 Newfoundland Power's total costs, and as a practical
21 matter, Hydro has been able, without any difficulty, to
22 predict the effect to Newfoundland Power's customers of an
23 increase in rates by Hydro to Newfoundland Power. So the
24 recommendation that two hearings be combined from
25 Newfoundland Power's perspective, would put the cart
26 before the horse, and would ultimately lengthen Hydro's
27 own general rate application.

28 At page 22, Mr. Kennedy addresses marginal cost
29 based rate design, and suggests that the Board consider
30 ordering both utilities to jointly conduct a marginal cost
31 study. Newfoundland Power just wants to remind the
32 Board on this point that it has already prepared and filed
33 with the Board a marginal cost study. It formed part of RFI
34 known as CA-186, which Dr. Wilson reviewed.

35 My final point arising from Mr. Kennedy's brief is
36 at page 24, and here Mr. Kennedy suggests that there may
37 be a question whether you have the evidentiary basis to,
38 sorry, upon which to render a rational decision on whether
39 one article only of the standard form contract for the
40 industrial customers is appropriate. Newfoundland Power,
41 Mr. Chairman, submits that the Board does not have that
42 evidentiary basis. Mr. Mifflin's evidence came very late in
43 the proceeding after all of Hydro's witnesses were heard,
44 and Newfoundland Power submits to decide an issue such
45 as that with consequences as far reaching as \$10 million per
46 occurrence, on the evidence only of Mr. Mifflin would be
47 inappropriate.

48 I turn now very briefly to the submission on
49 behalf of the Town of Lab City, and since Newfoundland
50 Power has no customers of its own in Labrador, it makes no
51 specific submission on whether there should be any

52 difference in rates between areas served by generation from
53 Hydro in Labrador or whether the rates should be
54 consolidated, other than to repeat the power policy of the
55 province which is stated, of course, in the *Electrical Power*
56 *Control Act, 1994*.

57 CFB Goose Bay, again, Mr. Chairman,
58 Newfoundland Power makes no submission on whether the
59 rates charged to CFB Goose Bay are unjustly
60 discriminatory, and therefore in violation of the EPCA 1994,
61 and we make no submission because CFB Goose Bay has
62 not filed supportive evidence by which the Board can
63 determine if the rates are unjustly discriminatory. For
64 example, Mr. Hamilton's evidence suggested that the rate
65 was negotiated on the basis of an avoided cost calculation
66 and you'll see that in his pre-filed testimony at page 14, and
67 in light of that fact, Mr. Chairman, it would be difficult to
68 address what other rate would be appropriate. In any
69 event, Newfoundland Power's written argument maintains,
70 and we reiterate, that any recovery over allocated costs for
71 this area should be treated as a credit to the rural deficit as
72 a whole and not just as a credit to Labrador's customers,
73 and on this point, of course, the Board has substantial
74 evidence which is all summarized for you in Section F-6 of
75 Newfoundland Power's argument.

76 I turn now to the argument on behalf of the
77 Consumer Advocate which advocates some fairly strong
78 positions on behalf of customers generally, amongst them,
79 of course, being the total abolition of the RSP, the
80 reactivation of DSM measures, and a new bill design and
81 enhanced meter readings for Hydro and Newfoundland
82 Power. I return back to Mr. Kennedy's guidance to you,
83 Mr. Chairman, and suggest that the evidence which was
84 heard before you does not support these specific
85 recommendations and I'll explain why.

86 Firstly, it was and is within the Consumer
87 Advocate's mandate to lead evidence on what consumers
88 want in relation to the Rate Stabilization Plan. The
89 Consumer Advocate called two experts ... one, Mr. Bowman
90 clearly recommended abolition of the RSP, and the other,
91 Dr. Kalymon, did not, so I don't think you have a clear
92 message on the evidence called by the Consumer Advocate
93 on that point.

94 On demand side management measures,
95 Newfoundland Power's bill format and Newfoundland
96 Power's metering, we suggest that the recommendations
97 made by the Consumer Advocate here which are 15, 16, and
98 24 to 26, also have an insufficient factual basis in the
99 evidence that you heard. First of all, on demand side
100 management measures, it was my recollection that Ms.
101 Mullally-Paulie suggested that DSM measures should be
102 in the hands of third parties, and perhaps when you have
103 the opportunity to reflect on this, you might look at her

1 testimony of October 26th, pages 13 and 14. I felt that she
2 had indicated that it would be more effective to have this
3 not managed by the utilities.

4 In relation to metering and bill design,
5 Newfoundland Power seriously questions the jurisdiction
6 of this Board on Hydro's hearing to address issues of
7 Newfoundland Power's bills and Newfoundland Power's
8 metering practices.

9 The final point that Newfoundland Power wishes
10 to address from the Consumer Advocate's argument is in
11 relation to his recommendation at page 39, and here he
12 suggested that the Board develop a test to determine if
13 there is duplication prior to approval of the capital budget
14 of either utility. Now, Mr. Chairman, while Newfoundland
15 Power agrees and we've addressed this in our written
16 argument, that there should be a consistent standard
17 applicable to justification of capital projects, we feel it is
18 impractical and unnecessary to make approval of
19 Newfoundland Power's capital budget dependent upon
20 approval of Hydro's capital budget. Newfoundland Power
21 has been, and will continue to be, fully accountable for its
22 own expenses.

23 I turn now, if I might, to the Industrial Customers'
24 argument, and here Newfoundland Power submits that the
25 Industrial Customers' argument has one thrust prevalent
26 throughout. It focuses on issues that improve the position
27 of the Industrial Customers relative to the retail customers
28 ... common plant is an example. The Industrial Customers'
29 argument challenges Hydro's definition of common plant
30 and the rules developed by Hydro with respect to the
31 assignment of plant. The argument also complains about
32 specific changes in plant assignment that do not improve
33 the Industrial Customers' situation, for example, Bottom
34 Brook, the Great Northern Peninsula, and the frequency
35 converters. Mr. Chairman, Newfoundland Power takes no
36 issue with Hydro's definition of common plant, and it takes
37 no issue with Hydro's rules respecting plant assignment.
38 It comes down to this, we think. Mr. Brockman said that
39 Mr. Budgell, who is an engineer who knows the system
40 made a judgement and he did not disagree with the
41 judgement that he had exercised in allocating costs. You
42 will find that in Mr. Brockman's transcript on December 3rd,
43 page 32. Both Mr. Brockman and Mr. Budgell, of course,
44 are engineers. Mr. Osler is an economist, and he
45 challenges Mr. Budgell's judgement in this area. He
46 proposes instead that generation in isolated areas does not
47 benefit the entire system because the generation does not
48 fully satisfy local load in peak conditions.

49 Mr. Budgell, however, I remind the Board, made it
50 clear that one of the benefits of this generation to the
51 system is its availability in emergency condition, including
52 a dry year or forced outages. My point is, Mr. Chairman,

53 that the Board has to therefore weigh the evidence on this
54 particular point of two planning engineers against Mr.
55 Osler's evidence as an economist, and while we're
56 addressing that point, let me refer, if I might, to page 16 of
57 the Industrial Customers' argument where they indicate that
58 Dr. Wilson agrees with Mr. Osler on the point, that is on
59 the definition of common plant. I had a chance to look back
60 at the transcript of December 6th, 2001, page 44, and I was
61 not able to come to the same conclusion in relation to that
62 reference, so I don't really think that it is clear that Dr.
63 Wilson did agree.

64 Back to my main point, however, and that is on the
65 thrust of the Industrial Customer's argument, I use the
66 example of Bay d'Espoir. Now the simple reference to Bay
67 d'Espoir streetlighting, I think reflects the difference in
68 focus between the Industrial Customers' argument and
69 ours. At page 41 of the Industrial Customers' argument,
70 they challenged Hydro's treatment of assigning \$60,000 in
71 streetlighting in the community of Bay d'Espoir as common.
72 The contended that it should be specifically assigned to
73 Hydro rural and paid for by retail customers, so that's an
74 attempt at shifting costs. Newfoundland Power, in
75 comparison at page C-31 of our argument, suggested this
76 was a grant from Hydro to the community, and therefore it
77 wasn't a regulated cost at all. We suggest that the \$60,000
78 should be removed entirely from Hydro's revenue
79 requirement and not merely shifted from one group of
80 customers to the other, and Ms. Greene this morning has
81 accepted that and removed it from the revenue requirement.

82 On the issue of the RSP, Mr. Chairman, nowhere
83 is the thrust of shifting costs from the Industrial Customers
84 to Newfoundland Power more prominent. Now here the
85 Industrial Customers make several suggestions. The plan
86 should be simplified, they call for more regular adjustment
87 on fuel, but a longer term adjustment on water. They
88 suggest the existing industrial and retail RSP's should be
89 blended. The load variation component should be
90 abolished, and they also suggest that Hydro has made a
91 mistake in its methodology requiring the Board to revisit
92 the calculations retroactive to 1992. It is the last three of
93 those that I want to address this morning.

94 Newfoundland Power does not support either.
95 The blended RSP, this was addressed at page 62 of the
96 Industrial Customers' argument. Mr. Chairman, this
97 recommendation makes no sense whatsoever, and there
98 was no evidentiary basis put before you to even allow you
99 to consider it. If there were not in and of itself reason to
100 reject the proposal, let me go further and highlight for you
101 at least two reasons why blending would be inappropriate
102 and would cause problems. First of all, the customers of
103 Newfoundland Power would be left to pay the balance in a
104 combined plan that remained if an industrial customer left

1 the system. Mr. Osmond who is the VP of Finance,
2 admitted in cross-examination that it would be most unfair
3 to burden retail customers with a balance in the industrial
4 plan associated with the departure of an industrial
5 customer, but if you have a blended plan, that is the only
6 result. Secondly, as it currently operates, any additional
7 revenue from rural rate increases between Hydro hearings
8 is credited to the retail RSP to reduce the deficit being paid
9 primarily by the customers of Newfoundland Power. If you
10 credited that amount to a blended plan you would be
11 providing a credit to the industrial customers for the rural
12 deficit to which they no longer contribute. That amount in
13 the year 2000, Mr. Chairman, was \$918,000.

14 The other issue, of course, that Newfoundland
15 Power takes with the Industrial Customers' argument on the
16 RSP, and addressing the last two of the three points I said
17 I would address, concerns Mr. Osler's recommendation.
18 Mr. Osler filed 135 pages in total of pre-filed evidence
19 including his supplementary, but the only point he clearly
20 labelled as a recommendation, Mr. Chairman, concerned
21 Hydro's calculations in the Rate Stabilization Plan, and on
22 this issue, the Industrial Customers' argument suggests
23 that the load variation component should be abolished as
24 it represents an anomaly, and that is referred to at page 67
25 of their written argument.

26 (12:00 noon)

27 Mr. Chairman, with the greatest of respect, we
28 have to draw our minds back to Mr. Osler's cross-
29 examination on November 30th, starting at page 17. I don't
30 think we need to go to the transcript but I will give you the
31 reference. At lines 20 to 24 he admitted that his report had
32 two main criticisms, strongly worded in my opinion. He
33 said that Hydro's process resulted in improper allocations
34 and reallocation of amounts that were not properly part of
35 the RSP, and later at lines 33 to 39, he admitted that these
36 were serious issues. But after his evidence was tested, Mr.
37 Chairman, he had to admit at page, I believe, 25, the
38 following ... that in 1985 the Board had made a
39 recommendation, in 1986 Hydro wrote the Board setting out
40 its methodology and when you look at that letter, Hydro
41 was totally transparent and the letter is comprehensive.
42 From 1986 to 2001, Hydro consistently applied the
43 methodology proposed in the 1986 letter to fulfil the
44 Board's order or recommendation. In 1993, a letter went to
45 Abitibi explaining the methodology. From 1993 to 2001 the
46 issue lay dormant and now in 2001, without the support of
47 any other cost of service experts, Mr. Osler suggests the
48 industrial customers had no input into the RSP, the method
49 used to split costs between the industrial customers and
50 Newfoundland Power has been improper, and he also
51 suggested in supplementary evidence filed in the week
52 before he testified, that the industrial customers were owed

53 \$1.5 million for the year 2000 alone. But again, Mr.
54 Chairman, once his evidence was tested, he admitted that
55 he had miscalculated that and that, in fact, as a result of
56 two industrial customers leaving the system, the industrial
57 customers saved money in 2000 instead of being due
58 money.

