

1 MR. NOSEWORTHY, CHAIRMAN: Good morning
2 everybody. I hope everybody is reasonably comfortable in
3 their surroundings here this morning. Some of us will likely
4 be here for a long time so it's good to start out with some
5 level of comfort, in any event, looking forward to the next
6 few weeks. I'd like to welcome indeed everybody in
7 attendance here this morning for the beginning of this
8 public hearing. We do have an agenda, I suppose, for
9 everybody's information, just to start out this morning. My
10 name, first of all, is Robert Noseworthy, and I'm Chair and
11 CEO of the Public Utilities Board and I guess for the
12 purposes of this hearing I'm serving as the panel, as Chair
13 of the panel delegated with the responsibility to hear this
14 application.

15 The agenda we will be following this morning, I
16 will be making a brief opening statement or some opening
17 remarks. I will then ask the Board counsel to report on
18 procedures and provide a procedural report. I understand
19 as well there's been agreement among counsels for an
20 opening statement by counsel for the Applicant and also
21 the registered intervenors and following that we will indeed
22 commence Hydro's case and the calling of the first witness.

23 I'll go directly to my opening remarks, if you will.
24 To all participants, including the Applicant, registered
25 intervenors, their counsels and support staff, along with
26 public organizations or individuals and the media, I extend
27 to each of you a sincere welcome and I look forward to a
28 productive and fair public hearing.

29 My colleagues joining me on the panel this
30 morning, to my left, Commissioner Darlene Whalen, who's
31 Vice-Chair of the Public Utilities Board. On my far right is
32 Commissioner Don Powell who is a businessman from the
33 Stephenville area. On my immediate right is Commissioner
34 Fred Saunders who is a retired former businessman and
35 now resides in St. John's. I'd also like to introduce our
36 Board counsel to my left, Mark Kennedy, and the Board's
37 secretary, Cheryl Blundon.

38 This public hearing by the Public Utilities Board
39 is for the purpose of deciding on the application of
40 Newfoundland and Labrador Hydro for a general rate
41 review. Pursuant to *The Public Utilities Act* Hydro are
42 seeking approval to increase rates to be charged for the
43 supply of electricity to its retail customer, Newfoundland
44 Power, and its rural customers. In addition, the application
45 is requesting approval of rates as well as terms and
46 conditions of contracts governing the supply of electricity
47 to Hydro's industrial customers. Finally in this application
48 Hydro are also seeking approval of their 2002 capital
49 budget.

50 I would ask at this point the persons indeed
51 seated at the tables representing the Applicant and each of

52 the registered intervenors to please introduce yourself and
53 indicate in what capacity you are participating in the
54 hearing, if you would, and each counsel I would affirm
55 (phonetic) will be given the opportunity to make some
56 opening remarks, but this really just for introduction
57 purposes for the benefit of us all, please. I'll start with
58 Hydro.

59 MS. GREENE, Q.C.: Good morning, Mr. Chairman,
60 Commissioners. My name is Maureen Greene. I am
61 counsel for Newfoundland and Labrador Hydro, the
62 Applicant, and with me throughout the hearing will be
63 Geoff Young.

64 MR. NOSEWORTHY, CHAIRMAN: Thank you.
65 Newfoundland Power.

66 MS. BUTLER, Q.C.: Mr. Chairman and Commissioners,
67 Gillian Butler and Peter Alteen will appear throughout this
68 process on behalf of Newfoundland Power.

69 MR. NOSEWORTHY, CHAIRMAN: Thank you. Industrial
70 customers.

71 MR. HUTCHINGS: Thank you, Mr. Chair. My name is
72 Joseph Hutchings and Janet Henley Andrews is with me.
73 We appear as counsel for the industrial customers. Seated
74 to my left is Mr. Mel Dean (phonetic), who is Coordinator
75 of Special Projects with Abitibi Consolidated in
76 Stephenville and will be assisting us but obviously not
77 acting as counsel throughout the hearing. Also present
78 further back in the room is Meg Gillies who is associated
79 with Mrs. Andrews' firm and who will be with me from time
80 to time as well.

81 MR. NOSEWORTHY, CHAIRMAN: Welcome back, Ms.
82 Henley Andrews.

83 MS. HENLEY ANDREWS: Thank you.

84 MR. NOSEWORTHY, CHAIRMAN: The consumer
85 advocate, please?

86 MR. BROWNE, Q.C.: My name is Dennis Browne,
87 Consumer Advocate appointed by the Lieutenant Governor
88 in Council to represent domestic and general service
89 customers. I have with me Stephen Fitzgerald, who is
90 appointed counsel to the Consumer Advocate.

91 MR. NOSEWORTHY, CHAIRMAN: Thank you. Labrador
92 City?

93 MR. HEARN, Q.C.: Edward Hearn, counsel for the town of
94 Labrador City, Mr. Chairman.

95 MR. NOSEWORTHY, CHAIRMAN: Thank you. The
96 remaining registered intervenor is Happy Valley-Goose
97 Bay, and I understand Dennis Peck, who is their Economic
98 Development Officer, will be representing the town of
99 Happy Valley-Goose Bay and he is not here this morning.

1 For those of you who are in attendance who may
2 not be familiar with the role of the Public Utilities Board and
3 the process we will follow in hearing this application, with
4 the indulgence of counsels, counsel for the parties, I will
5 take a brief moment to review each of these.

6 The Board derives its authority to conduct this
7 hearing from provincial statutes and legislation, primarily
8 *The Public Utilities Act* and *The Electric (sic) Power*
9 *Control Act*. The Board has an obligation under this
10 legislation to regulate electric utilities operating in this
11 province and this includes Newfoundland and Labrador
12 Hydro. The panel, which I just introduced, has been seized
13 with the application and in accordance with our legislative
14 responsibilities we have a duty to hear the evidence
15 presented by the Applicant, Hydro, and other interested
16 parties and at the end of the process render a fair and
17 equitable decision. The statutes require the Board to make
18 rate decisions that are reasonable and just and not
19 discriminatory. The legislation requires that the Utility be
20 allowed to earn a just and reasonable financial return. The
21 legislation also dictates that power be delivered to
22 customers in the province at the lowest possible cost while
23 ensuring safe and reliable service. In fulfilling its statutory
24 responsibilities, the Board must protect the interests of all
25 parties including producers, retailers and consumers of
26 electricity. In doing this it must also be sensitive and strive
27 to balance the interests of each class of consumer, whether
28 they be households, business, industry, both small and
29 larger users of electricity.

30 Having described some of the reasons why we are
31 here this morning, I would like to spend another brief
32 moment explaining the process, what has occurred to this
33 point and what we can expect in the weeks ahead. The
34 application was submitted on May the 31st of this year
35 following which a notice of public hearing was advertised
36 throughout the province. A pre-hearing conference was
37 held on July the 5th at which time registered intervenors
38 were identified and various schedules, times and dates,
39 order of witnesses and other procedural matters were set.
40 Following the pre-hearing conference, two motions' days
41 were held on July the 18th and August the 29th to hear
42 specific motions presented by the parties and to fine-tune
43 the rules and procedures governing the conduct of this
44 hearing. These procedures are now outlined in Orders No.
45 PU-7, 18 and 22, 2001/2002, and these have been distributed
46 to all parties.

47 In addition, the preliminary process allows for
48 questions to be asked by one party of another and
49 responses to be prepared and circulated among all parties.
50 Also pre-filed evidence of any expert witness engaged by
51 the parties has now been received and distributed. To give
52 you some idea of the volume of material pre-filed to date, it

53 comprises some 42 rather large binders which can be
54 indeed seen behind me.

55 We have reached this stage here this morning with
56 hopefully most of the preliminary and procedural work out
57 of the way, such that we may embark upon the next more
58 rigorous phase of the hearing. In this phase each of the
59 parties will have the opportunity to question company
60 witnesses and their experts and in turn present the views of
61 their own experts which will also be subject to cross-
62 examination by the other parties. The process involves one
63 of examining, evaluating and questioning the large quantity
64 of information and testimony presented. The purpose is to
65 ensure that all the necessary evidence required to reach a
66 determination on rates and other matters contained in the
67 application are placed before the panel. The process will
68 enable the panel to assess all the issues covered by the
69 application and render a fair and equitable decision that will
70 serve to balance in the best manner possible the interests
71 of all stakeholders.

72 This application affects every consumer of
73 electricity in the province and the rates each will pay for
74 that electricity in future. As this hearing unfolds, public
75 interest in this application will likely be high. It is with this
76 in mind that the panel has scheduled, beginning in mid-
77 October, a number of public participation days to be held
78 throughout the province. These public participation days
79 are designed to provide the opportunity for individuals and
80 organizations to make their views known directly to the
81 Board on matters contained in the application. These
82 public participation days are scheduled for St. Anthony,
83 Labrador City, Wabush, Happy Valley-Goose Bay,
84 Stephenville, Grand Falls-Windsor, and St. John's. I will be
85 specifying the times and locations for this part of the public
86 hearing just a little later, but I would at this point ask
87 indeed any media that are here to please report on this
88 aspect of the hearing in order that we may encourage the
89 highest level of public input possible from municipal
90 councils, economic development associations, chambers of
91 commerce and others.

92 Another challenge in organizing the hearing is the
93 sheer volume of information and evidence which must be
94 appropriately filed and available for ready access
95 throughout the proceeding. I think you only need look
96 around the room to get some idea of the information
97 management challenge that's presented. The Board has
98 established procedures and protocols for the filing of
99 electronic copies of original hard copy documentation, and
100 while paper copies remain the official record for the Board,
101 I am pleased to report that much of the information you see
102 behind me, including the application, pre-filed evidence,
103 public notices, procedural orders, etc., are available for
104 public viewing on the Board's web site. In addition, we are

1 electronically equipped to call up evidence and other
2 information which should avoid awkward delays and
3 (unintelligible) shuffling of paper during the proceedings.
4 Mr. Terry O'Reilly, an employee of Hydro, will be assisting
5 us in this aspect of the technology and I thank him for
6 agreeing to this assignment. These electronic
7 improvements should enhance public access and
8 contribute to the overall efficiency of the hearing and I also
9 want to thank each of the parties for their cooperation in
10 making this happen.