59 He also agreed that the remaining \$1.1 million was
60 based on his assumption that the term "load" as used in
61 the RSP, and despite the well accepted meaning of the term
62 in regulatory practice, from his perspective meant energy
63 only and not demand and energy. Now Mr. Chairman,
64 when I read back over that transcript of November 30th,
65 and look at the proposal that's being made in the written
66 argument, I'd have to say that I think the proposal is
67 incredible and is an attempt to retroactively shift costs from
68 the industrial customers to the retail consumers and the
69 industrial customers' brief at page 74 does not specifically
70 say that you shouldn't shift these costs to Newfoundland
71 Power. So as indicated in our written argument, the
72 position of the Industrial Customers on this issue is
73 suspect on both legal and regulatory grounds and you
74 should reject it.

75 The Industrial Customers are seeking their costs,
76 and beyond what I've said about Mr. Osler's
77 recommendation, there are perhaps two other points I wish
78 to make about that. The Industrial Customers appropriately
79 addressed Hydro's financial targets and made
80 recommendations or submissions very similar to
81 Newfoundland Power. However, they continue to support
82 the recommendation of Dr. Vilbert on the ATWACC
83 principles. Newfoundland Power submits, Mr. Chairman,
84 that that evidence was irrelevant to the issues before the
85 Board on this hearing, and that it unnecessarily
86 complicated an already complex proceeding. Hydro, by
87 seeking three percent return on equity basically sought at
88 least five percent below the market rate. It was
89 unnecessary for Dr. Vilbert to address the ATWACC
90 principles, and in fact, Newfoundland Power took the
91 position that it was unnecessary to call a cost of capital
92 expert at all. In short, the Industrial Customers' thrust was
93 in shifting costs from the Industrial Customers to
94 Newfoundland Power's customers, and that is their right.
95 They are entitled to do that, but the Board has to now ask
96 itself if the evidence they called was helpful, and whether
97 Newfoundland Power's customers should pay the costs
98 associated with the specialized intervention that the
99 Industrial Customers waged. Newfoundland Power's
100 customers, Mr. Chairman, do not benefit from an
101 intervention that's designed to shift costs to them.

102 Before I close now, Mr. Chairman, I would like to
103 stress that portion of our own argument which is dedicated
104 to Hydro's fuel and controllable costs. I wonder, Terry, if

1 we might go to Newfoundland Power's argument at page C-
2 1 please? Thank you. Can you just scroll down slightly
3 there, thank you. So as you can see on the screen, Hydro's
4 test year 2002 forecast for the cost of No. 6 fuel is \$77.4
5 million, and in its last test year it was \$37.9 million. Three
6 factors, we indicate in our argument, affect the \$77.4 million,
7 and they are, of course, the price of fuel, the hydraulic
8 forecast, that's the volume of fuel used and the efficiency
9 factor at Holyrood.

10 On the price of fuel first, Mr. Chairman, if I might,
11 Hydro proposes to embed \$20.00 per barrel for 2002 which
12 means that base rates, as we can see on the screen, will
13 reflect fuel costs of \$21.20 per barrel, representing a blend
14 of the year end 2001 inventory at cost, and the forecast
15 2002. Can you just scroll down to the next page, Terry,
16 please? The second factor affecting Hydro's annual cost
17 for No. 6 fuel is the volume of fuel actually consumed, and
18 in order to forecast this, of course, you have to reflect on
19 what amount of energy the entire system will need in 2002
20 and then subtract from it the amount that Hydro can
21 generate hydraulically, and by default, calculate the amount
22 it will need to generate in the more expensive way, by
23 thermal. And the final factor at the bottom of the page
24 there is the conversion of efficiency factor for production
25 at Holyrood, typically expressed in kilowatt hours per
26 barrel.

27 I want to look at the three factors closely if I can.
28 Newfoundland Power's argument at pages C-4 to C-8, deals
29 with the issue of the price. On page C-4, if I might, okay,
30 can we just scroll up a bit there please? Yeah, no, the other
31 way, sorry, thank you. Hydro's forecasting to use 3.5
32 million barrels of No. 6 fuel for producing power in 2002.
33 Therefore, for each dollar per barrel increase in fuel price in
34 base rates, the revenue requirement will increase by
35 approximately \$3.5 million. An increase of \$7.50 per barrel
36 in the No. 6 fuel cost from \$12.50 to \$20.00 will therefore
37 result in an additional \$26 million in fuel costs being
38 recovered in base rates. This increase is a significant
39 improvement from the current recovery of fuel costs in base
40 rates.

41 The estimated increase in the retail RSP recovery
42 rate to Newfoundland Power on July 1st will increase the
43 purchased power cost to Newfoundland Power by
44 approximately six percent in addition to the base rate
45 increase. A corresponding increase to consumers flowing
46 from the RSP will be approximately 3.4 percent. Just one
47 more paragraph there, Terry, please. Thank you.
48 Increasing the price of No. 6 fuel in base rates to \$20.00 a
49 barrel, Mr. Chairman, together with the operation of the
50 RSP on July 1st, 2002, will result in annual fuel cost
51 recovery improving by approximately \$40 million after July
52 of this year, \$26 million from base rates and \$13 million in

53 RSP recovery.

54 Let me summarize what the balance of this
55 argument from pages C-4 to C-8 submits. Essentially what
56 Newfoundland Power is saying is that Rome was not built
57 in a day, Mr. Chairman, and we shouldn't try to solve a
58 legacy problem such as the large RSP balance on this
59 hearing with one fell swoop. The balance, as you can see
60 from the paragraphs I've highlighted, will stabilize once
61 \$20.00 per barrel is embedded, and this will result in a 3.4
62 percent increase to Newfoundland Power's 216,000
63 customers on July 1st, 2002. It is inevitable, but it is also
64 enough. A graduated and moderated approach is
65 necessary here. In the balance of this section
66 Newfoundland Power has submitted that increasing the
67 \$20.00 ... sorry, increasing the price to \$20.00 per barrel will
68 result in significant improvement in Hydro's recovery of
69 fuel costs. Mr. Brockman supports Hydro's proposal to
70 use \$20.00 a barrel. No other expert, Mr. Chairman, has
71 recommended that you use anything but \$20.00 per barrel.
72 We also know that while the current price of oil is \$25.90,
73 the price of No. 6 is declining and not increasing, so that is
74 the trend, and we also know from history, that even if the
75 price of oil increased beyond what you embed, hydrology
76 itself may assist in keeping the RSP balance down ... it
77 assisted in keeping the RSP balance down in the last ten
78 years when the price of oil sometimes was as much as three
79 times the price that was embedded.

80 We also make some submissions on this topic in
81 Section D of our argument, pages D-2 to D-5, and if we
82 might go to that, Terry, please. Can you scroll down for
83 me, thank you? You see there, Mr. Brushett accepted that
84 the most significant factor contributing to the increasing
85 balance in the RSP is the cost per barrel of No. 6 fuel but he
86 was not prepared to recommend that you embed into the
87 operations of the RSP a price per barrel different than
88 \$20.00. Further increases in consumer rates may be
89 required, Mr. Chairman, beyond 2002, to deal with this
90 legacy issue, and it is Newfoundland Power's submission
91 that any future required increases should be gradual and
92 considered on an annual basis by the Board. Hydro's
93 annual fuel costs are subject to numerous unpredictable
94 forces. No one in this room can foretell the actual price of
95 No. 6 fuel, current exchange rates, or the hydraulic
96 conditions which Hydro will actually experience.

97 If I might just go to page D-5, Terry please, at the
98 bottom, thank you. Depending upon actual 2002 hydraulic
99 production, and No. 6 fuel prices experienced by Hydro, the
100 actual retail RSP balance at year end 2002 may be more or
101 less than Hydro's current forecast. The prudent course for
102 the Board in dealing with this matter, uncertainty
103 (*phonetic*), is to require Hydro to report on actual 2002
104 experience early in 2003 and to assess whether a short

1 hearing to modify the retail RSP recovery is necessary to
2 ensure further progress in bringing Hydro's fuel cost
3 recovery into equilibrium, and I go on to indicate what
4 modifications could be included.

5 Newfoundland Power does advocate annual
6 reviews, Mr. Chairman, and feels that those annual reviews
7 will place the Board in the best position to ensure that
8 consumers' rates reflect the most current relevant facts and
9 estimates, and with this information supplied on an annual
10 basis, we believe the Board will be in the best position to
11 determine appropriate changes to consumer rates to
12 recover current and past fuel costs, and I think it goes
13 without saying, Mr. Chairman, that this course will avoid a
14 repeat of the circumstances that the Board finds itself in
15 today, that is having to deal with a very large RSP balance
16 and still having to control consumers' rates.

17 So that is the submission of Newfoundland Power
18 on the future of oil pricing. Essentially we support the use
19 of the \$20.00 per barrel and accept that the July 1st, 2002
20 increase of 3.4 percent to Newfoundland Power's customers
21 on the Rate Stabilization Plan are inevitable. In the pages
22 which follow at C-8 to C-17, we address the issue of
23 hydraulic production forecast in a substantial way. If we
24 might go back to that, Terry, please? I won't go through
25 the evidence, or I'm sorry, the argument here, Mr. Chairman,
26 but I will summarize for you by saying that we feel strongly
27 that the Board has substantial evidence on which it can
28 base a conclusion that there is another means of
29 forecasting this hydraulic, and therefore thermal
30 production, and that that other means is, in fact, more
31 accurate, and U-Hydro-17 is all you need to look to there
32 for satisfaction of that point. And therefore, back to the
33 scales of justice again, we feel that the scales are tipped in
34 favour of the use of the 30 year rolling average for the
35 hydraulic production forecast.

36 *(12:15 p.m.)*

37 On the third point which addresses or affects
38 the price overall of Hydro's fuel, No. 6 fuel, and that is the
39 conversion factor, our argument deals with this on pages
40 C-18 to C-22, and again, we feel the Board has substantial
41 evidence on which it can conclude that Hydro's choice of
42 an efficiency factor is low and that a more realistic factor
43 can save consumers \$2.85 million.

44 The diesel issue, which is also a fuel issue, I won't
45 address specifically, but Ms. Greene has already reminded
46 the Board this morning that there are savings of \$300,000
47 there which result from the most recent evidence of Mr.
48 Henderson.

49 Can we just look, please, to page C-23, and you
50 will see the summary there of the effect of the ... 24 maybe
51 ... that's fine, Terry, we'll go back to C-23. So, in

52 conclusion, Mr. Chairman, we submitted that the Board
53 should accept Hydro's proposal to use a purchase price of
54 \$20.00 a barrel, and the second recommendation, we've
55 recommended that you order Hydro to use the 30 year
56 rolling average, require Hydro to use the fuel efficiency
57 factor of 633, and the fourth deals with the diesel fuel
58 forecast reduction of \$300,000.

59 By virtue of those four recommendations, Mr.
60 Chairman, we have shown the Board where \$8.15 million
61 can be trimmed off Hydro's fuel costs, and then in the
62 pages that follow, which are C-25 to 51, we have gone
63 through a discussion of the other costs, some of which Ms.
64 Greene reviewed this morning in her argument, and we
65 conclude on page C-34, if you might just go to that page,
66 Terry, please, at the bottom ... can you scroll up a little,
67 down a little further, please, to get the last paragraph on the
68 page. We've shown how \$4.135 million can potentially be
69 reduced from Hydro's revenue requirement and how the
70 effect of the application of a productivity allowance of 1.5
71 percent can assist you in finding another \$1.5 million for a
72 total of \$5.535 million in the other costs category.

73 In Section C-3.3 which is pages 35 to 38,
74 Newfoundland Power has addressed how the Board can
75 trim \$2.6 million off interest expenses, primarily as a result
76 of the deeming of a capital structure consistent with
77 Hydro's dividend policy, essentially not allowing the large
78 dividend proposed to the Government of Newfoundland, at
79 least for rate making purposes.

80 And I'd like to go last, if I could, to page C-51,
81 where all of these categories are summarized, and can you
82 get the figures on the page there please? Thank you. So
83 it's the adjustments column, of course, which is relevant,
84 and you will recall that in the very first page of
85 Newfoundland Power's written argument, we had indicated
86 that Hydro was seeking to pass on an additional \$17.4
87 million in costs and therefore rates to customers, so the
88 adjustments that Newfoundland Power's written argument
89 addresses cover almost all of that \$17.4 million, and that is,
90 of course, before discussion of the excess income from CFB
91 Goose Bay. So we'll just leave that on the screen for a
92 moment, Terry, if I might.

93 Mr. Chairman, we've gone through our
94 submissions on test year costs and we've shown you
95 where we think that money can be saved. Hydro clearly is
96 accountable for its costs, just as Newfoundland Power has
97 been and will continue to be in any future hearings, and in
98 determining whether, in fact, any base rate increase is
99 justified, I think what you have to ask yourselves is
100 whether the witnesses convinced you that they were in
101 control of the expenses that they can control, and that is
102 the thought that I'll leave you with in relation to the
103 adjustments that Newfoundland Power feels can be made

1 to the revenue requirement.

2 In closing though, Mr. Chairman, I would like to
3 say that this was a lengthy but fair and reasonable hearing,
4 and Hydro, to its credit, cooperated with an enormous
5 information disclosure, and developed this electronic
6 system as a means of speeding up the process for all of us.
7 Newfoundland Power commends the applicant, in
8 particular, as well as all other counsel and the Board for a
9 courteous and orderly hearing. These are the submissions
10 of Newfoundland Power, subject to any questions, and I
11 thank you for your patience, Mr. Chairman.

12 MR. NOSEWORTHY, CHAIRMAN: Thank you very much,
13 Ms. Butler. I think in my haste to perhaps move on, I didn't
14 afford the panel, I didn't have any questions, but the panel
15 the opportunity of asking Ms. Greene any questions earlier,
16 so I will ask the panel at this point in time if they have any
17 for Ms. Butler in the first instance, given her evidence.

18 COMMISSIONER POWELL: No, I haven't got any
19 questions.

20 MR. NOSEWORTHY, CHAIRMAN: And then I'll revert
21 back to see if the panel has any questions for Ms. Greene
22 as a result of her presentation this morning. Okay, having
23 heard none, we are closing in on 12:30, so what we'll do is
24 we'll break for lunch and we'll reconvene at 2:00 with the
25 Industrial Customers' presentation please. Thank you.

26 (break)

27 (2:00)

28 MR. NOSEWORTHY, CHAIRMAN: Thank you and good
29 afternoon. Before we begin, are there any preliminary
30 matters, Mr. Kennedy?

31 MR. KENNEDY: I don't believe so Chair.

32 MR. NOSEWORTHY, CHAIRMAN: Okay.

33 MR. KENNEDY: None that anyone's raised. For your
34 information, I believe Mr. Hutchings is leading off the
35 presentation for the industrial customers, Chair. That was
36 the plan.

37 MR. NOSEWORTHY, CHAIRMAN: Thank you, very
38 much.

39 MR. NOSEWORTHY, CHAIRMAN: Mr. Hutchings, if I
40 could ask you to begin? Our schedule calls for an hour and
41 a half, and a half hour for CFB Goose Bay after that, so we'll
42 likely try and break around 3:00 or so or it might be
43 appropriate, if it's an equal split in terms of your
44 presentation after yourself, Mr. Hutchings. We hope to
45 play it by ear and see what happens. Good afternoon, sir.

46 MR. HUTCHINGS: Thank you, Mr. Chair. We'll work that
47 out as it goes along. As Mr. Kennedy indicated, I'll be

48 leading off and Mrs. Henley Andrews will be following
49 behind, so my concentration in terms of my timing will be
50 less on the clock and more on my colleague who will
51 undoubtedly jealously guard her time as I would if I were in
52 the same position.

53 Mr. Chair and Commissioners, it was quite some
54 time ago that we made our opening statements in this
55 proceeding, last September, but I think it is useful to harken
56 back to the issues which we identified then and see where
57 we have taken them through the 16 weeks of hearing.

58 In terms of our presentation here, I'll have some
59 general introductory remarks and I'll deal with issues
60 involving capital structure and rate of return, as well as the
61 RSP and the frequency converters, and the balance of the
62 issues that we have chosen to address in our oral
63 presentation will be dealt with by Mrs. Henley Andrews.

64 But initially, I think it is useful to harken back to
65 the number of firsts which we mentioned in the opening of
66 this hearing in September, and many of the firsts, as we
67 noted them, arose from legislative change. Hydro is now a
68 more fully regulated utility under ... and the principles of
69 the *Public Utilities Act* are more applicable to Hydro than
70 they once were, and that brings us back to the legislative
71 context of this whole proceeding and how the Board is to
72 approach Hydro in its regulation.

73 In looking at the various written submissions that
74 have been filed, there is a detailed treatment of a lot of
75 individual topics, and I think there is a danger of losing the
76 broad picture in looking at the individual topics.
77 Obviously, the Board needs to address the evidence as it
78 relates to each of the individual topics, but without losing
79 the fact that there are interactions. Simply because a
80 common heading shows up in each of the submissions
81 doesn't mean that those issues are isolated and can
82 necessarily be dealt with as a single topic. By way of
83 example, whether or not Newfoundland Power has a
84 demand energy rate will have implications for the way the
85 RSP works, whether or not the debt equity ratio is tending
86 in a certain direction will be affected by whether there's a
87 guarantee, what the dividend policy is, and to a certain
88 extent, how far the Board can go in specifying the financial
89 parameters that are to apply to Hydro, and all of these
90 things have to be considered within the legislative
91 framework that now applies to Hydro.

92 This is I think though, something different than
93 Mrs. Greene spoke about this morning when she spoke of
94 interdependence of issues and the package deal. I had the
95 impression from her remarks that Hydro was putting
96 forward an entire package for the Board's approval and was
97 basically asking the Board to approve the entire package or
98 otherwise they'd want to come back and redo much of what

1 they had said and, of course, that's not the position that
2 the Board is in. Obviously, Hydro does put together an
3 entire package, but any number of issues arise and the
4 Board is free, and indeed must deal with each of the issues
5 and the consequences that come out of the Board's
6 consideration of those issues have to be dealt with and
7 considered, but the Board is not restricted in any sense by
8 the fact that Hydro has put together this in a package. I
9 guess the best illustration of that, and it came up a number
10 of times in Mrs. Greene's submissions this morning, is the
11 notion that changing any number of other items, such as
12 the RSP or some of the other issues that have been raised,
13 whether a change in those would necessarily lead to a
14 change in the return on equity, and I think quite frankly
15 that that's a non issue in the current case simply because
16 this is not a return on equity application. Everyone's
17 agreed that the three percent is not a commercial return and
18 the difference that any changes in the parameters to the
19 RSP would make for instance would not be such as would
20 need a change from three percent to anything else, and this
21 ties in as well to the whole legislative change and the
22 approach that Hydro is taking to that.

23 Hydro in its argument says it wants to be treated
24 similarly to an investor owned utility. Mrs. McShane is
25 quoted, in the Hydro submission, as saying that Hydro
26 should be operated as a commercial entity. I think we
27 should, however, be clear that Hydro is not a commercial
28 entity and isn't operated like a commercial entity. We have
29 seen from the way that dividends are treated within Hydro
30 that it is, in fact, used as a source of funding for its
31 shareholder, the government. It is not seeking and does
32 not seek in this application a commercial rate of return as a
33 commercial entity would have to or an IOU would have to.
34 There is no investor owned utility that could come before
35 a Board in current circumstances and look for a three
36 percent rate of return on equity. It doesn't have a so called
37 stand alone equity base and it doesn't have any plan to get
38 one. The only reason that all of these things can happen
39 is because government guarantees the debt of Hydro and
40 that makes Hydro different from an investor owned utility
41 or an ordinary commercial operation.

42 The Board has to look back to legislative intent,
43 and it is quite clear in the legislation that government, the
44 legislature, did not choose to privatize Hydro. There is a
45 clear legislative intent that this is not a private corporation.
46 It has a special status. The government has reserved to
47 itself the right to give directions to this Board as to certain
48 aspects of the regulation of Hydro and while it does that as
49 a government one cannot escape the fact that it is also the
50 shareholder of Hydro, and the Board has to realize that not
51 only is this the legislative intent, but obviously because it's
52 in the legislation, there's nothing the Board can do about it.
53 That is a given in respect of your consideration and what

54 you can do as a Board under the *Public Utilities Act* and
55 the *Electrical Power Control Act*.

56 The final comment I would make in respect of this
57 particular area of legislative change and this notion that
58 Hydro has of moving to a more commercial type of
59 operation is that there is not a justification for making
60 Hydro more commercial if the effect of this is to increase
61 the price of power. There is equally, in our submission, a
62 clear legislative intent that power be provided at the lowest
63 possible price consistent with a reasonable level of service,
64 and chasing this notion of a commercial entity to the extent
65 that it costs ratepayers money is not, in our view, either
66 mandated or justified by the legislation that governs this
67 Board in its considerations.

68 Getting back to the question of firsts. This is,
69 because of the legislative change, the first time that the
70 industrial customers have been before this Board as
71 regulated customers, if we may call them that. And I guess
72 it may have been that Mrs. Butler was aware that she wasn't
73 going to use all of her time that she actually took time this
74 morning to point out to us that this is at base an adversarial
75 proceeding. We all knew that. It was no surprise, I don't
76 think to anyone that Mrs. Henley Andrews and I came in
77 here to advocate for positions that would assist our clients,
78 just as Ms. Butler came in to advocate for positions that
79 would assist her client and so on. It is an adversarial
80 proceeding and the interesting thing about this as a first
81 adversarial proceeding involving industrial customers is
82 that in looking at issues revolving around the cost of
83 service, up until this point the Board has only had the
84 benefit of one side. The Board has to this point been
85 regulating retail rates. There have been industrial rates but
86 the Board has not regulated them. Now, you are in a
87 different position in that you have two obviously
88 competing interests when one deals with cost of service
89 issues and the industrial customers are not here to impose
90 costs upon Newfoundland Power or its customers. The
91 industrial customers are here, as we said on the 24th of
92 September, to ensure that we pay our fair share, but no
93 more than our fair share of the cost of providing electrical
94 service in the province, so you now have the benefit of the
95 workings of the adversarial system with the two principle
96 classes of customers of Hydro, that is to say, the retailer
97 and the industrial customers fully represented and putting
98 positions.

99 I think I said as well in my opening that in
100 contrasting revenue requirement issues with cost of service
101 issues that there would be different positions taken by
102 different parties depending on the nature of the issue and
103 I think we have seen that come to fruition here in that while
104 we can support many of the very well founded positions
105 that Newfoundland Power takes on revenue requirement

1 issues, we have considerable doubt about some of the
2 rather dubious positions that they had espoused in respect
3 of cost of service issues.