11 This application represents Hydro's first rate
12 application before the Public Utilities Board. The initial
13 establishment of appropriate regulatory base, the volume
14 of evidence to be heard, and the myriad of social, financial
15 and economic issues which will arise promises to make this
16 one of the most challenging and complex applications ever
17 before the Board. It is important for the benefit of all
18 parties to keep issues focused and provide as clear and
19 clean a path as possible in outlining evidence and
20 formulating arguments. My expectations for this hearing
21 are that the evidence will be presented in a crisp and
22 succinct fashion, questions by parties and responses by
23 witnesses will be direct and transparent and in a language
24 simple and concise and free to the extent possible of
25 technical detail.

26 Given the length of this hearing and at times its
27 intensity, I am sure that nerves will become frayed on
28 occasion, both yours and mine. During these times I would
29 ask that we all maintain decorum based on respect and
30 advocacy as opposed to personality. I am assured by
31 Board counsel that we have experienced litigators in the
32 room and this should not happen. Because of this
33 experience also, I am also advised that we will likely benefit
34 from a complete and thorough presentation and analysis of
35 the evidence and I look forward to this.

36 These are the conclusion of some of my general
37 remarks and there are a number of other specific items I
38 would now like to cover. These proceedings are being
39 recorded under the supervision of the Board's secretary,
40 Ms. Blundon, and will be transcribed overnight. These will
41 be e-mailed to the parties immediately on completion with
42 a paper copy available by the commencement of the
43 hearing on the following day. In this way we will hopefully
44 maintain continuity and have an up-to-date and current
45 record of the proceedings as they unfold. I am requested
46 by the Board's secretary as well, she has a list of e-mail
47 addresses, and if you could at least confirm for us your e-
48 mail address against that list we would appreciate that.

49 The procedural rules and regulations we are
50 following for this hearing are set out in our regulations
51 identified, Newfoundland Regulations 39 of 96, and as
52 referenced earlier, more specifically contained in order Nos.

53 PU-7, 18 and 22. These orders outline the registered
54 intervenors, schedule of dates, order of witnesses,
55 procedures for the presentation of evidence and cross-
56 examination, protocol and other procedures for this
57 hearing. These orders are available on the Board's web site
58 or may be viewed by contacting the Board's secretary, Ms.
59 Blundon. While it is not my intention to review each of
60 these, I would like to comment particularly on the schedule.

61 We have assessed the material to be covered in
62 consultation with counsel for the parties. We have set for
63 ourselves what is an ambitious, what may appear to be a
64 lengthy schedule. While this is my first public hearing, I
65 am advised by more experienced colleagues that we indeed
66 will have to keep things focused and on track to achieve
67 even this schedule. Beginning here today we will be sitting
68 each week day, virtually uninterrupted, through to
69 December the 7th. Notable exceptions are Thanksgiving
70 Day on October the 8th, Memorial Day, November the 11th,
71 and two days, October the 24th and November the 23rd,
72 which we have set aside as non-hearing days. These are
73 necessary to hold our scheduled monthly meetings of the
74 Board of Commissioners to deal with other matters affecting
75 the PUB. I would note for everybody's benefit that
76 December the 1st is indeed listed on the order schedule.
77 This is a Saturday and it's an error. December the 1st will
78 be deleted from the schedule and the order amended
79 accordingly.

80 I would like to draw everyone's attention to the
81 public participation days which I noted earlier as being
82 particularly important to this hearing. The dates, times and
83 locations for these public participation days are as follows:
84 October the 15th at 9:30 we will be at St. Anthony in the
85 Vinland Hotel, October the 16th and 17th we will be in
86 Wabush at the Wabush Hotel, October the 18th and 19th
87 we will be in Goose Bay at the Labrador Inn, October the
88 22nd we will be in Stephenville at Holiday Inn, October the
89 23rd we will be in Grand Falls at the Mount Peyton, and
90 October the 25th and 26th we will be here in St. John's in
91 this room.

92 Information on these public participation days
93 have been advertised in newspapers throughout the
94 province and can be seen on the Board's web site once
95 again. Arrangements to make oral presentations before the
96 Board during these public participation sitting days can be
97 done again by contacting the Board's secretary. The daily
98 sitting hours will be 9:30 a.m. to 12:30 p.m. and from 2 to 4
99 p.m. Breaks of 15-minute duration will be at or near 11 a.m.
100 and 3:15 p.m. I understand from the Board's secretary that
101 adherence to the 15-minute time limit has been a problem in
102 the past, and given the large number of persons
103 participating in the hearing and what will present a
104 difficulty for the Board's secretary to round everybody up,

1 I would ask you to keep to the 15 minutes allotted, please.

2 Board hearings are not court trials, however,
3 evidence is given under oath and the procedures
4 governing conduct are somewhat similar to a court. The
5 Board's main goal is to get the facts on the record in a way
6 that is convenient to the parties and in the public interest.
7 Persons addressing the panel may, for the benefit of
8 transcription services, refer to Commissioners Powell,
9 Saunders and Whalen in that fashion, and myself as simply
10 the Chair. It is not necessary for lawyers or witnesses to
11 stand while questioning or giving evidence. Certainly we
12 would ask the witnesses to take their designated seat to my
13 right unless making a presentation or referring to a display
14 and counsel may wish to sit or stand during questioning if
15 indeed that's your preference.

16 The binders you see in front of me here represent
17 the official unblemished, if you will, version of the
18 documents for the hearing and these will be used for
19 reference purposes as needed.

20 I would ask that the parties throughout these
21 proceedings adhere to the procedures for pre-filing
22 additional evidence and ensure requisite notice and copies
23 of documentation and exhibits are provided to all parties.
24 We would like to avoid surprises and allow parties to
25 adequately prepare for their questioning of witnesses.

26 I would ask the Board counsel in a moment to deal
27 with matters of reading into the record appropriate notices
28 and other preliminary items, along with information on how
29 evidence will be handled for purposes of the record.

30 In summary, I want to commend all parties for the
31 exhaustive amount of work undertaken in preparing for this
32 hearing and while I am sure there will be some irritants at
33 times throughout the remainder of the process, I am
34 hopeful we can continue through this phase of the hearing
35 in a productive, efficient and cooperative manner, at the
36 same time allowing each party to aggressively represent
37 their respective interests. I believe the extensive planning
38 and procedural effort in which we have all participated to
39 this point has positioned us to go forward expeditiously.
40 Given the time and money expended to date, I would not
41 want to see these efforts wasted. I would like to see
42 unnecessary disruptions kept to a minimum that indeed
43 may unduly add to the schedule and resulting costs of this
44 hearing. I am sure the various ratepayers of the province
45 will wish us to all get on with our jobs in the most efficient
46 and cost-effective manner possible and I think we should
47 all be cognizant of this throughout the weeks ahead and I
48 ask for your cooperation in applying this rather
49 fundamental premise.

50 That's the end of my opening remarks and I would
51 now like to ask Mr. Kennedy, the Board counsel, to

52 address preliminary matters of record. Thank you.

53 MR. KENNEDY: Thank you, Chair, Commissioners. First
54 I'll read into the record the official recitals for the
55 application. It's in the matter of *The Electrical Power*
56 *Control Act 1994* and *The Public Utilities Act* and their
57 subordinate regulations, and in the matter of an application
58 by Newfoundland and Labrador Hydro for approvals of: (1)
59 under Section 70 of the Act, changes in the rates to be
60 charged for the supply of power and energy to its retail
61 customer, Newfoundland Power, its rural customers and its
62 industrial customers; (2) under Section 71 of the Act, its
63 rules and regulations applicable to the supply of electricity
64 to its rural customers; (3) under Section 71 of the Act, the
65 contract setting out the terms and conditions applicable to
66 the supply of electricity to its industrial customers; and (4)
67 under Section 41 of the Act its 2002 capital budget.

68 I can confirm, Chair and Commissioners, that the
69 appropriate notices have been published in a province-
70 wide circulation, including *The Evening Telegram*, two
71 insertions, dated September the 8th and 12th, *The Western*
72 *Star*, two insertions, the same date, *The Herald*, one
73 insertion in the week of September the 17th to the 23rd, and
74 the following Robinson and Blackmore papers, two
75 insertions commencing on September the 4th, *The Express*,
76 *The Compass*, *The Packet (phonetic)*, *The Southern*
77 *Gazette*, *The Beacon*, *The Pilot*, *The Advertiser*, *The*
78 *Nor'wester*, *The Coaster Harbour*, *The Humber Log*, *The*
79 *Georgian*, *The Gulf News*, *The Charter*, *The Aurora*, *The*
80 *Labradorian*, *The Northern Pen*.

81 There's also been, in addition to the official
82 intervenors, representations made by individuals and
83 parties requesting the ability to make oral presentations to
84 the panel and a full list has already been published by the
85 Board pursuant to its procedural orders, so I will read just
86 the names and the titles and affiliations of those individuals
87 and leave out the details of phone numbers and the like.
88 Scott Hurley, Mayor of the Town of Stephenville; Fred
89 Powell, President of the Bay St. George Chamber of
90 Commerce; Don Power, the President of Local 1093 of the
91 Communications Energy and Paper Workers Union of
92 Canada; Yvonne Jones, MHA for Cartwright/L'Anse-au-
93 Clair; Mr. Harry Shiwak, Town Manager, Town of Rigolet;
94 Mr. David Dyson, Town Manager, Makkovik Town
95 Council; Ms. Margaret Fox, Mayor, Town Council of Nain;
96 Ms. Florence Harnett, Town Clerk, Town of Wabush; Mr.
97 Glen Sheppard, Mayor, Town Council of Postville; Mr.
98 Dean Coombs, Mayor, Town Council of Hopedale; Mr.
99 Tom Hutchings, Executive Director, Long Range Regional
100 Economic Development Board; Mr. Aaron Condon, the
101 Town of Labrador City; Mr. George Kean, (phonetic) the
102 President of the United Steelworkers of America, Local
103 5795; and Mr. Randy Collins, MHA for Labrador West.

1 And that, I believe, takes care of the procedural
2 matters, Mr. Chair, and in the (unintelligible) opinion of
3 Board counsel that the Hydro application is properly before
4 the Board.

5 MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr.
6 Kennedy. We should be in a position now to proceed to
7 the opening statements, and I would ask the Applicant,
8 Hydro, I assume Ms. Greene, to begin the opening
9 statement for Hydro, please.