4 So bearing in mind that dichotomy and the fact
5 that there is an adversarial nature to the proceeding, I want
6 to move to deal with the short number of subjects that I
7 wish to address in the course of this submission.

8 One final point though which relates to the nature
9 of this as the first hearing in which industrial customers are
10 an active party in that sense. Ms. Greene made a point of
11 saying that the rates for industrial customers will, in fact, be
12 lower even with the proposed increases than they were in
13 1992, and while that is something that the industrial
14 customers can certainly appreciate, in our view this simply
15 goes to illustrate that the rates in 1992 were clearly too
16 high. I think that is demonstrated in the evidence when
17 one looks at the rates of return, the interest coverage that
18 has been achieved by Hydro from its industrial customers,
19 and the revenue to cost ratios which were dealt with with
20 Mr. Wells and some of the other witnesses.

21 So as a part of the adversarial nature of the
22 proceeding, Ms. Greene will highlight, as Ms. Butler has,
23 the parts of the evidence that tend to support their
24 particular case, and the impression that rates for industrial
25 customers are falling is a good one for Ms. Greene to point
26 out to the Board. Equally from our side we have to point
27 out that they have not fallen far enough and the perception
28 of their falling is simply a reflection of the fact that they
29 were too high in the beginning.

30 (2:15)

31 The revenue requirement issue that I wish to deal
32 with relates to the cost of capital and attached to that, I
33 guess, in a way is the question of capital structure. As
34 pointed out in our written submission from our viewpoint,
35 with the adoption which we continue to strongly
36 recommend of the ATWACC approach to the determination
37 of rate of return, the capital structure in the sense of the
38 debt equity ratio becomes irrelevant. The formulation used
39 by the ATWACC method, as Dr. Vilbert pointed out on a
40 number of occasions, is one that is independent of capital
41 structure, except on the very fringes, if financial distress is
42 to be felt, so this, I think, is just another of the good
43 attributes of the ATWACC from the point of view of this
44 Board, because realistically there's nothing this Board can
45 do to affect the actual capital structure of Hydro. If
46 government is going to take dividends and reduce the
47 equity it will do that and it seems to be generally agreed
48 that there's not really anything the Board can do about it,
49 other than perhaps deem a capital structure which doesn't
50 exist, which doesn't actually exist and get into all of the
51 complications that that involves.

52 With the ATWACC approach, the calculations are
53 done in such a fashion that doesn't make any real
54 difference whether Hydro is moving toward a different
55 capital structure or not. The overall average total weight of
56 average cost of capital will remain the same and the
57 appropriate division to equity and debt can be done, so
58 from that point of view we do continue to recommend to
59 the Board the adoption of that type of provision.

60 The interesting reaction, I guess, to this approach
61 by Hydro in their written submission was that nobody has
62 adopted this. This is an unknown, hasn't been actually
63 used anywhere.

64 It's interesting that Hydro doesn't take the same
65 position with the RSP. Everyone agreed that the RSP was
66 a totally unique vehicle and, as was pointed out in the
67 course of some of the cross-examination, it has been
68 (inaudible) in this jurisdiction now for 17 years and no
69 other jurisdiction in North America or anywhere else that
70 we know of has adopted a plan of this nature. I think it was
71 Mr. Kennedy who raised the topic as to whether or not this
72 may, in fact, be something like the cutting edge, and after
73 17 years I think it was pointed out that the cutting edge, if
74 it was there originally, has long since passed.

75 On the other hand, the ATWACC is, in fact, on
76 the cutting edge and represents a sound statement of
77 principles that this Board can and, in our submission,
78 should adopt to simplify its own considerations with
79 respect to rate of return, and to make the whole process
80 more transparent in terms of what we are doing. Contrary
81 to what was stated in the submissions by Hydro, the
82 Ontario Energy and Utilities Board actually did, and this
83 appears in the consent that Ms. Greene cited, they actually
84 did use the ATWACC as well as their traditional method
85 for the purpose of determining rate of return in that
86 proceeding.

87 There was also a bit of discussion about the
88 positions of other parties relative to the ATWACC, and Dr.
89 Kalymon was quoted along the lines of saying, and this, I
90 think, we don't need to go to, but the November 14th
91 transcript, at page 6, at line 41, saying that it was
92 unnecessary to bring in the complication of taxes. He then
93 goes on to misunderstand, with all respect, the theory that
94 Dr. Vilbert had put forward and his misunderstanding was
95 highlighted in the redirect which appears at page 12 from
96 the same day at line 87, and he indicated that he had, in
97 fact, mis-spoken himself.

98 The other reference in the argument of Hydro was
99 to what the AEUB had said in respect of taxes and the
100 ATWACC method collapsing into the traditional method if
101 you took the tax away. I will just refer you to the redirect of
102 Dr. Vilbert in that regard. It starts at the bottom of page 15

1 of the transcript of November 13th at line 91, and Dr.
2 Vilbert's explanation goes from lines 1 to 24 of the next
3 page, page 16 of that transcript, but it was quite clear that
4 Dr. Vilbert's evidence in Alberta was not directed toward a
5 nontaxable entity at all, it was actually directed toward the
6 taxable entity, so consistent with the nature of the
7 adversarial proceeding, those references that Ms. Greene
8 has made will be put in context in our submission by
9 looking at these other references to which I've directed
10 your attention now.

11 The interesting part to me of the submissions of
12 both Hydro and the other parties in the written form on the
13 question of equity is that no one has addressed the
14 argument which is on page 100 of the hard copy of the
15 industrial customers submissions which deals with the
16 question of ratepayers equity, and it may be that the other
17 parties simply do not have an answer to this position, but
18 it is one that the Board, in my submission, should look to
19 very carefully in this, the first hearing where Hydro is being
20 regulated on a rate of return basis. Up until this hearing it
21 didn't make any difference what equity was in Hydro.
22 Hydro was regulated on the basis of a margin over interest
23 coverage, so that whether or not there was a million or 100
24 million dollars of equity in Hydro made no difference to
25 what this Board had to do. Now it makes a big difference
26 to what this Board has to do, how much shareholders
27 equity is in Hydro, and not just shareholders equity, but
28 regulated shareholders equity, and follow through the
29 argument that begins at page 100 of the hard copy of the
30 Industrial Customers' submission.

31 Ms. McShane and everyone who spoke to it said
32 that the investor is entitled to a return and we fully agree
33 that the investor is entitled to a return. For every dollar
34 that the government has invested in the regulated retained
35 earnings of Hydro they should have a fair and reasonable
36 return. However, that return, as of today, would amount to
37 zero, simply because the government has not invested a
38 single dollar, not one in Newfoundland and Labrador
39 Hydro on the regulated side. It's apparent in the financial
40 statements that are at IC-211 when Hydro was created it
41 assumed the debt of the Power Commission and it assumed
42 the assets. However, the liabilities were greater than the
43 assets, so there wasn't a dollar of equity in it to assume at
44 that point, government hasn't contributed a dollar since,
45 and it is therefore, on financial principles that Ms.
46 McShane adopts, not entitled to a return.

47 (2:30)

48 Hydro has, and the references are in the
49 submission, characterized this money, these retained
50 earnings in the past which came from the interest coverage
51 as being a contribution by ratepayers to Hydro's capital
52 program. That's what we were told we were paying in the

53 1980s, and that's how the interest coverage was justified to
54 the Board by the president of Hydro as he then was, so as
55 ratepayers as a group we are asking you no more than that
56 you hold Hydro to what they said in the 1980s when they
57 wanted this interest coverage that they would, in fact, use
58 it as a contribution to their capital program, and in order to
59 do that all the Board has to do is to segregate those
60 retained earnings because they all came from ratepayers,
61 every cent, segregate the regulated retained earnings. It
62 will constitute zero cost capital in Hydro's capital structure
63 and it will be available to Hydro and to Hydro management
64 to use and provide the benefits to the ratepayers which it
65 was supposed to provide in the first place.

66 A brief comment on the frequency converters
67 before I move to the RSP. Ms. Greene highlighted the
68 comment about the breach ... what we regard as the breach
69 of the historical pact in connection with these converters,
70 and it was, I think, a noteworthy comment and one that was
71 thought out in that there has been genuine puzzlement for
72 quite awhile, I think, on the part of the industrial customers
73 affected by this that Newfoundland and Labrador Hydro,
74 with whom the industrial customers generally have such a
75 good relationship, have not been able to see the light in
76 respect of this particular issue. Think of it this way ... and
77 the argument is in the submission, I don't need to repeat it,
78 but, think of it this way. If the decision had been taken in
79 the 1960s not to put in these permanent frequency
80 converters, as Hydro called them, and some of the
81 generation at Bay d'Espoir had been 50 cycle power as a
82 result, today Hydro would be applying to abandon that 50
83 cycle service, and it would have to apply to this Board to
84 abandon it. It's not allowed to abandon a service without
85 approval of the Board, and what would it have to do? It
86 would have to go out today and buy frequency converters
87 in order to continue to supply customers their demand.
88 This notion that ... the position that Ms. Greene puts as to
89 why other customers should pay for equipment that is not
90 providing any service to them is simply based on wrong
91 facts. It is providing, and continues to provide, and has
92 provided since the 1960s, a service to all the customers
93 because it has allowed the grid to be created in a certain
94 way which was the cheapest way at the time to do it, and is
95 still the cheapest way to do it so the decision was correct.
96 Hydro now, for some reason unknown to us, wishes that
97 history was different, but I'm afraid it isn't. Those are the
98 facts, that the grid continues to get the benefit of the
99 frequency converter and it should therefore be a common
100 cost.

101 The RSP. The RSP has been a significant issue in
102 this hearing, and we have attempted, starting at page 58 of
103 the hard copy, to take a broad view of rate stabilization
104 without necessarily calling it the Rate Stabilization Plan or
105 the RSP. The Board has heard a great deal of evidence, and

1 I think it is fair to say that the proposal of the industrial
2 customers for the future of the RSP is much more in line
3 with North American experience and the way others handle
4 these difficult issues, and we point out that Ms. McShane,
5 herself, in evidence in another proceeding which is at NLH-
6 99 points out that the risk of load forecasting should, in
7 fact, be the utilities and not be subdivided among any one
8 group of customers, so once you take the load element out
9 of RSP the system is very much simplified.

10 I note Ms. Butler's point this morning as to the
11 difficulties that she sees in the so called blended RSP,
12 which is one plan. Ms. McShane answers her first
13 difficulty in that she says if an industrial customer left then
14 retail customers would have to pay. If an industrial
15 customer leaves, all customers have to pay. That is the
16 way it should be and I don't think there's any real issue
17 about that. Why should the risk of a competitor fall upon
18 the remaining industrial customers? It's not, with respect,
19 a rational position. Her second point is one that is not
20 addressed in our submission, and that is that the additional
21 revenue from the industrial ... from the rural customers goes
22 into the retail plan, and that is a peculiarity that arises out
23 of the way the rates for rural customers are set. I don't
24 think we would really have a problem if those revenues
25 were again funnelled back to reduce the deficit in some
26 other fashion. You don't have to have two RSP plans in
27 order to do that. All you have to do is credit that revenue
28 back to the rural deficit so that it goes where it should go,
29 so that is not an issue. Her third point related to Mr. Osler's
30 testimony, and we've already spoken of Ms. McShane's
31 evidence and, you know, the general accepted principle
32 that load variance is the utility's risk.

33 So in terms of the ongoing plan, I think the
34 industrial customers have outlined a rational and more
35 appropriate system, and the Board is in a position to carry
36 on and direct Hydro to implement that at the present time.

37 In this instance the adversarial system has thrown
38 up a number of interesting points in that both Hydro and
39 Newfoundland Power are wedded to this system and it is
40 clearly in their interest. It preserves their bottom line, it
41 takes away all their risk and has allowed Hydro, for
42 instance, to stay away from this Board for ten years
43 without having to come back for a rate increase. The
44 difficulties in the system are seen by examining the past,
45 and it is, I think, not at all unfair to say that the existing
46 system once it is examined in detail becomes for most
47 people incomprehensible. The history of the system has
48 been examined by Mr. Osler in his evidence and it is quite
49 frankly clearly unfair to the industrial customers and
50 reflects the fact that the industrial customers were not part
51 of the proceedings in the same way that they are today
52 when this system was designed.

53 Hydro takes the position that the industrial
54 customers must have known not later than 1993, when Mr.
55 Sturge wrote to Mr. Dean the letter that is attached to IC-
56 286E. Now, we know how we've laboured through the RSP
57 at this hearing. Mr. Osler gave a great deal of evidence
58 about the RSP, and if you look back specifically to his
59 redirect evidence and to his taking us through IC-271 and
60 some of the other information requests it became clear that
61 Mr. Osler understands this now. He is ... he knows what
62 happens and quite frankly I think he was an impressive
63 witness and one who can establish that. He's good at what
64 he does. It took Mr. Osler and his associates four rounds
65 of information requests to get out the information that they
66 needed in order to understand what was really happening
67 with this RSP. You need all of that information and no one,
68 I don't think, can, from the three page letter from Mr. Sturge
69 to Mr. Dean, get all that information. You need all that
70 information and you have to be a cost of service expert in
71 order to understand what's happening with the RSP. To
72 understand what's happening with the RSP from this three
73 page letter, Mr. Chairman, I would submit, with respect, that
74 you need to be a clairvoyant cost of service expert. It's just
75 impossible to take from the information that was on the
76 record in '93 what is actually happening. Where does it
77 say in here that if another customer in the industrial class
78 goes out of business it's going to cost you an extra
79 \$322,000 a year? That's the sort of red flag that you need to
80 satisfy yourselves that the industrial customers knew what
81 was going on.

82 I need to refer briefly to Ms. Butler's submissions
83 again where she talks about the ... Mr. Osler's testimony,
84 and again, in a quite legitimate fashion, to highlight what is
85 in support of her case, says that Mr. Osler in some of his
86 evidence indicated that a number that was referred to in his
87 evidence, and particularly, specifically it's the number in the
88 footnote, footnote 22 on page 9 of his second
89 supplementary evidence, wasn't the right number, and he
90 was right, but by the time he got back with redirect ... and
91 the numbers all appear on Exhibit IC-6 ... it became clear
92 exactly what was going on, and it wasn't, with respect, what
93 Ms. Butler said was going on, that the industrial customers
94 were saving money. They weren't just losing quite as much
95 as had been said, and Mr. Osler was very careful in what he
96 said in his evidence. There is insufficient information on
97 the record to quantify the specific impact of these changes,
98 but for 2000 alone the impact was expected to be a credit to
99 the IC RSP of the order of \$1.5 million. IC-6 shows that the
100 \$415,000 which is charged against the industrial customers
101 is balanced by a credit on the other side, the fuel savings
102 and so on, of \$442,000. The only thing is, that \$319,000 of
103 the saving is credited to Newfoundland Power, \$29,000 of
104 the saving is credited to the rural customers and the
105 industrial customers, who take the whole hit for the

1 \$415,000 get only a credit of \$93,000, so it does cost them
2 \$322,000 in that particular year, and that's just one part of
3 this \$1.5 million, so Mr. Osler's statement is factually
4 correct in my submission. The credit may be \$1.4 million
5 instead of \$1.5 million, but it is on the order of 1.5 million,
6 and clearly demonstrated in his evidence.

7 The Board has to step away from the adversarial
8 part of this and balance both sides. It's not for the Board
9 to look at just what's highlighted on one side or just what's
10 highlighted on the other side, but to look at all the
11 evidence. If you're referred to a piece of cross-examination,
12 look for the redirect. You'll find clarifications, you'll find
13 explanations, and the Board has to make that balance itself.

14 (2:45)

15 The issue of whether the RSP constitutes any sort
16 of retroactive regulated ... well, the suggestion that there
17 should be a credit back to the industrial customers is said
18 by Newfoundland Power and others to run contrary to
19 certain provisions of the *Electrical Power Control Act*,
20 and that subject was anticipated and is specifically dealt
21 with in our submissions where, at the end of our section on
22 the RSP, beginning at page 79, we deal directly with those
23 provisions and explain through to page 81 why this is not
24 an alteration of a previously existing rate. This is simply
25 establishing how the balance in the RSP is going to be
26 recovered, if at all, and that is always something that the
27 Board reserved to itself. That's the whole reason why there
28 was a cap on the RSP in the first place. All the cap ever did
29 was require Hydro to come back. Obviously, when the cap
30 was exceeded the Board was going to deal with the
31 balance, and the Board has credited things and debited
32 things to the RSP balance from time to time and certainly
33 has the power to do that and always had the power to do
34 that.

35 So in summary, with respect to the RSP, Mr. Chair,
36 there are issues for the future to be decided, and the
37 industrial customers, rather than suggesting that the whole
38 process be abandoned or that it be held sacrosanct and not
39 touched under any circumstances, have put forward a
40 reasoned proposal, in our submission, for a new way of
41 dealing with these issues, and it is one that the Board can
42 direct Hydro to adopt, and at the same time, the Board
43 needs to address the unfairness that has appeared and is
44 demonstrated in the evidence with respect to the previous
45 workings of the RSP and provide the appropriate relief to
46 the industrial customers.

47 And when you're dealing with the evidence on
48 that, don't forget also that what is not said and what is not
49 asked can also be evidence from which you can draw
50 conclusions. Mr. Dean was on the stand. He was not
51 cross-examined about the 1993 letter, he wasn't asked what

52 he took from it, what he couldn't take from it, and the fact
53 that those things were not put to him when the opportunity
54 was there to put them to him speaks a great deal as to the
55 validity of the position that both Hydro and Newfoundland
56 Power would put to you now to the effect that the
57 industrial customers knew what was happening under the
58 RSP.

59 Those are the points with which I intended to
60 deal, Mr. Chair. I'll leave it to you as to whether we break
61 at this point before we move to Ms. Henley Andrews.

62 MR. NOSEWORTHY, CHAIRMAN: Okay.

63 MS. HENLEY ANDREWS: Stop the clock.

64 MR. NOSEWORTHY, CHAIRMAN: We'll stop the clock.
65 We'll take a short ten minute break rather than interrupt you
66 in full flight, Ms. Henley Andrews.

67 (break)

68 (3:00 p.m.)

69 MR. NOSEWORTHY, CHAIRMAN: Good afternoon, Ms.
70 Henley Andrews, could I ask you to begin please?

71 MS. HENLEY ANDREWS, Q.C.: Thank you, Mr. Chairman
72 and Commissioners. I am going to start with revenue
73 requirement issues and by revenue requirement issues I
74 mean those areas where the issue is how much Hydro
75 should recover in total from its customers, so to some
76 extent, as between the intervenors, this is the issue where
77 there is the least disagreement.

78 We have gone through all of the submissions of
79 the parties and have identified \$17,395,646 in potential
80 savings, which is only \$4,500 off what Hydro says it needs
81 as a result of this rate hearing. Most of the areas are also
82 identified by Newfoundland Power. What I'm going to do
83 is go down through each of them so that you see or hear
84 them all together and address our position with respect to
85 some items as I go.

86 The first issue is the cash working capital
87 reduction. As Ms. Greene pointed out this morning, and as
88 we were aware, there is a mistake in our final submission.
89 It is in fact a typographical error, and that is that there is an
90 extra zero on page 121. It says this would reduce the
91 revenue requirement by approximately \$10 million, and it
92 should be approximately \$1 million. The actual figure by
93 our calculation is \$982,646, and that is calculated by taking
94 the, Mr. Drazen's change in the cash working capital
95 allowance of \$13,279,000 and multiplying it by the return on
96 rate base to which Ms. McShane testified of 7.4 percent. If
97 you do that multiplication you will get the \$982,646.

98 We note that this has not been mentioned in
99 Newfoundland Power's submission. We don't know

1 whether it's an oversight or reflects the fact that they don't
2 want it included in their calculation of cash working capital
3 in the future.

4 Hydro's revision with respect to hydraulic
5 generation, as Hydro pointed out this morning, and as all
6 the intervenors have, reflects a \$400,000 savings for its
7 customers. Newfoundland Power, in utilizing a 30 year
8 rolling average on hydraulic production rather than the
9 basis that Hydro has proposed projects a savings of \$4.6
10 million. We don't have enough technical expertise to give
11 an opinion one way or another with respect to the most
12 appropriate history to be using. However, we do have
13 some concerns with respect to the data that was used,
14 some of the very old data based on river flows, particularly
15 since not all of the tributaries to the reservoirs are counted
16 for the purpose of determining those historical inflows.
17 Given that the older data shows much dryer history than
18 the later data, we do have some concerns with respect to
19 the reliability of that data, and it is on that basis that we are
20 raising questions with respect to Hydro's proposed
21 hydrological forecast.

22 Newfoundland Power has calculated that there is
23 \$2,850,000 to be saved if we use an expected average
24 weather fuel efficiency of 633 kilowatt hours per barrel for
25 Holyrood. This 633 kilowatt hours per barrel reflects what
26 could be expected in an average water year. Hydro is using
27 its hydraulic production numbers based on an average
28 water year. It's use of 610 kilowatt hours per barrel is based
29 on a low, a high water time period which means that it is the
30 time when the Holyrood thermal generation is least
31 efficient. 600 kilowatt hours per barrel results in too much
32 room to manoeuvre for Hydro. They have, in utilizing both
33 average water and an efficiency factor based upon a high
34 water year rather than an average water year, they have
35 built in both forecasts the most favourable data to Hydro.

36 The diesel fuel forecast change as acknowledged
37 by Hydro results in a reduction of \$300,000. Newfoundland
38 Power has proposed a vacancy allowance at four percent
39 based upon Hydro's own historical record with respect to
40 its vacancies. As far as the industrial customers are
41 concerned, this is a reasonable position and the \$800,000 in
42 proposed savings should be added to the list.
43 Newfoundland Power has also proposed a capital
44 expenditure reduction and has quantified the related
45 effects. This is from eliminating the telecommunications
46 plan, capital expense, and Harbour Deep only. It results in
47 a savings, or would result in a savings of \$1.7 million. The
48 industrial customers, as noted and outlined in detail in our
49 written submission, have serious problems with respect to
50 the way in which Hydro has documented its proposed
51 capital projects. We have outlined our recommendations
52 for safeguards for all of the parties in the future and

53 guidelines to be given to Hydro. The Board has to utilize
54 its own discretion with respect to Hydro's capital budget,
55 and the Board has to be satisfied that it has sufficient
56 evidence before it that the expenditures are reasonable and
57 prudent. This is required by the power policy of the
58 province as set forth in Section 3 of the *Electrical Power
59 Control Act, 1994*. It is not enough for Hydro to say on
60 any of these expenses that the Board's consultant hadn't
61 indicated that they're unreasonable.

62 The Board must be satisfied that they are
63 reasonable and that they are prudent. We would submit
64 that on most of the projects that have been submitted to
65 you, there is insufficient information provided to the Board,
66 even after the replies to the information requests to satisfy
67 the Board that these expenses are needed in the 2002 test
68 year. There are obviously some projects which should go
69 ahead and those are the projects to which we have already
70 agreed. With respect to those outlined in our brief to
71 which we don't agree, our objection is that we don't think
72 they're sufficiently documented, so we weren't in a position
73 to make a decision as to whether they were proper or not.