10 MR. FITZGERALD: Mr. Chairman, before we commence,
11 we have filed a notice of motion following Board Order PU-
12 22, which we received five o'clock on Friday. I didn't hear
13 in your opening comments how the Board intends to deal
14 with that motion or when. To, you know, follow your
15 direction this morning regarding keeping things
16 expeditious, although the motion is a formal motion, you
17 will note that it is really a request for clarification of PU-22
18 and it may be appropriate now to clarify, at least in our
19 minds, and perhaps other counsel may have something to
20 say on that, as to just exactly which set of rules we are
21 being governed by. If we could speak to that now, that
22 would be appreciated.

23 MR. NOSEWORTHY, CHAIRMAN: We've just received
24 the motion at 8:45, I think, this morning and to be quite
25 frank with you, we haven't had an opportunity to convene
26 to deal with that yet. We will do that. I think the result is
27 the same in terms of the order that we would have issued
28 on Friday, provides for intervenors to provide direct or to
29 provide redirect, I should say, on questions where they are
30 leading with direct evidence. I don't think that's at issue.
31 It's a matter of clarifying the regulations versus the
32 procedural order and I am not anticipating that that would
33 be an issue until later on in the week and certainly when the
34 Board convenes we will deal with that over the next couple
35 of days.

36 MR. FITZGERALD: With respect, Mr. Chair, the difficulty
37 is that the issue is going to raise itself sooner than that.
38 Once we get through the opening statements, I'm assuming
39 that Mr. Wells will be taking the stand, and it is at that
40 point when this issue will become glaringly obvious in our
41 estimation. Currently we are being governed by Appendix
42 A, Item 4, in PU No. 7, which is a September 7th order of the
43 Board, it's very clear, and nowhere in this order does
44 Hydro, and I'm not arguing Hydro's case right now,
45 anticipating our witnesses, but nowhere in PU No. 7 does
46 Hydro have the opportunity to redirect Mr. Wells, and in
47 fact it may be in our interest if they do decide to redirect
48 Mr. Wells to object. There may ... and we would think that
49 that would be a fair thing to do in light of the order.

50 All we are seeking really is again a clarification.
51 We are very aware that Section 18 of the regulations

52 entitles a party to redirect examination and in fact we're also
53 aware that this is actually the past practice of the Board.
54 That's all granted. What isn't granted and what isn't
55 obvious to us is a black and white issue, there is no black
56 ink on Appendix A, Item 4, authorizing or allowing or
57 granting any party the time honoured right to redirect
58 examination. It's merely a stroke of a pen, it's not a big deal,
59 however, it can be a big deal if in fact we don't want Mr.
60 Wells to be redirected by Hydro. It would be within our
61 right then to object. Again, not saying that that's going to
62 happen, but certainly that this is a procedural problem that
63 we perceive, and again it would be easily rectified by a
64 small amendment to Appendix A, Item 4, in PU No. 7.

65 Again, the timeliness of it, we did file the
66 application at 8:45 this morning, however, we only got the
67 Board Order at five o'clock on Friday, so we really didn't
68 have any opportunity to address this earlier, and it is our
69 submission that it is an important point.

70 MR. NOSEWORTHY, CHAIRMAN: I can only reiterate,
71 Mr. Fitzgerald, that we have not had as a panel an
72 opportunity to discuss the motion and we will certainly
73 deal with it before it becomes an issue for you.

74 MR. FITZGERALD: I understand that, Mr. Chairman. I
75 guess with all due respect, as I've indicated, as soon as Mr.
76 Wells is called, then we've crossed the Rubicon then, it's
77 too late then to amend things. We have to have a clear
78 procedural route, framework now. Otherwise the evidence
79 ... if one party has the right to redirect or doesn't have the
80 right to redirect at this point, and later it's determined that
81 parties do, I would suggest that would be a fundamental
82 flaw in the evidence. If ... I don't know if other counsel has
83 any ... in fact, all counsel had agreed to a very small, and we
84 do with unanimous consent, to our application on Friday,
85 and really it's kind of a bit of an obvious point. There was
86 no argument against what we were suggesting and we
87 believe it may have arisen out of error, that PU No. 7
88 doesn't give the right to redirect. Mr. Chairman, if in fact
89 you do, the Board does proceed without considering our
90 motion, well we would like to put on the record that we
91 object to embarking upon the examination of any
92 witnesses.

93 MR. NOSEWORTHY, CHAIRMAN: I don't think that will
94 occur. We can either break now and I can deal with my
95 colleagues now. I don't see the utility in that, quite frankly.
96 We have opening statements from all parties, which is
97 likely to consume a period of time in any event before Mr.
98 Wells is called. We will be having a break and I'll have the
99 opportunity to at least discuss with my colleagues, which
100 I haven't heretofore, the motion.

101 MR. FITZGERALD: Thank you, Mr. Chairman.

102 MR. NOSEWORTHY, CHAIRMAN: Okay, thank you.

1 We'll proceed now with Ms. Greene, please.

2 MS. GREENE, Q.C.: Thank you, Mr. Chair, Commissioners.
3 As the Chair mentioned in his opening comments, Hydro
4 filed this application on May 31st of this year requesting
5 approval from the Board for increases in the rates charged
6 its three main customer groups, Newfoundland Power,
7 industrial customers and rural customers.

8 The base rate now charged Newfoundland Power
9 has not changed since 1990. Hydro is proposing to
10 increase this rate as of January 1, 2002, by 6.7 percent,
11 which at Newfoundland Power's end (phonetic) customer
12 level will be approximately 3.7 percent after 12 years.

13 For industrial customers Hydro is proposing an
14 increase of 10.4 percent. These customers have had base
15 rate changes, both increases and decreases, in the past 10
16 years.

17 With respect to rural customers, there are three
18 main groups, island interconnected customers, isolated
19 customers, both on the island and in Labrador, and
20 Labrador interconnected customers. With respect to the
21 first two customer groups, Hydro is proposing generally a
22 continuation of the existing policies for the island
23 interconnected and the isolated rural customers. Currently
24 island interconnected customers pay the same rates as
25 charged by Newfoundland Power to its customers, as do
26 isolated rural customers for the first 700 kilowatt hours per
27 month of consumption. For consumption above 700
28 kilowatt hours per month, isolated rural, for isolated rural
29 customers, Hydro is proposing a continuation of the
30 existing policy, the rates for consumption above this lifeline
31 block, as we refer to is, be increased by the average
32 percentage increase in Newfoundland Power's rates.

33 Hydro is further proposing that the preferential
34 rates paid by some customers in the isolated areas be
35 phased out over time but not commencing at this hearing,
36 with the exception of Government departments and
37 agencies where the phase-out will commence following this
38 hearing if approved by the Board and as proposed by
39 Hydro.

40 Turning now to the Labrador interconnected
41 customers, I would point out that customers served from
42 this interconnected system now pay different rates. There
43 are three main areas served from this grid, Lab City,
44 Wabush and Happy Valley-Goose Bay, and all pay
45 different, and all customers pay different rates in those
46 three areas. Hydro is proposing as a principle that all
47 customers served from the Labrador interconnected system
48 be subject to a common rate classification system with
49 uniform rates and to start the implementation of that
50 following this hearing if that proposal is accepted by the
51 Board.

52 I would like to turn now to the main issues that are
53 before the Board at this hearing. There are quite a number
54 of significant issues to be addressed by all the parties and
55 by the Board at this hearing. I have categorized them into
56 three very broad categories for the purpose of these
57 opening comments.

58 The first is legislative change, those that arise
59 from legislative amendments, the second broad category
60 would relate to Hydro's cost and its revenue requirements,
61 and the third I have categorized as rate policy or rate
62 design issues.

63 Turning to the first broad category of legislative
64 change, those issues that arise as a result of amendments
65 passed to the relevant legislations since Hydro's last rate
66 hearing. As I mentioned earlier, this is Hydro's first general
67 rate hearing since 1992. It is also Hydro's first since
68 legislative amendments were passed in 1996 to make Hydro
69 a fully-regulated utility under *The Public Utilities Act*.
70 There are a number of issues which must be considered for
71 the first time at this hearing in light of these amendments.

72 Here I refer to such issues as the determination of
73 Hydro's rate base, the appropriate return on that rate base,
74 the appropriate capital structure for Hydro and the
75 appropriate return on equity for Hydro. These questions
76 all relate to Hydro's financial structure and financial
77 position and they all impact the rates charged to Hydro's
78 customers.

79 Another issue to be addressed due to legislative
80 change is the reallocation to other customers of the portion
81 of the rural subsidy previously paid by industrial
82 customers and which they now no longer pay since 1999.

83 The second broad category of issues that I have
84 referred to are those of costs and Hydro's revenue
85 requirement. This category deals with all of those issues
86 relating to what our costs are and whether they have been
87 reasonable and prudent and what items are included in
88 Hydro's revenue requirement.

89 Hydro has submitted evidence on all of its costs
90 that are included in the proposed rates for 2002 and in fact
91 we have submitted evidence on how all of these costs have
92 changed in the last ten years. One of the biggest increases
93 in costs that is significant for this hearing is the dramatic
94 increase in the cost of No. 6 fuel which Hydro burns at the
95 Holyrood generating plant. The Holyrood plant now
96 supplies approximately 30 percent of the production
97 requirements for the Island of Newfoundland. The current
98 base rates were set using \$12.50 a barrel and these rates
99 were set in 1992. Prices have varied significantly since
100 then, particularly in the last 12 to 18 months. Hydro is
101 proposing that the price to be used for No. 6 fuel in setting
102 base prices be increased (sic) from \$12.50 a barrel to \$20 a

1 barrel and that the Rate Stabilization Plan continue to
2 operate to cushion the impact of the difference between the
3 actual price paid and the \$20 a barrel to be in the base rate
4 if Hydro's proposal is accepted. Undoubtedly the price of
5 Bunker, or No. 6 fuel, as well as the operation of the Rate
6 Stabilization Plan, will be significant issues before the
7 Board.

8 The third broad category of issues relates to rate
9 policies and specific rate design issues. I have already
10 outlined the main policies that Hydro is proposing
11 concerning rural customers. Our proposal in this regard is
12 generally a continuation of the current policies for this
13 hearing with the exception of Labrador interconnected
14 customers and Government departments and agencies in
15 isolated areas.

16 There are also a number of rate design issues and
17 here I include such issues as the appropriate rate structure
18 for Newfoundland Power, the appropriateness of marginal
19 cost base rates in Newfoundland, the appropriate allocation
20 of certain assets to certain customer groups, the
21 appropriate phase-out period for preferential rates paid by
22 certain rural customers, and these are just, but just a few of
23 the many rate design issues that will be before the Board.

24 One of the significant rate design issues that has
25 been raised is the continuation of the Rate Stabilization
26 Plan. Hydro's position is that this plan has worked well for
27 its customers and that it should be continued. From a
28 financial perspective, Hydro is indifferent to the existence
29 of the Rate Stabilization Plan. Hydro must be paid for the
30 fuel when it is burnt. The issue is how customers pay for
31 it, whether they pay immediately or over time. We believe
32 that that is one of the central issues before this hearing and
33 it is clear that our position is again that the Rate
34 Stabilization Plan has worked well for customers, it has
35 achieved the principal objective for which it was designed
36 and that it should continue with the changes that have
37 been proposed by Hydro.

38 There are also other issues which do not fit neatly
39 within the three broad categories I have outlined, for
40 example, the 2002 capital budget, the appropriate time
41 period to use for hydrological purposes, industrial power
42 contracts, are but to name a few.

43 There are numerous other issues as well before the
44 Board and with respect to all of these issues, particularly
45 the significant ones that I have referred to, the Board will
46 find that there are as many different views and positions as
47 there are parties before the Board. Hydro has to date and
48 will continue to provide all information necessary for the
49 Board and for the other parties to make a full and fair
50 assessment of all of these issues.

51 To support its application, Hydro filed, as the

52 Chair has already mentioned, the application and its pre-
53 filed testimony in May. Since then we have responded to
54 over 825 information requests. When the number of parts
55 of each information request is considered, the number rises
56 to several thousand questions Hydro has responded to to
57 assist the parties in understanding the issues before the
58 Board. Undoubtedly there will be other information filed
59 during the course of this hearing, and again Hydro's role in
60 providing the information is to ensure that all of the
61 evidence is before the Board so they can make a full and
62 informed decision in light of the competing positions that
63 will be put forward before the Board.

64 At this time I'd like to indicate the witnesses that
65 Hydro will be calling in support of its application. Hydro
66 will be calling ten witnesses. There are seven internal
67 Hydro employees and three internal (*sic*) experts. The
68 internal witnesses are William Wells, President and Chief
69 Executive Officer; Dave Reid, Vice-President of
70 Transmission and Rural Operations; Rob Henderson,
71 Manager of System Operations; Hubert Budgell, Director of
72 System Planning; John Roberts, Corporate Controller;
73 Derek Osmond, Vice-President of Finance and Chief
74 Financial Officer; and Paul Hamilton, Regulatory Specialist.
75 The three external witnesses are Cathy McShane of Foster
76 Associates; Douglas Hall of RBC Dominion Securities; and
77 John Brickfill (phonetic) of Foster Associates.

78 Ms. McShane will speak to Hydro's appropriate
79 capital structure, both short-term and long-term, the
80 determination of rate base and the appropriate return on
81 rate base for Hydro. Mr. Hall will give evidence on the
82 appropriate level of debt and equity for Hydro and
83 implications of the provincial guarantee on Hydro's capital
84 structure. Mr. Brickfill (phonetic) will give evidence on
85 the 2002 cost of service study that has been filed and will
86 speak generally to the cost of service methodology.

87 Each of the seven internal Hydro witnesses will
88 speak to issues within their area of responsibility as
89 relevant to this hearing, and I will not go through the
90 outline at this time but I will as each witness comes to give
91 evidence.

92 Mr. Wells will be the first witness for Hydro. He
93 will give an overview or outline of the main points of the
94 application and speak to the significant policy type issues
95 that are relevant. Today after he adopts his pre-filed
96 evidence, Mr. Wells will have some additional comments in
97 the nature of a general overview to speak today. That
98 issue has been raised with other counsel in preparation for
99 today and I understand has been agreed to by counsel. It
100 is not new evidence in the sense of new facts, but it's
101 Hydro's opportunity to give a very brief overview of its
102 approach to the application.

1 So that concludes my opening comments for now.
2 Thank you very much.

3 MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms.
4 Greene. I'll move next to Newfoundland Power, please, for
5 your opening remarks.

6 MS. BUTLER, Q.C.: Thank you, Mr. Chairman and
7 Commissioners. As Ms. Greene has stated, in the 1996
8 amendment to *The Hydro Corporation Act* repealed the
9 provisions that had previously exempted Hydro from the
10 provisions of *The Public Utilities Act* and in doing this the
11 Government determined that Newfoundland and Labrador
12 Hydro would be a fully-regulated utility. Today therefore
13 this Board commences its first investigation into Hydro's
14 rates under the terms of *The Public Utilities Act*.
15 Remember that the last hearing into Hydro's rates under the
16 predecessor *Electrical Power Control Act* used a test year
17 of 1992, and from the public's point of view, ten years is a
18 long time. The rules in that intervening period, Mr.
19 Chairman, as you alluded to this morning in your own
20 opening statement, have changed significantly. These
21 facts suggest that this will perhaps be the longest hearing
22 in Board history.

23 This is of course an investigation into the
24 reasonableness of Hydro's proposed rate. As an intervenor
25 it is Newfoundland Power's responsibility, as other
26 intervenors, to bring forward issues, evidence and
27 recommendations to assist the Board in this investigation.
28 We will fulfill that responsibility, Mr. Chairman, in a manner
29 that is most helpful to the Board in fulfilling its duty, again
30 as outlined by you this morning, and I should say at this
31 point that I do commend the Board and its counsel for the
32 electronic improvements which are present in the room. I
33 believe since I will likely be the first to use the technology
34 for cross-examination of Mr. Wells, that it will in fact be
35 helpful to focus us all on an orderly hearing.

36 Hydro is seeking rate increases on January 1st,
37 2002, sufficient to recover \$18 million from its various
38 customers. Hydro proposes that approximately 13 1/2
39 million of this be recovered from Newfoundland Power and
40 therefore Newfoundland Power's 215,000 island customers.
41 This translates, as Ms. Greene has said, into a rate increase
42 of approximately 3.7 percent for the retail consumer.
43 However, Hydro is also proposing a further increase to
44 Newfoundland Power's customer of 3.4 percent on July 1st,
45 2002, by virtue of the Rate Stabilization Plan. The
46 consumer has to appreciate that the total increase Hydro
47 proposes from Newfoundland Power's customers in 2002
48 exceeds 7 percent. Newfoundland Power knows that the
49 price of electricity is important to its customers and before
50 it delivers bills with higher rates, Newfoundland Power has
51 to do its best to ensure those higher rates are justified.

52 The rate increases proposed by Hydro in this
53 application, Mr. Chairman, are high by recent standards,
54 but Newfoundland Power's interest in the application is in
55 fact broader than that. Because Newfoundland Power's
56 customers pay approximately two-thirds of Hydro's total
57 regulated costs on an annual basis, we have a distinct
58 interest in ensuring that the ongoing regulation of Hydro
59 is transparent, also a term used by the Chairman this
60 morning, that improvements in Hydro's current regulatory
61 reporting will be required to achieve this. The regulation of
62 Hydro must be consistent with achieving least cost
63 operation of electric systems in Newfoundland. That is the
64 power policy which is established by the province and set
65 out in *The Electrical Power Control Act* 1994, and your
66 regulation of Hydro must be in accord with sound public
67 utility practice. Newfoundland Power believes that some of
68 Hydro's proposals in this case will need to be modified to
69 reflect that standard.

70 Now again to assist this Board, Hydro and my
71 fellow intervenors, in understanding what issues
72 principally concern Newfoundland Power, I too will express
73 these in very general terms. Naturally in some areas there
74 will be many subsidiary issues that will consume a great
75 deal of time but for today's purposes I will categorize them
76 broadly.

77 The first, Mr. Chairman, category of interest to
78 Newfoundland Power in these proceedings is Hydro's 2002
79 test year costs. These costs are what will most directly and
80 immediately be reflected in our customers' rates. One of the
81 most prominent of these costs is Hydro's 2002 forecast
82 production costs. Newfoundland Power has serious
83 misgivings about the appropriateness of Hydro's hydraulic
84 production forecast and this in turn of course impacts upon
85 the thermal production forecast and the cost of No. 6 fuel
86 to be recognized in the test year.

87 Mr. Chairman, Hydro's hydraulic forecasts are
88 conservative and Newfoundland Power will be asking you
89 to increase them for the benefit of Newfoundland Power's
90 customers. The amounts at issue on this one issue alone
91 amounts to many millions of dollars.

92 In addition, still under the subject of the 2002 test
93 year costs, Newfoundland Power will examine and question
94 Hydro's other costs, both capital and operating for the test
95 year with a view to ensuring that they provide an
96 appropriate basis to set future rates and that they reflect
97 reasonable operating efficiencies as required by the
98 regulatory legislation.

99 A second issue for Newfoundland Power relates
100 to Hydro's proposed financial target. Newfoundland and
101 Labrador Hydro has presented its application to the Board
102 requesting approval of both short-term and long-term

1 financial target. Newfoundland Power will be asking this
2 Board to be cautious when considering approval of these
3 financial targets, particularly those which will not have
4 impact until well into the future. Newfoundland Power in
5 fact disputes that it is reasonable for this Board to approve
6 some of these proposals at this time because it would be
7 inappropriate to pre-approve future rate increases in a way
8 that Hydro has requested.

9 Newfoundland Power will not take substantial
10 issue with Hydro's request for approval of the 3 percent
11 return on equity for the 2002 test year or the target 80/20
12 debt equity ratio which Hydro proposes for the short-term,
13 however, Newfoundland Power takes issue with some
14 aspects of Hydro's financial targets for 2002, particularly as
15 they are inconsistent with Hydro's stated 2002 goal, either
16 in the application or in Newfoundland and Labrador
17 Hydro's formal financial plan.

18 A third significant issue in this proceeding are the
19 changes which are proposed by Hydro to the Rate
20 Stabilization Plan. Newfoundland Power believes the Rate
21 Stabilization Plan continues to benefit consumers by
22 smoothing out the impact of changing fuel prices on
23 electricity rates. Newfoundland Power does not believe its
24 consumers want wide fluctuations in their electrical bills.
25 However, Newfoundland Power will be suggesting or
26 recommending modifications to Hydro's proposed changes
27 to ensure that electricity rate changes which result from the
28 operation of the Rate Stabilization Plan are subject to a
29 reasonable degree of regulatory control.