74 Hydro's position as expressed today with respect
75 to deferral of the costs of the hearing is interesting.
76 Newfoundland Power says that if you split the deferral and
77 you take some of the costs in the 2001 year then the
78 potential savings is \$500,000. The Industrial Customers'
79 position on that is that, in fact, none of the costs of the
80 hearing should be deferred. They are incurred ... those that
81 have been incurred in 2001 should come out of Hydro's
82 2001 budget. The fact is that Hydro has not had a rate
83 hearing in close to ten years. In fact, it's ten years this
84 month since the start of its last rate hearing. It is not too
85 much to ask that those costs be absorbed.

86 The thing that we find most interesting about
87 Hydro's position this morning is that somehow or other its
88 position on deferral of costs has now been tied to the
89 Industrial Customers' request for costs. In other words, if
90 you deny us our costs, Hydro is prepared to absorb its
91 costs in 2001, but if you grant us our costs, they're not, and
92 I think that this is a very unfair position to take to the
93 Board, and in fact, it is a position that is very unfair to the
94 Industrial Customers.

95 It says, in effect, we'll give all of Hydro's
96 customers the benefit of the doubt and we'll give them the
97 benefit of reduced expenses if you ding the industrial
98 customers for their own costs, and we don't think that that
99 is reasonable. But for the purpose of my calculation, I am
100 using Newfoundland Power's \$500,000.

101 With respect to Bay d'Espoir's street lighting, this
102 is an issue that was raised by both Ms. Greene and by Ms.
103 Butler. We don't have any problem with Newfoundland

1 Power's suggestion that that is a grant that should come
 2 out of Hydro's profit. We'd like to think we thought of that
 3 solution, but we didn't. It is not some Machiavellian
 4 attempt on the part of the Industrial Customers to shift
 5 costs to Newfoundland Power. We simply don't think that
 6 that \$60,000 in street lighting for a rural community should
 7 be treated as a common expense. I recognize in hindsight
 8 that the effect of proposing to treat it specifically assigned
 9 is that the rural deficit goes up and that Newfoundland
 10 Power ends up being responsible for the rural deficit. That
 11 was not our intent and we have no difficulty at all with
 12 respect to Newfoundland Power's proposal on how to deal
 13 with Bay d'Espoir street lighting.

14 Newfoundland Power has also indicated that there
 15 are some categories of Hydro's corporate communications
 16 plan which would not be allowed if it were Newfoundland
 17 Power. They have identified approximately \$75,000 in
 18 savings in the revenue requirement if those categories were
 19 eliminated. We support that.

20 In addition, Newfoundland Power has applied the
 21 productivity allowance suggested by Mr. Brushett, and has
 22 indicated that this would result in a savings of \$1.5 million.
 23 We agree with that. With respect to the interest charges
 24 related to the excessive dividend, we agree with
 25 Newfoundland Power's position that the \$1.5 million
 26 associated with that item should also come off Hydro's
 27 revenue requirement.

28 With respect to recall sales, interest savings, and
 29 the debt guarantee fee reduction, the total amount in
 30 potential savings from those items is \$800,000. That is
 31 indicated in Mr. Brushett's testimony. Having reviewed
 32 Hydro's submission with respect to this matter, it appears
 33 that Hydro doesn't understand our position with respect to
 34 the debt guarantee fee. Hydro is currently claiming as part
 35 of its revenue requirement a debt guarantee fee with respect
 36 to the deemed debt. I think our submission makes it
 37 perfectly clear that the Act provides that Hydro will pay, or
 38 the legislation requires that Hydro pay a debt guarantee fee
 39 based upon its debt, but there is no debt associated with
 40 the recall sales money that it holds, and therefore, there is
 41 no requirement to pay a debt guarantee fee on that amount
 42 of money, and it shouldn't be allowed.

43 The next item is the change with respect to the
 44 cash to the accrual basis for depreciation. Newfoundland
 45 Power has suggested that this amount of \$1 million, which
 46 is included in the revenue requirement, shouldn't be
 47 included at this point because of the total impact on rates,
 48 and that it, and that Mr. Brushett has indicated that it's not
 49 mandatory that it be done now.

50 With respect to capital expenditures, it was the
 51 Board's consultant, Mr. Brushett, who suggested that a 15

52 percent reduction in Hydro's total approved capital budget
 53 should be made to reflect its past practices, and this is its
 54 15 percent after his normalization adjustment, and it reflects
 55 Hydro's experience over the last ten years. We support
 56 that and the result would be a savings of \$328,000.

57 By my calculation, the total of all those amounts
 58 is \$17.395 million, and Hydro has indicated in its rate
 59 application that it has increased costs of \$17.4 million,
 60 which are justifying its rate application. If the Board
 61 approves those reductions in Hydro's revenue requirement,
 62 the Board would have to agree that there is no justification
 63 in any rate increase for any of Hydro's customers at this
 64 time.

65 In addition, in order that Hydro would continue to
 66 have operating flexibility which we submit they would still
 67 have a considerable amount of, even with those reductions,
 68 there is the issue of interest on overdue accounts, which is
 69 not accounted for in its submission, and the cost of which
 70 is unknown at this time. There is the potential for savings
 71 in fuel costs through strategic fuel purchasing, also
 72 unknown. There is the potential savings for effective
 73 consumer conservation programs to limit peak growth and
 74 to reduce Hydro's fuel consumption at Holyrood ...
 75 potential savings unknown. And there's the potential for
 76 Hydro to save money by reducing the duplication that
 77 exists between Hydro and Newfoundland Power, and
 78 taking a more coordinated approach to those areas where
 79 their services potentially overlap or where economies of
 80 scale are possible.

81 We have also submitted that there should be a
 82 reduction in the supplies inventory by \$600,000. That
 83 suggestion results from the cross-examination of Hydro's
 84 Mr. Roberts by Newfoundland Power.

85 Commissioners, this hearing is a critical hearing,
 86 not just for the year 2002, but for the years which follow.
 87 It is particularly critical for the industrial customers. The
 88 proposed rate increase for the industrial customers, overall
 89 rate increase is more than two times the proposed rate
 90 increase for Newfoundland Power and Hydro's rural
 91 customers. You have to ask yourselves how can that be,
 92 how can that be fair. If you want to see the impact of this,
 93 you need to look at IC-254, and in IC-254, it shows that for
 94 the industrial customers, the proposed rate increase at the
 95 beginning of this process for 2002 over 2001 was 18.6
 96 percent, now reduced to approximately 17 percent. By
 97 2003, however, in which there is not projected to be any
 98 increase at all in the actual rates to be charged, the
 99 industrial customers' effective increase over its 2001 costs
 100 is 27 percent, and by 2004, the year in which Hydro expects
 101 to implement another rate increase, it's expected to be 35
 102 percent. This is clearly indicated on page 1 of 2 of IC-254.

1 Why is there an increase of, an effective increase
2 of 27 percent in 2003 when there's not expected to be a rate
3 increase in 2003? The answer to that is the RSP. It is the
4 effect of recovery of the balance on the RSP starting in
5 2003. 27 percent is a big increase over two years. 35
6 percent is a huge increase over three years, particularly
7 when you consider the dollars that are actually involved in
8 those amounts for the four, and there are only four, island
9 industrial customers.

10 As I noted earlier, Hydro argues that because Mr.
11 Brushett said the costs are not unreasonable the Board
12 should accept them. That is not the purpose of a hearing.
13 If it were that easy, and if the Act provided that, there
14 wouldn't be a hearing at all. The Board would simply get a
15 report from its consultant and set the rates. The Board
16 must ensure that Hydro's rates reflect the policy that's set
17 out in the *Electrical Power Control Act, 1994*. It requires
18 reasonable rates and it requires lowest possible cost
19 consistent with reliable service.

20 This hearing has tested Hydro's hypotheses and
21 its resulting costs. We agree that it is not the role of the
22 Board to manage Hydro. We submit that our proposals for
23 the reduced revenue requirement in combination with the
24 proposals of Newfoundland Power and the proposals of
25 the Consumer Advocate don't do that, they don't manage
26 Hydro. They establish reasonable parameters within which
27 Hydro can manage its expenses. The end result is that the
28 Board will tell Hydro how much it can recover in its rates.
29 Hydro then has to manage that revenue and expenses.

30 All the potential cost savings which have been
31 outlined are measured, logical, well-documented and
32 consistent with Hydro's own records and evidence. It is
33 not what Hydro wants, but it is not radical and it is not
34 outside Hydro's own operating experience.

35 If you go to IC-30, Table 6, it shows what Hydro's
36 proposed 2002 increases in rates mean to the industrial
37 customers. You'll have to note when you look at that Table
38 6, that it does not include the impact of the RSP. When
39 you look at those numbers, it is clear that there are many
40 millions of dollars involved, nearly \$2 million for Abitibi
41 Stephenville alone. But that is not the only issue that is
42 before you.

43 Newfoundland Power has suggested that the
44 industrial customers have taken an approach which is to
45 feather their own nest. My mother always advised me that
46 people who live in glass houses should not throw stones,
47 and that advice would be well given to Newfoundland
48 Power. The industrial customers are not proposing change.
49 Hydro is, in fact, proposing change. If you look at IC-134,
50 Revision 1, and perhaps Mr. O'Rielly, we could bring that
51 one up, you will see, as you will in reviewing Mr. Budgell's

52 testimony, that Hydro in this hearing is the one who is
53 proposing changes in plant assignment. In the current
54 rates which were set in 1992, Great Northern Peninsula
55 transmission and generation is specifically assigned to the
56 rural customers. The frequency converters are treated as
57 common in the current rates. The Stephenville Bottom
58 Brook assets are treated as common, and the Doyles
59 Bottom Brook is treated as specifically assigned to
60 Newfoundland Power. That is what the industrial
61 customers would like to keep. Hydro is proposing to
62 change the assignment of those assets in this hearing. The
63 industrial customers were reasonably satisfied with Hydro's
64 1992 definition of common plant. Hydro has redefined, or
65 proposes to redefine its definition of common plant as
66 indicated in the testimony of Mr. Budgell and through
67 cross-examination, so that these assets get moved. So this
68 is not the industrial customers coming in to the Board and
69 saying we want change. This is the industrial customers
70 coming in to the Board and saying we want the status quo
71 on these assets, unless Hydro or some other intervenor can
72 satisfy the Board that these assets provide substantial
73 benefit to more than two customers of Hydro.

74 Now Ms. Greene in her argument referred to
75 benefit. She did not refer to substantial benefit. We
76 acknowledge the problem that Mr. Budgell identified, which
77 is that substantial benefit is a subjective evaluation, but the
78 fact is that that is the accepted definition of common plant,
79 and it does require a subjective evaluation. When you look
80 at the reality, Newfoundland Power seems to suggest that
81 if you're not a systems engineer you can't define
82 substantial benefit. Well I would suggest to you that in fact
83 an economist is in a much better position to look at the
84 issue of substantial benefit than a systems engineer. What
85 has been focused on by Newfoundland Power and by, or
86 more importantly by Hydro, is the fact that there is some
87 generation on the Great Northern Peninsula, for example,
88 and Newfoundland Power generation at the end of the
89 Doyles, Port aux Basques, Bottom Brook transmission line.
90 But in that process, as we have pointed out through out
91 cross-examination of various witnesses, the issue is, well
92 when these areas were interconnected ... take the Great
93 Northern Peninsula as an example, what was the impact on
94 the system? Well the truth is, that during peak demand, the
95 Great Northern Peninsula customers have increased
96 Hydro's requirements for peaking capacity. The generation
97 on the Great Northern Peninsula is not sufficient to satisfy
98 the peaking needs of the Great Northern Peninsula. This
99 affects the calculation of LOLH. It's equally true with
100 respect to Doyles, Port aux Basques, and Newfoundland
101 Power service area. Their demand during peak exceeds the
102 potential generation. Hydro's decisions with respect to
103 adding additional capacity and incurring the cost of
104 additional capacity depends upon its LOLH, and these

1 areas are negatively impacting that. Yes, it is true that there
2 is some possibility in light load conditions, that a few
3 megawatts of energy might make it from the Great Northern
4 Peninsula to the grid in order to help in a crisis, but most of
5 the crises don't occur during light load, and during normal
6 load and during maximum load situations, the generation in
7 those areas is insufficient to meet the demand in those
8 areas. As a result it's our position that Hydro has not
9 demonstrated that the interconnection, and therefore the
10 transmission lines interconnecting this generation to the
11 grid provides a substantial, or indeed any benefit to the
12 grid. It may, and you may be prepared to acknowledge that
13 it provides some benefit, but every one of the experts
14 indicated that substantial benefit meant more than minor,
15 above average. All these things are outlined in our written
16 submission.