30 And finally, the fourth broad issue, Mr. Chairman,
31 Newfoundland Power will ask the Board to consider sub-
32 issues relating to regulatory control and reporting.
33 Addressing these issues now is important because this is
34 Hydro's first hearing as a fully-regulated public utility. This
35 issue is complicated by the fact that Hydro has both
36 regulated and unregulated operations. Clarifying how
37 these costs will be dealt with for regulatory purposes and
38 reported to this Board in future will ensure that the 2002
39 test year costs give regulatory transparency, I'm sorry, will
40 ensure regulatory transparency.

41 So to summarize, Mr. Chairman, the four broad
42 issues that Newfoundland Power will pursue are the 2002
43 test year costs, principally hydrology, financial target, the
44 RSP and the regulatory control and reporting. Because this
45 is Hydro's hearing, not Newfoundland Power's hearing, and
46 Newfoundland Power is an intervenor, we anticipate calling
47 only two external witnesses, experts by the name of Mr.
48 John Brown and Mr. Larry Brockman, whose credentials are
49 reflected in the curriculum vitae filed with their pre-filed
50 testimony.

51 In summary then, Mr. Chairman and

52 Commissioners, before you today is the proposal for a large
53 electrical rate increase, amounts to \$18 million. In addition
54 to considering that, you will have to consider other major
55 decisions which could have a significant influence on
56 future rates. At the conclusion of this hearing I am
57 confident that Newfoundland Power will be asking you to
58 approve rates for Hydro at a lower level proposed in the
59 application and also to establish reasonable policies to
60 provide for the effective future regulation of Hydro. Mr.
61 Chairman, that is the opening statement of Newfoundland
62 on behalf of its 215,000 island customers. Thank you.

63 MR. NOSEWORTHY, CHAIRMAN: Thank you very much,
64 Ms. Butler. Could I ask the industrial customers to proceed
65 with their opening statement, please?

66 MR. HUTCHINGS: Thank you, Mr. Chair. As each person
67 who has spoken this morning I think has already said in
68 one way or another, this is not a typical hearing before this
69 Board. For some of the panel members it has been noted
70 this will be their first full hearing on a major public utilities
71 application. For Newfoundland and Labrador Hydro, as
72 has been noted, it is the first general rate hearing since the
73 legislative amendments which have been spoken of, which
74 mean that this Board doesn't just recommend rates for
75 Newfoundland and Labrador Hydro now as they did under
76 the old legislation. They fix the rates and approve the
77 rates. And for everyone here, as again has already been
78 noted, it's the first time in ten years that Hydro has been
79 before the Board with a general rate application, and this
80 has meant there's been a great deal of catching up to do to
81 bring the parties and the Board up-to-date on what has
82 been happening over all these years. Partly, I guess, as a
83 result of all these firsts, the path to the opening of this
84 hearing today has been a little rocky.

85 Hydro is here because the Board ordered it to be
86 here. Hydro did not meet the initial deadline that the Board
87 set for its filing of May 1st, 2001, and that gave rise to a
88 month's delay in the time available for everyone to cope
89 with this rather unusual hearing. This has been especially
90 bothersome to the industrial customers since it represents
91 a delay in implementing the cost allocation methodology
92 approved by the Board in its 1993 report, after the hearing
93 in 1992 in that regard. Allocations which the industrial
94 customers regarded as inappropriate and unfair were to
95 change after that hearing with significant cost savings to
96 the industrial customers forecast to occur. These
97 customers have been forced to continue to pay rates based
98 on these unfair allocations due to Hydro's decision not to
99 come before this Board and have new methodology
100 implemented. This represents millions of dollars that have
101 now been lost to our clients.

102 In the lead-up to this hearing there have been
103 many hundreds, as Ms. Greene has noted, of information

1 requests asked and answered, there have been disputes
2 over some of them and there are still some questions
3 unanswered. We must applaud the effort that Hydro has
4 made in producing the huge quantities of information
5 which we do have but we are still left with some concern
6 that the delays have occurred due to Hydro failing to
7 provide complete explanation of items that have been
8 questioned.

9 The principal case in point is the Rate Stabilization
10 Plan which was described only in outline form in the pre-
11 filed evidence and is still not fully explained despite several
12 rounds of questions. Just for future reference we would
13 suggest it would serve Hydro and the process well if some
14 thought were given to the likely issues to be raised by
15 intervenors, the likely questions that will be asked, the
16 advisability of providing the basic information at the time
17 of its initial filing rather than in bits and pieces throughout
18 the process.

19 The industrial customers have been delayed in
20 filing evidence in the matter. Much of what was filed as
21 supplementary evidence we would have rather filed as the
22 initial evidence, especially in the case of our expert, Mr.
23 Osler, and it may well be that we'll have to file additional
24 further evidence before Mr. Osler actually comes here to
25 give his evidence before the Board, but for now we must
26 move on, I think, from the point that we are and try to deal
27 with the matter as efficiently as possible.

28 To put the whole matter into context, however, I
29 think another unusual aspect of this hearing is that it has
30 to be regarded as stage one. While it did not appear from
31 the pre-filed evidence, Hydro has told us since in the
32 answer to one of the demands that in accordance with its
33 five-year forecast it plans a further rate hearing in the year
34 2003 for rates to be effective in 2004. From the point of
35 view of our clients, however, the truly frightening numbers
36 appear in the answer to IC-254, which tells us that in 2004
37 the average rate paid by industrial customers per kilowatt
38 hour will be 35 percent higher than the 2001 rate. Increases
39 of this magnitude clearly change the cost characteristics of
40 industrial operations and negatively impact
41 competitiveness. It is vital to bear in mind various elements
42 in the current case which Hydro wishes to postpone until
43 the next case, primarily the so-called market rate of return
44 and plans for various rate changes in different systems.

45 Stage two will be the 2003 hearing, and that will be
46 on us all too quickly and we need to deal here with the
47 issues in the context of where rates are projected to go
48 within 25 months of the projected conclusion of this
49 hearing.

50 I want to say a few words now about the clients
51 that my friend, Mrs. Andrews, and I represent here, the

52 industrial customers. The Board obviously is familiar with
53 Hydro and familiar with Newfoundland Power as regulated
54 utilities but perhaps not necessarily as familiar with the
55 three companies and four operations that are intervening
56 here as the industrial customers.

57 Abitibi Consolidated Inc. operates integrated pulp
58 and paper mill facilities at Grand Falls and Stephenville.
59 Corner Brook Pulp and Paper Limited operates the Corner
60 Brook paper mill and is notably the successor to both
61 Bowaters Newfoundland Limited and Bowater Power
62 Company Limited, the latter company itself being a
63 regulated utility before this Board some many years ago
64 when it supplied electricity in Corner Brook and a number
65 of other areas on the west coast. It's also interesting to
66 note that the predecessors of both Abitibi and Corner
67 Brook Pulp and Paper Limited have been generating and
68 transmitting power on this island since long before
69 Newfoundland Hydro actually existed. North Atlantic
70 Refining, as we all know, operates the Come By Chance oil
71 refinery.

72 Collectively the industrial customers represent in
73 excess of 16 percent of Hydro's annual sales. As a group
74 they employ close to 3,000 Newfoundlanders, and their
75 combined annual payroll is in the vicinity of \$150 million.
76 They are being asked in the year 2002 to pay power bills
77 that will exceed \$50 million. It's not surprising that these
78 customers have a very significant interest in these
79 proceedings, and that is reflected in the fact of Mr. Dean,
80 here sitting to my left, coming here and actually moving to
81 St. John's for the duration of this hearing. It's reflected in
82 the presence behind me of the Mill Manager from
83 Stephenville, Mr. Backus (phonetic), and the Manager of
84 the Deer Lake power operation out of Corner Brook Pulp
85 and Paper, Mr. Carl Stratton, who is also here this morning,
86 and we may in fact see more of any number of these people
87 as the hearing goes on. This is a matter which is of such
88 import to these various operations that the attention of
89 their most senior personnel is attracted.

90 The industrial customers of Hydro are businesses.
91 These companies use our natural resources, including our
92 labour force, to create economic activity which provides
93 jobs both directly and indirectly in several different regions
94 in this province. In order to do so, they must make a profit.
95 They are price takers. They sell their products in
96 international markets in which they cannot, either
97 individually or collectively, affect the price at which their
98 product sells. They compete within their own corporate
99 groups for work and with the world at large. Their ability to
100 continue to create economic activity in this province is
101 dependent upon their ability to produce a product at a cost
102 which allows them to be competitive in world markets. If
103 the gap between their costs and the price dictated by the

1 market does not produce a sufficient return on the
2 investment by the shareholders of these companies, they
3 cannot continue to operate. These are truly bottom line
4 operations. They are good corporate citizens who support
5 many activities in various communities in the province but
6 they are required to contribute to the bottom line in order
7 to be able to continue. The companies ask nothing more of
8 this hearing than that they be asked only to pay their fair
9 share of the costs which are incurred overall in the
10 production of electricity in this province, and this bottom
11 line philosophy also guides the approach to this hearing.

12 It is appropriate and supported by precedent that
13 those in the position of the industrial customers in this
14 hearing be awarded their costs of participating in these
15 hearings, but the business approach needs to be applied to
16 these proceedings in the sense that the total cost of the
17 process needs to be minimized. The parties need to
18 identify for the Board the issues which need to be
19 addressed and address them, as the Chair said this
20 morning, succinctly and directly. There are literally
21 thousands of factual matters raised in the material before
22 the Board. There are hundreds and possibly thousands of
23 decisions that have been made by Hydro since it was last
24 before the Board which affect the cost of providing
25 electrical service to the people and businesses of the
26 province. The parties here need to identify those issues
27 that make a difference, which either, because of a matter of
28 principal or a simple matter of number of dollars involved,
29 can or should have an impact on the rates for or the terms
30 and conditions applicable to the sale of power in the
31 province.

32 The Board is here to regulate Hydro, not to
33 manage it. Unless a particular expenditure allocation or
34 determination raises a point of principle or involves a
35 significant amount of cost, the details of such expenditure
36 allocation or determination do not merit consideration in
37 this hearing or justify the inevitable cost that examination
38 in this forum implies.

39 The industrial customers will endeavour to
40 implement this philosophy through the hearing process.
41 We will identify the issues which we wish the Board to
42 address, offer evidence on those to the extent that it is
43 necessary, cross-examine those witnesses who can speak
44 to those issues, and offer submissions on those issues for
45 the Board's consideration. We will not be addressing those
46 points which do not affect our client's interest or which are
47 not of sufficient significance to merit consideration at the
48 hearing. We will not offer evidence, cross-exam witnesses
49 or offer submissions unless there are issues of concern to
50 us that require it, and we would hope that that will be the
51 approach of all the other parties in order to facilitate an
52 efficient hearing.

53 I want to deal now with the types of issues that
54 the Board must address. Inevitably there will be an
55 emphasis throughout this hearing from all the intervenors,
56 ourselves included, on reducing the cost to the ratepayer
57 for electrical service. We must, however, introduce now
58 and never forget this caveat. Continued reliability of the
59 service is a vital part of what the industrial customers and
60 others require. Interruption of electrical service is an
61 inconvenience to everyone, but to those who rely on
62 power for industrial processes, the consequences of an
63 interruption can be devastating, involving both loss of
64 product and process, damage to equipment and long
65 periods of down time to re-set equipment which result in
66 loss of production, loss of profit and damaged reputation
67 in the marketplace. While we are all interested in lower
68 costs, none of us will benefit if such apparent savings
69 come at the price of downgrading the current level of
70 reliability on the system.

71 Typically, Mr. Chair, a general rate hearing of this
72 type involves three classes of issues. The first are the
73 revenue requirement issues, those which determine the
74 amount of money which Hydro must collect to meet
75 expenses and satisfy any need for a return that the Board
76 may approve. This reflects the first basic principle of
77 public utilities regulation that rates in total must meet
78 expenses and return in total. It is in the best interest of
79 every ratepayer that revenue requirement be minimized.
80 This represents savings to the entire system and means
81 lower rates.

82 The second class of issues is the cost of service
83 issues. These address questions of how the revenue
84 requirement is allocated among services and among classes
85 of ratepayers. Here different classes may have different
86 interests. Once revenue requirement is determined, all
87 classes together must contribute in total that amount.
88 Allocation to one class under cost of service of a particular
89 amount or a certain proportion of a particular amount
90 affects the amounts that other customers and other classes
91 must pay. Accordingly, parties who supported one
92 another on a particular revenue requirement issue may be
93 completely at odds on a cost of service issue related to the
94 same cost.

95 The third class of issues are rate issues. Once
96 costs have been allocated to each class, the next step is to
97 design a rate that recovers those costs from that class and
98 meets the other rate design criteria that are spoken of by
99 the expert witnesses as to price signals and other concerns.
100 Again, different classes of ratepayers may have different
101 views on rate issues.

102 These classifications of issues provide structure
103 to any proceeding of this nature. The given issue may be
104 dealt with as a revenue requirement issue, a cost of service

1 issue and a rate issue, but its implications can always be
2 identified for each classification separately. For instance,
3 in this hearing the Rate Stabilization Plan has revenue
4 requirement implications since amounts affected by it are
5 added to or subtracted from the current year's revenue
6 requirement. It has cost of service implications as amounts
7 associated with particular variances under the plan may
8 need to be assigned to different customer classes, and it
9 has rate design implications since its effects may act to
10 enhance or diminish a price signal intended to be sent by
11 a particular rate. It's important in considering any given
12 issue to identify it as a revenue requirement issue, a cost of
13 service issue or a rate issue.

14 I want to speak now of the various rate
15 requirement issues that the industrial customers have
16 identified to be addressed at this hearing. The first and
17 perhaps the greatest in terms of dollar significance is the
18 question of fuel prices. The Board needs to know if we
19 have the best forecasts available and if issues of foreign
20 exchange have been given their proper weight in respect of
21 the forecast for the price of No. 6 fuel. That's clearly a
22 revenue requirement issue and affects directly the amount
23 of money that Hydro needs to recover in the test year.

24 The second revenue requirement issue we would
25 address is the RSP. Over 50 percent of the fuel price
26 increase is being deducted from the revenue requirement
27 and funnelled through the RSP. This represents a shifting
28 of cost from current customers to future customers and
29 presents significant issue if the Board gives consideration
30 to modifying or abolishing the plan, as some have
31 suggested. It becomes necessary to determine how the
32 RSP has functioned in the past and how it should function
33 in the future.

34 Getting back to my initial comments, this is
35 another first. This is the first time the Board is setting rates
36 for industrial customers that are determined in large part by
37 the RSP. RSP was a creation which came into effect for the
38 retail customers in the course of a hearing before this
39 Board, 1985, but the industrial plan was a creation of Hydro
40 arising out of that and has not previously been considered
41 by the Board.

42 The Board will have to consider at this hearing
43 whether the current form of the plan is appropriate, whether
44 there should be separate plans for the industrial customers
45 and the retailers, and whether all of the variances in fuel
46 price, hydraulic production and load should be
47 components of the plan. These are big revenue
48 requirement issues simply because the balances in the plan
49 are so large and are forecast to continue to be large.

50 The complexities of this plan are well illustrated by
51 the fact that Hydro missed the effect that the plan was

52 having on the effort to eliminate the industrial customers'
53 contribution to the rural deficit, and as we can see in the
54 answer to IC-242, Hydro is now crediting back in excess of
55 \$1.5 million to the industrial customers which the plan
56 inadvertently took from them as a contribution to the rural
57 deficit, so it is clear that this plan deserves special scrutiny
58 in the course of this hearing.

59 The hydraulic production forecast issue, which my
60 friend, Ms. Butler, raised, is a revenue requirement issue.
61 If the production forecast changes, obviously revenue
62 requirement will be affected since more or less fuel will be
63 used, and the Board will need to grapple with whether or
64 not the forecast ought to be changed.

65 Another revenue requirement issue is the question
66 of forecast variations. If any of Hydro's forecasts are
67 shown to be inappropriate or to display statistical or other
68 biases over time, the revenue requirement for the test year
69 based on these forecasts should change accordingly.

70 There is an example that appears I think on the
71 face of the record already in the sense that Hydro's forecast
72 of when capital projects will be in service is generally
73 optimistic and projects forecast to be in service in 2002 may
74 not actually be in service in that year. If that's the case,
75 Hydro will be recovering depreciation and a return on
76 assets which are not properly in rate base. I think Mr.
77 Brushett has identified this problem in his report and this
78 is a point that emphasizes how important it is to rely on
79 good forecasting. We'll deal with that point in more detail
80 later.

81 As my friend, Ms. Butler, also mentioned, the
82 prudence of Hydro's expenses is a revenue requirement
83 issue. Hydro should only recover expenses that have been
84 or will be in the test year prudently incurred. The Board
85 will need to examine whether expenses charged in the test
86 year relative for instance to the Great Northern Peninsula
87 interconnection are prudently incurred. This reflects upon
88 the impacts of past decisions and will probably be a useful
89 lead-in for the Board in what I've called stage two of this
90 hearing in 2003 when the prudence of decisions on future
91 sources of generation will be at issue.

92 Other expenses may also be questioned, especially
93 those which have been incurred or may have been incurred
94 in pursuance of Government policies or corporate
95 promotion as opposed to the business of generating and
96 delivering power.

97 The final revenue requirement issue that deserves
98 attention, and this is usually the biggest revenue
99 requirement issue in a hearing of this type, is the question
100 of return on equity. Again, this not being a typical hearing,
101 this untypically is not a big issue in terms of percentage
102 return at the current hearing. Hydro is seeking a three

1 percent return on what it calls equity, and the level of profit
2 that would be produced by that is not really inconsistent
3 with the type of number that the old, the margin for interest
4 coverage would have produced.

5 The real issue that we see here is the question of
6 who owns the equity and hence who should get the return.
7 We feel the evidence shows that all the current retained
8 earnings in Hydro, the so-called regulated equity, belongs
9 to the ratepayers, that the ratepayers should get the return,
10 and according to proper principles of financial accounting,
11 this retained earnings amount should be regarded as zero
12 cost capital, exactly the same as the employee benefit
13 amounts that have already been referred to by Hydro as
14 zero cost capital. On this basis, ratepayers have in fact
15 been subsidizing taxpayers and not vice versa.

16 There is of course also a related issue which is the
17 desire of Hydro to move to a particular debt-equity ratio
18 and the Board will have to determine, given that issue's
19 effect on revenue requirement, whether that is a good, bad
20 or indifferent thing from the ratepayers' point of view.

21 Those being the revenue requirement issues that
22 we need to address, I'll move now to the cost of service
23 issues, and the cost of service issues that affect the
24 industrial customers are of course issues related to the
25 interconnected grid since the industrial customers are on
26 the interconnected grid and are no longer required to
27 contribute to the rural subsidy.

28 The first and sort of overriding issue, which is a
29 cost of service issue for the industrial customers, is
30 represented by the simple question, why is our increase so
31 large. With the new methodology approved by the Board
32 in its 1993 report, there should have been significant
33 savings to the industrial customers, yet the average
34 increase in rates for industrial customers is well above the
35 percentage for the retailer. Intuitively there should have
36 been little or no increase to industrial rates at this point.
37 These rates have been adjusted already, while
38 Newfoundland Power's rates, as Ms. Greene pointed out,
39 have been the same since the early '90s. There's no huge
40 change in patterns of use or loss of, change in patterns of
41 use by the customers and the issues of loss of other
42 industrial customers have already been absorbed. The
43 evidence that has been pre-filed, the supplementary
44 evidence of Cam Osler, deals with this question in Section
45 2, and it will be an overriding theme for the industrial
46 customers as we deal with cost of service issues.

47 While under the legislation the industrial
48 customers are no longer required to contribute to the rural
49 deficit, there remains a question as to whether or not Hydro
50 has fully complied with that legislation. It appears that
51 there was no gradual reduction in the industrial customers'

52 contribution to the deficit as required by the legislation.
53 There was simply a cut-off at the deadline date provided in
54 the legislation. Accordingly, in our submission, Hydro has
55 collected amounts from the industrial customers unlawfully
56 for a number of years. The Board has the jurisdiction to
57 correct that error since Hydro has not been before the
58 Board for rates since it occurred.