17 Now the issues of converters is the same. Hydro
18 has tried to make the argument that it is the party that
19 comes up the middle in this hearing on the issue of cost of
20 service because it says its revenue neutral. Well we would
21 submit that Hydro is not, in fact, revenue neutral with
22 respect to these assignments. As a result of our
23 understanding of the cost of service methodology, Hydro
24 is not entitled, or at this point in time is not able to earn a
25 return on its deficit areas, its rural areas, and that was a
26 previous decision of the Board, which was that it would be
27 unfair to enable Hydro to earn a rate of return in areas
28 where it was carrying a deficit that was also being passed
29 on. If the Great Northern Peninsula generation and
30 transmission is treated as common, it becomes part of the
31 rate base upon which the profit is calculated. It is our
32 calculation, very rough, that Hydro's increased profit as a
33 result of its proposal to reassign these assets is
34 approximately \$300,000. It is not revenue neutral. Equally
35 important, reassigning these assets makes it look like the
36 deficit is less and makes it look like there's much less of a
37 subsidization of Hydro's rural customers by Newfoundland
38 Power.

39 On transformer losses, Ms. Greene referred to IC-
40 227. We would point out that Mr. Dean testified with
41 respect to his calculation of the proposed effect of Hydro's
42 treatment of transformer losses. It is contained in his pre-
43 filed evidence, and his estimate is \$75,000 to \$100,000 for
44 Stephenville alone. Hydro, in IC-227 did provide an answer
45 to a question that related to transformer losses. Mr. Dean
46 was not cross-examined with respect to this number. It is
47 a basic principle of evidence that facts have to be proven
48 through testimony, and basically then dealt with through
49 cross-examination. Having chosen not to cross-examine
50 Mr. Dean with respect to his estimate of the effect on
51 Stephenville, then his evidence of the \$75,000 to \$100,000
52 is, has to be accepted. In fact, what it reflects is his
53 calculation of some things that are not included in IC-227,

54 but the dollar amount with respect to transformer losses is
55 much less important than the principle.

56 Hydro has said that the current treatment of
57 transformer losses is unfair, and it has proposed another
58 treatment, a different treatment of transformer losses. The
59 position of the Industrial Customers is that its proposed
60 treatment of transformer losses is equally unfair. Now we're
61 in the unenviable position as a group of industrial
62 customers that what Hydro is proposing is much more
63 beneficial to one of our group, namely Corner Brook Pulp
64 and Paper, than what we are proposing, because Corner
65 Brook Pulp and Paper was going to save money as a result
66 of Hydro's proposal while the other industrial customers
67 were going to pay a lot more. So we actually had to take a
68 very careful look at this particular issue, and even though
69 our proposal will also cost a little more for Corner Brook
70 Pulp and Paper, we feel that the proposal that is contained
71 in our written submission with respect to transformer
72 losses is fair, not only to the industrial customers, but also
73 to Hydro's other customers. It reflects the fact that some
74 customers take at 66 kV, others take at 230 kV, and some
75 others take at 138, thank you, and by using the cut off of 66
76 kV, you eliminate any discrimination as between different
77 customers at different transformers.

78 With respect to the 1-CP to 2-CP issue on
79 generation demand, the only witness who favoured any
80 more than 2-CP was Mr. Brockman. That would transfer
81 \$360,000 of costs from Newfoundland Power to the
82 Industrial Customers. All the other witnesses, including
83 Mr. Brickhill, indicated that they either favoured 1-CP or
84 had no objection to 1-CP. We submit that the 1-CP which
85 is already contained in the interim order of the Board in its
86 1993 cost of service methodology should be adopted.

87 In keeping with my expression that people who
88 live in glass houses shouldn't throw stones, I would
89 commend to you page 13 of the 1993 cost of service
90 methodology report of this Board, and I commend that
91 because the summary indicates that Newfoundland Power
92 submitted that Hydro rural was a single customer class
93 under the Board's previous guidelines and there was no
94 need to change them, but while Hydro rural constituent
95 classes need to be recognized for purposes of rate design,
96 Hydro rural remains a single class, as does Newfoundland
97 Power, vis a vis Hydro's overall cost of service.
98 Newfoundland Power further argued that Hydro's approach
99 would assign costs to Newfoundland Power and
100 Industrials for lines serving only rural customers, and that
101 this contradicts the pre-filed testimony of Dr. Surekaiis
102 (*phonetic*), that each customer class should be allocated
103 only those functions used in supplying service to it. So, in
104 fact, at the 1993 cost of service methodology hearing,
105 Newfoundland Power's view with respect to the

1 transmission on the Great Northern Peninsula was that it
2 should remain specifically assigned to Hydro rural. Now
3 why would its position have changed? And the answer is,
4 in fact, very simple. At the time of the Board's last hearing
5 with respect to Hydro's rates, the industrial customers and
6 Newfoundland Power were sharing in the deficit, so at the
7 end of the day what you transferred on one end, you
8 picked up on the other, that if you got the costs specifically
9 assigned, well then you picked it up in the deficit, and we
10 all picked it up proportionately.

11 However, as a result of the change to *The*
12 *Electrical Power Control Act*, so that the industrial
13 customers no longer contribute to the deficit, any
14 assignment of assets or re-assignment of assets to common
15 means that the industrial customers pick up a share that
16 they didn't otherwise have and Newfoundland Power's
17 contribution to the deficit is in fact reduced. So I think that
18 the intervenor to whom you must look in terms of change
19 of position is in fact Newfoundland Power, which has
20 changed its position significantly and reversed it with
21 respect to the treatment of the transmission on the Great
22 Northern Peninsula.

23 Now, we raised during our testimony, during our
24 cross-examination, the issue of the Burin Peninsula. Right
25 at the present time the Burin Peninsula transmission
26 technically serves two customers. It serves Hydro rural
27 and it serves Newfoundland Power. There is an argument
28 that the line going down the western side of the Burin
29 Peninsula should be specifically assigned to
30 Newfoundland Power and that the line going down the
31 eastern side of the Burin Peninsula can be treated as
32 common.

33 We've decided not to take that position with
34 respect to this hearing, however, we do have some
35 concerns that Newfoundland and Labrador Hydro has
36 very, very few customers, roughly 150, I think it is, in a very
37 small section of the Burin Peninsula which is
38 overwhelmingly served by Newfoundland Power, and one
39 of the issues which ought to be investigated is whether it
40 is reasonable and practical to transfer those customers to
41 Newfoundland Power, and therefore perhaps save in some
42 duplication costs.

43 One of the issues which everybody has focused
44 on to some extent is the issue of a generation credit. We
45 think that we have been misunderstood with respect to our
46 position on the generation credit and our position may now
47 be better understood as a result of our written submission.
48 We have never suggested that the industrial customers are
49 looking for an Interruptible B rate that is the equivalent of
50 the generation credit. In fact, what we are suggesting is
51 that the mechanism by which Hydro recognizes
52 Newfoundland Power's generation support to meet peak or

53 emergency situations ought to be calculated in the same
54 general basis that the Interruptible B credit is. In other
55 words, it should be transparent, everybody should
56 understand how it works, and it should be calculated using
57 the same general parameters, and that would have several
58 benefits.

59 First of all, it would treat similar services similarly.
60 Now it might be that because of an ability to provide a
61 slightly different service, but only slightly different, that
62 the compensation for it might be a little different than the
63 compensation for, for example, Abitibi in Stephenville or
64 any other industrial customer taking advantage of an
65 Interruptible B rate, but the principle remains that similar
66 services, all of Hydro's witnesses, everybody's witnesses,
67 indicated that it was a similar service, should be
68 compensated, and, more importantly, those services
69 should, the costs of those services should be transparent.

70 (3:45 p.m.)

71 One of the problems that we have with the
72 generation credit is that it treats Newfoundland Power's
73 generation as if it's serving the system all of the time, and
74 it's not, so Newfoundland Power's peak is treated as if it is
75 generating its own energy all of the time and it only
76 generates that energy on their circumstances. This shifts
77 costs to the industrial customers for every single hour of
78 generation and we don't think that that's fair and we think
79 that the evidence that has been submitted through our
80 witnesses, and in particular the exhibit that was put to Mr.
81 Brockman, indicates that the amount of compensation that
82 Newfoundland Power is receiving for the availability of that
83 generation is out of proportion to what it ought to be.

84 Now, the demand energy rate is an interesting
85 thing because as we have seen through the evidence of
86 Mr. Brockman and others, in 1990 and 1992, Hydro and
87 Newfoundland Power were all in favour of a demand energy
88 rate for Newfoundland Power. They both wanted it, but the
89 Board didn't set one. The Board asked them to work
90 together to design a rate, and here we are in 2002 and they
91 have not in ten years been able to agree on an appropriate
92 rate design for demand energy rate. Given ... and that
93 seems to be the entire reason ... I mean, this whole revenue
94 volatility thing, as far as I'm concerned, is a red herring.
95 The thing is that there's obviously a little bit of a battle as
96 to who should bear what risk involved in the design of that
97 rate. Given that they have not been able to come up with
98 their own rate, then basically the Board is now in the
99 position where it should impose a solution.

100 The Newfoundland Power revised forecast as
101 submitted to the Board in October, our position again as
102 detailed in our written submission, is that it is not
103 reasonable. We believe that as a result of our cross-

1 examination of various witnesses we have shown that
2 Newfoundland Power has not in the past been able to
3 achieve the type of load factor that its proposed new
4 forecast would lead you to believe would be their load
5 factor in 2002. We believe that the evidence indicates that
6 it's not reasonable.

7 There is, however, one other issue with respect to
8 forecast, and we're really not clear what Hydro's position is
9 on this because we're not sure we fully understand what
10 they've said in their submission. You may recall that Hydro
11 indicated that Corner Brook Pulp and Paper had, when it
12 indicated its amount of power on order for 2002, and I will
13 point out that it will pay for that demand, whether it utilizes
14 it or not, and if it exceeds that demand it will have to pay for
15 non-firm rates. The question is whether that should be
16 incorporated in the forecast. We believe that it ought to be
17 and certainly because it is firm and it is a commitment for
18 which there are negative consequences if Corner Brook
19 Pulp and Paper is wrong.

20 We think Hydro may have said that it's not
21 planning to make any further changes with respect to the
22 forecast, but if it is prepared to make changes with respect
23 to the Newfoundland Power forecast, it certainly should be
24 prepared to make changes with respect to the Corner Brook
25 Pulp and Paper forecast which also ultimately affects the
26 demand and the load factor for the industrial customers as
27 a whole, and we want to make sure that the Board actually
28 directs Hydro that when it does its final cost of service,
29 that this projection by Corner Brook Pulp and Paper for a 12
30 megawatt reduction in its amount of power on order should
31 be accommodated.

32 With respect to the deficit, we don't believe that
33 Section 17(5) of *The Public Utilities Act* authorized Hydro
34 to break the law, and with respect to the phase-out of the
35 industrial contribution to the subsidy, for whether the
36 reasons based on Government policy and all that kind of
37 thing are justified or not, it does not take away from the fact
38 that the legislation required it to be phased out, and IC-8
39 and IC-248 indicate that as a result of that statutory breach
40 the industrial customers have paid \$9,681,000 in additional
41 contribution to the rural subsidy which they otherwise
42 should not have paid.

43 With respect to Board counsel, we agree with Mr.
44 Kennedy's interpretation of the law as set forth at pages 21
45 and 22 of his submission. We think you should strike the
46 section of his submission with respect to marginal rates,
47 with respect to capital budget exclusion and with respect to
48 industrial contracts. In all three of those sections he is
49 taking a position with respect to matters that are before the
50 Board. He agreed before we broke that he would not do
51 that. It is our submission that it is inappropriate for him to
52 take a position and even though we actually like his

53 position with respect to whether or not the industrial,
54 whether or not Hydro should be treated as an investor-
55 owned utility, and there's a possibility that that could be
56 construed as a matter of law for interpretation by the Board,
57 we have always taken the position that it is inappropriate
58 for Board counsel to intervene on the issues and we
59 reiterate that position.

60 In conclusion, we believe that the industrial
61 customers are entitled to their costs. Newfoundland Power
62 said that they shouldn't be required to contribute to the
63 costs, I guess, of the enemy. Well, neither should we. And
64 the result, when Newfoundland Power sets its rates, it
65 includes in its revenue requirement its anticipated costs of
66 participating in regulatory hearings, and therefore it
67 recovers from its customers its costs of participating in
68 regulatory hearings. Hydro recovers its costs, the
69 Consumer Advocate recovers its costs. The only
70 participant in this hearing who is not represented by the
71 Consumer Advocate is the industrial customers, the only
72 one, so why should the industrial customers who have
73 such a large stake in the outcome of the hearing be
74 excluded from recovery of their costs?

75 As we've stated in our submission, we believe that
76 Hydro can save a significant amount of its revenue
77 requirement. Ms. Greene opened by indicating that in spite
78 of changes in the cost of living over the last ten years,
79 Hydro's customers have not had to deal with a rate
80 increase. Well, the converse of that argument is that if
81 Hydro has not had to come back to the Board for a rate
82 increase in ten years, perhaps its rates in 1992 were set too
83 high.

84 We urge the Board to restrict costs where
85 reasonable, to look at cost of service principles carefully
86 and analyze the substantial benefit and promote the status
87 quo with respect to assignment of rural assets, to set
88 ground rules and reasonable restrictions with respect to
89 capital projects, to influence Hydro to only incur prudent
90 reasonable rate design and to award the industrial
91 customers their costs. Thank you.

92 MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms.
93 Henley Andrews.

94 MS. GREENE, Q.C.: You have ten more seconds, Janet.

95 MR. NOSEWORTHY, CHAIRMAN: Timing is impeccable.
96 Thank you very much. We'll move now to Mr. Lockyer
97 who's here to make a presentation on behalf of CFB Goose
98 Bay. Welcome, Mr. Lockyer.

99 MR. LOCKYER: Thank you, Mr. Chairman, Commissioners.
100 The thrust of our argument is that the proposed rate for
101 secondary energy is unreasonable and unjustly
102 discriminatory and therefore contrary to Section 3 of *The*

1 *Electrical Power Control Act 1994*. This argument is set
2 out in our written submission and it's not my intention to
3 go over each and every point that's made in that
4 submission. I will, however, refer to some of those points,
5 particularly in responding to submissions made by other
6 counsel this morning.

7 Hydro stated this morning that in the case of
8 secondary power, the revenue to cost ratio is not the best
9 factor to look at. It suggests that the value of the power to
10 the customer should be considered. Firstly, I cannot point
11 you to any evidentiary basis to support that statement.
12 There is on page 81 of Hydro's final submission reference
13 to the issue at 5-Wing Goose Bay and the argument refers
14 to evidence given by Mr. Hamilton, particularly at line six
15 on page 81 wherein it states, "At that time Mr. Hamilton
16 explained that the method for the pricing is based on the
17 value to CFB Goose Bay and Hydro's lost opportunity cost
18 if it sells to CFB Goose Bay."

19 There is a distinction between what the pricing is
20 actually based on and a statement as to what is the
21 appropriate measure to look at when considering the
22 pricing of the power. To bolster our submission in that
23 respect we need simply refer the Commissioners to *The*
24 *Electrical Power Control Act of 1994* itself which provides
25 in Section 3 that, "The rates to be charged, either generally
26 or under specific contracts, for the supply of power within
27 the province," and at subparagraph 2, "should be
28 established wherever practicable based upon forecast costs
29 for that supply of power for one or more years."

30 It is our position that to price energy based upon
31 the value to the customer is a very subjective approach and
32 as well is contrary to the Act. The Act indicates that it has
33 to be based upon the forecast costs. To determine the
34 value of power from one customer to another would be an
35 exceedingly difficult exercise for anyone to embark upon.

36 Thirdly, as stated in our written submission at
37 paragraph 17, the Wing could receive firm power to supply
38 its electric boilers if it chose. There's nothing to prevent it
39 from asking for firm power and in our view Hydro would
40 have a duty to provide it. As a result, one could argue that
41 the value of a secondary energy to the Wing is no more
42 than the cost of firm power. The value of it to Hydro, and
43 more particularly to those customers who are subsidized by
44 it, is significant however.

45 The evidence clearly shows an excess payment, as
46 it's termed in the submission of Newfoundland Power, of
47 \$3.75 million from 5-Wing Goose Bay. The application of
48 Newfoundland and Labrador Hydro has the sum allocated
49 to subsidize users on the Labrador interconnected grid.
50 Newfoundland Power in its submission wants its customers
51 to get a share of this as demonstrated by its

52 recommendation on page F-7 that the excess revenue be
53 applied to reduce the rural deficit.

54 In its submission this morning, Newfoundland
55 Power has submitted that there's no evidence upon which
56 to conclude that the rate proposed to be charged to the
57 Wing for secondary energy is unjustly discriminatory.

58 (4:00 p.m.)

59 We submit that the cost of coverage compared to
60 other categories of non-firm power speaks to itself. There
61 is significant evidence before this board, the evidence of
62 Hydro's own expert, Mr. Brickhill and in particular, as
63 referred to in our submission, Exhibit 1.2, Table 1.2, Exhibit
64 1, JAB-1, sets out the various cost, revenue to cost
65 coverages.

66 And just to recap for the Commissioners, for
67 instance, IOCC non-firm energy is supplied at a revenue to
68 cost coverage of 1.00. The industrial non-firm energy is
69 supplied at a revenue to cost coverage of 2.43 times. The
70 secondary energy to be supplied to 5-Wing Goose Bay has
71 a revenue to cost coverage of 21.61 times. Again on the
72 face of that, that is clear evidence of a discrimination
73 visited upon 5-Wing Goose Bay. The cost, the revenue to
74 cost coverage in respect of 5-Wing is clearly out of
75 proportion to anything else that is proposed for secondary
76 or interruptible or non-firm power.

77 Further evidence of this can be seen from the fact
78 that 5-Wing will pay \$5.5 million annually for both its firm
79 and secondary energy. This comes from the evidence of
80 Colonel McCabe given before the Board in Goose Bay. It
81 is then calculated, particularly in Newfoundland Power's
82 brief, that the excess payment is \$3.75 million. This is an
83 incredible number when compared with a total cost of \$5.5
84 million. Of the payments of \$5.5 million made by 5-Wing
85 Goose Bay on an annual basis, \$3.75 million of that is
86 excess to the requirement to cover the cost.

87 In its submission this morning, Newfoundland
88 Power also stated that the rates were negotiated on the
89 basis of an avoided cost basis, and again that comes from
90 the evidence of Mr. Hamilton. A number of points on that
91 statement, firstly, that is obviously historical. There is no
92 opportunity at present to negotiate the rate. These rates
93 were negotiated in the past. That is irrelevant to the
94 present proceeding. If negotiations were to be held today,
95 they may not result in a rate as has been proposed by
96 Newfoundland Hydro or indeed as has been negotiated in
97 the past. Hydro has decided to propose a rate which
98 includes a floor. Now it's a submission of 5-Wing that the
99 floor was never included before. You'll see this in the
100 evidence of Colonel McCabe, and this is making reference
101 to the Part B of the charge under the proposed rate for
102 secondary energy.

1 This is not a negotiation and the Wing is
2 presenting its views before the Board as it is entitled to do
3 and anything that may be agreed to in negotiations held
4 years ago does not preclude or estop the Wing from raising
5 it now.

6 We have included in our brief the importance of
7 the Wing and its operations to the Lake Melville area, and
8 I think this is very important for the Commissioners to keep
9 in mind when they're looking at the reasonableness of the
10 rate that is being proposed. We do agree with the
11 submissions of the industrial customers with respect to the
12 fact that the Board is not restricted by the fact that Hydro
13 has submitted this application as a package. Clearly the
14 Board must look at each and every rate that has been
15 proposed by Hydro in its application and decide whether
16 those rates in total, but also on a singular basis, a
17 standalone basis, are reasonable and not unjustly
18 discriminatory.

19 The industrial customers as well have spoken of
20 the Interruptible B power provided to Abitibi at
21 Stephenville and this, we submit, is a further example of
22 where interruptible power can be treated differently
23 obviously than the firm power and that the approach taken
24 with Abitibi at Stephenville could well be instructive as well
25 in dealing with the secondary energy provided to the Wing
26 at Goose Bay.

27 Finally, I want to refer the Commissioners as well
28 to a couple of other items in our submission, firstly the
29 differential rates in Labrador West, and to reiterate that the
30 Wing supports the view presented by the Town of Happy
31 Valley-Goose Bay that ultimately there should be no
32 difference in the rates between Labrador West and the
33 Happy Valley-Goose Bay area.

34 Lastly I want to spend a few moments talking
35 about the requirement of the Board to look at these rates
36 and make changes in the rates if it is deemed that the rates
37 as proposed are contrary to the policy as set out in *The*
38 *Electrical Power Control Act*. It is our view that *The*
39 *Electrical Power Control Act* and *The Public Utilities Act*
40 must be read together, and by doing so results in a
41 mandatory statement for the Board in this application to act
42 to change rates where you are of the view that the rate is
43 unreasonable or unjustly discriminatory. While the
44 provisions of *The Public Utilities Act* appear to be
45 permissive in its language, the language of *The Electrical*
46 *Power Control Act*, particularly Section 4, is mandatory,
47 and that section provides in carrying out its duties and
48 exercising its powers under this act or under *The Public*
49 *Utilities Act*, the Public Utilities Board shall implement the
50 power policy declared in Section 3, and in doing so shall
51 apply tests which are consistent with generally accepted
52 sound public utility practice, and to reiterate our position,

53 Section 3 of *The Electrical Power Control Act* provides
54 that the rates charged shall not be unreasonable and shall
55 not be unjustly discriminatory. Furthermore, the rates must
56 be based upon a forecast of costs, not upon a subjective
57 consideration or determination of the value of power to the
58 client, to the customer.

59 In summary, Mr. Chairman and Commissioners, it
60 is our view that 5-Wing Goose Bay is paying more than its
61 fair share of the cost of the power that it consumes. It is
62 subsidizing other users to an extent much greater than
63 other users in the Labrador interconnected grid and that
64 this, on the face of it, is clearly unreasonable, unjust and
65 discriminatory, and we ask the Board to reduce the rate to
66 a reasonable level. Thank you.

67 MR. NOSEWORTHY, CHAIRMAN: Thank you very much,
68 Mr. Lockyer. Does anybody have any questions? Thank
69 you. That concludes our schedule for today and we will
70 reconvene tomorrow morning at 9:30. Thank you.

71 (adjourned to January 29, 2002)