59 There is a related issue as to why Hydro has failed
60 to amend the rates to recover the portion of the deficit
61 previously recovered from industrial customers, and that
62 becomes an issue because their failure to do so is likely or
63 may lead to a reduction in retained earnings, and if in fact
64 those retained earnings are the property of the ratepayers,
65 they have been improperly reduced by Hydro in that way.
66 That will be a significant issue for cost of service.

67 I have already mentioned the Great Northern
68 Peninsula interconnection and the allocation of assets
69 relative to the Great Northern Peninsula is a very significant
70 issue for the industrial customers in this hearing. Who
71 should pay for the costs of interconnection and the supply
72 of power to customers on the Great Northern Peninsula? Is
73 this properly a common cost, as Hydro suggests? Is there
74 a tangible benefit to the interconnected grid as it existed
75 prior to interconnection and, if so, what is the value of that
76 benefit? This is a major issue which involves, so far as we
77 can tell, a cost in excess of \$1.5 million a year to industrial
78 customers. And that's not the only allocation issues.
79 There are others. There is the question of the transmission
80 line from Port aux Basques to Bottom Brook and Hydro
81 itself has raised an issue with respect to assets on the Burin
82 Peninsula. These are all cost of service issues.

83 There are some leftover issues relative to cost
84 allocation methodology, which of course are clearly cost of
85 service issues. Some parties appear to want to re-try some
86 of the issues that were already decided in 1993, such as the
87 assignment of transmission facilities or some part thereof
88 on the basis of energy use. It is not our view that there
89 appears evidence on the record at this point that would
90 justify re-trying any of those issues, but there are issues
91 that the Board must consider in terms of whether the best
92 allocator for generation is a one coincident peak or two
93 coincident peak allocator, and that was specifically left for
94 this hearing, and that's a cost of service issue.

95 Another cost of service issue arises in connection
96 with the frequency converters that have been provided
97 previously for the use of Abitibi and Corner Brook Pulp
98 and Paper, and I note you're looking at the clock, Mr. Chair.
99 I can probably finish inside of ten minutes, if that's okay.

100 MR. NOSEWORTHY, CHAIRMAN: Sure.

101 MR. HUTCHINGS: We need to look at whether or not it's
102 fair to back out of the understandings under which these

1 frequency converters were put in place in the 1960s. There
2 is a significant issue here because if these converters were
3 not in fact in place, the Board would be dealing with a much
4 larger issue at this point and that would be the conversion
5 of generation at Bay D'Espoir from 50 cycle to 60 cycle, and
6 that will appear from the documents that have been
7 provided.

8 Another cost of service issue is what we've called
9 the question of dispatchable reductions in load. This is a
10 somewhat complex issue but relates to the relationship
11 between the interruptible "B" power, as it now exists and is
12 provided to Abitibi at Stephenville, and the generation
13 credit which is provided to Newfoundland Power in respect
14 of its own generation. In our view, these two things
15 amount to a similar benefit to the grid and ought to be
16 costed and credited to each of the persons providing those
17 benefits in a similar way. It does not appear that that is the
18 case now and that is an issue that we need to examine
19 further.

20 There will be a further cost of service issue in
21 connection with transformer losses. Hydro is proposing a
22 change in the allocation of costs associated with these
23 losses. We recognize that the current system may not be
24 entirely fair. We would suggest that Hydro's system as
25 proposed is equally unfair and Mr. Dean will address this
26 issue in his evidence and will have a suggested solution.

27 Another cost of service issue the Board has to
28 deal with is the question of non-utility generators and how
29 the costs of the power purchased from non-utility
30 generators will be allocated under the cost of service. That
31 is one that has not been addressed previously by the
32 Board. We can simply say that Hydro's proposed
33 treatment, which is similar to that applied to its own
34 generation, is appropriate, but that needs confirmation by
35 the Board.

36 Again with the RSP, as I've mentioned, that can
37 also be a cost of service issue. If there continue to be two
38 plans, one for the industrial customers and one for the
39 retailer, there will be cost allocations as between those two
40 plans.

41 And those, Mr. Chair, are the cost of service
42 issues that we have identified to date.

43 There are a number, but fewer, thankfully, of rate
44 issues. The wheeling rates as proposed by Newfoundland
45 Hydro need to be examined and we need to understand
46 why parts of the system that are not used for wheeling and
47 cannot be used for wheeling are used to established a
48 wheeling rate.

49 The issue will be raised no doubt with respect to
50 rate options, both for industrial customers and perhaps

51 also the retailer. As an example, the interruptible "B" rate,
52 which now exists only in a contract with one particular
53 customer, in our view ought to be confirmed in a rate
54 schedule and the customer should know whether or not
55 this rate is going to be available on an ongoing basis.

56 The question of a split rate for Newfoundland
57 Power has been raised and that may tie into the question of
58 whether or not load variances should be accommodated
59 within the RSP. If in fact the load variation were to be
60 removed from the RSP, a split rate for Newfoundland Power
61 may in fact be the proper way to allocate the load forecast
62 risk, and that's an issue that will undoubtedly get some
63 attention during the course of the hearing, and equally then
64 with the transformer losses, depending upon how the cost
65 of service issue goes, there may be rate questions to be
66 resolved in that regard.

67 The other question of, that would fall within the
68 subject of rates are questions involving the form of
69 contract for the industrial customers. We are not in a
70 position to delineate all the issues at that point but we will
71 be making further submissions as the hearing requires as
72 we progress.

73 Those are the issues we've identified.
74 Undoubtedly others will arise as we go along. Again, we
75 will address only those which will have an impact on the
76 industrial customers.

77 A final word in terms of where we should be at the
78 end of this hearing. Clearly we are in, we are simply at a
79 point in time in the process of regulation of Hydro and the
80 Board should consider some direction to Hydro at the end
81 of this hearing to facilitate that ongoing process. We
82 would suggest that all the participants here receive a cost
83 of service study based upon the Board's final order,
84 whatever that may be. Equally, all the participants should
85 receive on an ongoing basis RSP reports modified to show
86 clearly the calculation of allocation and any customer
87 splits, if such splits are so required under the final form of
88 the plan. Actual cost of service results, study results,
89 should be provided annually, both to the Board and
90 interested parties, and the parties here should be copied
91 with the annual review reports prepared for the Board.
92 These steps, in our view, will make future hearings a much
93 less trying procedure.

94 We have pre-filed evidence on behalf, from Dr.
95 Michael Vilbutt (phonetic), questions of cost of capital, and
96 from Mr. Cam Osler on a number of cost of service issues
97 and related items. We must advise the Board this morning
98 that the proposed witness, Pierre Coté (phonetic), will be
99 taking up a new position outside of the Abitibi organization
100 prior to the time of his anticipated appearance before the
101 Board. We are in the process of identifying another

1 individual who can step into Mr. Cote's place and we will
2 file appropriately amended evidence as soon as possible.
3 We do not expect that the substance of the evidence will
4 be affected by this change.

5 I'd like to thank you for your patience, Mr. Chair.
6 I wanted to set out in as great a detail as possible the
7 issues that we wish to address so that when you hear from
8 us during the course of this hearing you'll be able to relate
9 our comments to specific issues and understand where
10 we're coming from.

11 Thank you, sir.

12 MR. NOSEWORTHY, CHAIRMAN: Thank you very much,
13 Mr. Hutchings. It is now 10 after 11:00. We will adjourn,
14 take a break until 11:25, at which time we'll resume our
15 opening statements. Thank you very much.

16 (break)

17 MR. NOSEWORTHY, CHAIRPERSON: ... before lunch, an
18 addendum to PU-18 which indeed should accommodate the
19 redirect sought by the Consumer Advocate. We do feel it's
20 contained in the regulations but I think to move the
21 proceeding along, given that this is the first day, we want
22 to get on to the presentation. We will be issuing that
23 addendum and everybody will have an opportunity to
24 review that, and I trust that will be satisfactory.

25 MR. FITZGERALD: Thank you, Mr. Chairman.

26 MR. NOSEWORTHY, CHAIRPERSON: Thank you. I'd
27 now ask the Consumer Advocate to proceed with his
28 opening statement please? Thank you.

29 MR. BROWNE, Q.C.: Yes, thank you, Mr. Chairman and
30 Vice-Chairman Whalen, and Commissioner Powell, and
31 Commissioner Saunders. We are pleased to be here this
32 morning. In June we were appointed under the authority of
33 Section 117 of the Public Utilities Act by the Lieutenant
34 Governor in Council to represent the interests of domestic
35 and general service consumers of electricity in the province
36 for purposes of this hearing. And with our appointment we
37 requested again permission to retain experts. We have
38 retained Douglas Bowman, a member of the Professional
39 Engineers of Ontario, and of the Institute of Electronic
40 Engineers, who has testified previously before this Board
41 and works with (inaudible) Consulting in Virginia, and he
42 has provided expert testimony previously before the Nova
43 Scotia Public Utilities Board. His expertise is in rate design
44 work, and he has conducted rate design work in Pakistan,
45 India, Shanghai, Vietnam, Egypt, and has extensive work
46 experience with Ontario Hydro. Despite the fact he has
47 worked all over, he had the good sense to marry a
48 Newfoundland girl from Hampton and so there is a
49 Newfoundland connection there.

50 We retained Dr. Basil Callaman (*phonetic*), a
51 professor of finance at the Richard Ivey School of Business
52 at the University of Western Ontario, and for over 30 years
53 was a professor of finance and management sciences at the
54 University of California in Los Angeles. He has taught at
55 Harvard University, the University of Toronto, and holds
56 a Ph.D. in Administrative Sciences from Yale University.
57 He will deal with the rate of return on capital structure. Dr.
58 Callaman has testified previously before this Board and
59 some counsel here are familiar with Dr. Callaman. We have
60 also had the assistance of Dr. James Feehan, an economist
61 with Memorial University who has assisted in the past. He
62 will not be testifying but he has provided invaluable advice
63 and assists us on a daily basis, and my colleague Steve
64 Fitzgerald has been working with me, and has been working
65 closely with Dr. Callaman, and will be dealing with evidence
66 pertaining to Dr. Callaman and the other experts who are
67 testifying on capital structure.

68 And Newfoundland Hydro in this application are
69 intending to raise revenues in 2002 from \$297 million to
70 \$314 million. This is an increase of \$18 million, and their
71 proposal is to spread the increase over major customer
72 groups. The biggest contributor will be, of this \$18 million
73 will be consumers who purchase their electricity from
74 Newfoundland Power. It must be remembered that 50
75 percent of the population, of the province's population
76 resides on the eastern portion of the island and mainly on
77 the Avalon Peninsula, which includes this capital city
78 region, of course, so most of the increase will be felt there.
79 The increase doesn't seem to affect Labrador according to
80 the proposal, although there are particular issues pertaining
81 to Labrador, and there is some increase anticipated in
82 Labrador, and our friend, Mr. Ed Hearn, is here and he will
83 be speaking to issues pertaining to Labrador City and
84 Wabush.

85 According to its evidence, Hydro is seeking an
86 increase because of increasing costs for purchases of
87 Bunker C oil at Hydro's thermal generating facility at
88 Holyrood, and the reason for this increase is because the
89 Rate Stabilization Plan has reached the limit of its deficit,
90 the \$50 million cap set by the Board some years ago, and I
91 can imagine when the Board set that it was never
92 anticipated it could ever be reached. Hydro's answer is
93 now to increase that cap to \$100 million, while providing us
94 with a forecast indicating that it would reach that limit by
95 December 2002. How realistic is that? What do we do after
96 December 2002 if we have reached the \$100 million mark as
97 is forecast? Where does it stop?

98 Hydro wants the rate for a barrel of oil moved from
99 \$12.50 and it was set at \$12.50 in 1992. At that time Hydro
100 actually wanted the price set at \$14.50, and Newfoundland
101 Power came along and said they wanted it at \$10.00, I

1 believe it was. It might have been \$10.50, but anyway, the
2 Board compromised and set it at \$12.50. That's how we're
3 at the \$12.50, and they want to move that price from \$12.50
4 to \$20.00 while providing evidence that oil is forecast in the
5 foreseeable future to be in the \$28.00 range. They want to
6 keep us in a deficit. They want to keep borrowing to pay
7 for this because they know full well that the consumers of
8 the province will be the people they have to turn to if
9 things go awry.

10 We have reviewed the expert evidence in reference
11 to the Rate Stabilization Plan. Our own witness, Doug
12 Bowman, recommends elimination of the Rate Stabilization
13 Fund. I have looked to the witness, Mr. John Wilson,
14 reviewed his evidence, and he provides no endorsement for
15 a Rate Stabilization Plan. And Newfoundland Power's own
16 expert, Mr. Brockman, is clear in stating that the funds
17 should not increase beyond \$50 million unless such
18 increases have specific Board approval. I think we might
19 be there now. We might be at the \$50 million mark now. So
20 there's danger that has been recognized by all of the
21 experts in reference to the Rate Stabilization Plan.

22 To allow Hydro to increase the Rate Stabilization
23 Plan to \$100 million with a hope that oil prices may drop is
24 not advocated by any expert who will appear before this
25 Board. We note inherent problems in the Rate Stabilization
26 Fund. For instance, those who exit the system, those who
27 leave the province for one reason or another, leave the bill
28 to the rest of us to pay. They're gone. This is hardly fair to
29 the consumers remaining. Neither is it fair to those making
30 a determination as to what form of heat they wish to install
31 in their house. We hear from time to time utilities saying we
32 have the cheapest electricity in Atlantic Canada, but they're
33 not telling people that we also have a Rate Stabilization
34 Fund which is debt-ridden, and for which we have to come
35 back and bill you at some time. While those heating their
36 homes with oil know the problems associated with market
37 fluctuation, we heard all the stories of last winter, those
38 heating their homes with electricity are assuming there is
39 no such fluctuation, and how wrong they all are.

40 For public policy reasons, if for no other, we
41 should have all the providers of energy at a level playing
42 field. There should be no subsidization of those who
43 purchase electricity to heat their homes because there is no
44 subsidization for those who choose to heat their homes
45 with oil or propane or wood. Should the Board be involved
46 in endorsing such a policy and interfering with the
47 marketplace? A person building their home can go to an oil
48 company and they know with what they have to deal.
49 There will be fluctuations. But here we have artificiality if
50 they go to seek information in reference to power because
51 the true effects of purchasing power now are not told to
52 them. It's a form of bait and switch (*phonetic*), I guess.

53 Now we appreciate, and fully appreciate,
54 Newfoundland Power's efforts to bring evidence in this
55 hearing which will be of assistance to cut costs, and we
56 acknowledge their comments this morning, but neither are
57 we naive. We fully recognize that Newfoundland Power
58 will be bringing their own rate application this spring and
59 I've never known them to bring an application that didn't
60 have an increase attached with it, so while looking to
61 Newfoundland Hydro's application, they are no doubt
62 setting the stage to protect their own interests this spring.

63 I do not fault Newfoundland Hydro for not
64 bringing an application since 1992. We all know, some of
65 us appeared before this Board and consented to
66 postponement of applications because the government had
67 initiated an energy policy review. We were all informed
68 that it wouldn't be in the province's interests to have
69 Newfoundland Hydro under scrutiny while the company
70 was involved in negotiations relating to Churchill Falls.
71 And we concurred with applications to defer reviews of
72 Newfoundland Hydro for those reasons, so that is not of
73 their doing, and they should not have to take responsibility
74 for that.

75 Newfoundland Hydro's expert, Kathleen McShane,
76 recently appeared before this Board on behalf of
77 Newfoundland Power in their failed application, advocates
78 a rate of return of between 11 and 11.5 percent. However,
79 Hydro is proposing only a 3 percent rate of return itself.
80 There's no expert evidence on that. It doesn't want to ... it
81 wants the rate of return, it wants that acknowledged, the
82 11.5 percent. It wants that acknowledged, which will make
83 them higher even than Newfoundland Power, and it's
84 unclear as to when they want the rate of return, which
85 eventually they are awarded, to cut in. Now we have a
86 right to know that and that should be made perfectly clear
87 by their opening witnesses. We should be able to know
88 what exactly is being proposed here. Are they seeking an
89 order of the Board, and we know an order of the Board is
90 the effective way of dealing with rate of return, are they
91 going and saying to the Board, it's like a bank ... I guess if
92 you went to a bank and told the banker that you want a line
93 of credit for \$20,000, but you promise never to go over the
94 \$10,000. Once you've got the line of credit, that's there.
95 Once he agrees to the \$20,000. So it seems to me it's that
96 type of comparison. We urge Newfoundland Hydro to,
97 without any ambiguity on this issue, to state exactly what
98 their plans are. Consumers need to know, this Board needs
99 to know, everyone here should be apprised of what's
100 happening.

101 In the past, before this Board, we have advocated
102 that it would be in the consumers' interests if
103 Newfoundland Power and Newfoundland Hydro
104 cooperated and made determined efforts to reduce costs.

1 We have all experienced the visual ... Hydro's truck on one
2 side of the Trans Canada passing Power's truck on the
3 other. We're paying for it all.

4 Now there is now information before this Board
5 which indicates that the two utilities were working together,
6 indeed at the highest levels, to find ways to reduce costs
7 from 1995 to May of 1999. There were, I believe, some 16
8 working groups within the project and four sub-working
9 groups for a total of 19, and meetings were held regularly
10 over the years, and what was the result? The utilities could
11 not produce a final report, and I recommend ...
12 recommended reading for the Board should be exhibit CA-
13 201 and CA-190. Take a look at those reports and those
14 minutes. They will be eye-opening. The utilities cannot
15 find ways to work together to reduce costs. It is incumbent
16 upon the Board to impose these ways. It is fair speculation
17 that companies who have a rate base system are only
18 interested in increasing the rate base and ultimately
19 increasing costs because to increase the rate base is to
20 increase profit, and now we're having two companies on a
21 rate base system. We have Newfoundland Hydro who
22 takes its direction from its shareholder, and we have
23 Newfoundland Hydro, who will take its direction from its
24 shareholder ... both Newfoundland Hydro and
25 Newfoundland Power are answering to one master, separate
26 masters.

27 On issues of conservation, no company, neither
28 utility is currently conducting any advertising in this
29 province urging consumers to conserve. We all remember
30 some years ago when we were approaching a crisis
31 situation, light switches had the label, please turn off this
32 switch. When have you seen that last? We see no
33 advertising. It seems they are not interested in
34 conservation. They are interested in finding more ways to
35 generate and to increase their rate base. That's all they are
36 interested in doing. The Board has a responsibility here to
37 encourage them to conserve. That's something you can
38 do. You can do it readily. You can require that they
39 conduct advertising campaigns suggesting people
40 conserve. Because if people consume less, there would be
41 less generation required and the result would be to keep
42 rates low. We urge that orders be given to both utilities to
43 conduct conservation campaigns now.

44 In reference to rate design, there is information
45 before this Board in one of the information requests, I
46 forget which one it is now, but I'll point it out at the
47 relevant time, that as early as 1985 the Economic Council of
48 Canada advised utilities to put in place time of use rates.
49 The President of Newfoundland Power at the time rejected
50 the suggestion. The evidence of Doug Bowman is that
51 Hydro has not performed an analysis of time of use rates
52 since 1990. His evidence is that without updated studies of

53 marginal costs, time of use rates, Hydro is missing an
54 opportunity to improve customer service by offering rate
55 options and providing customers a level of control over
56 their bills.

57 Why can't we have time of use rates in this
58 province? They're in vogue all over the United States.
59 They are in place in many parts of Ontario. What makes us
60 so different here? I would offer that the difference is here
61 that the utilities want no part in them. They want
62 everything operating at its peak. They want you paying
63 only for energy charges. They don't want to look to the
64 demand side at all. I know, and you know yourself, just
65 seeing people in supermarkets, everyone loves a bargain,
66 everyone goes where ... we are oriented towards specials
67 and flyers. I can only think that if people had the option of
68 doing their laundry later in the night and operating their
69 dryer later at night because the rate was reduced, many
70 people would do it. They would move, they would assist
71 to move the system from its peak, but they're not being
72 offered any such option. We operate as if we're at a peak
73 at all times. The most expensive electricity is what we're
74 charged. That is not reasonable, that has to change.

75 Why won't the utilities try to improve customer
76 service and reduce supply costs? The answer is found in
77 PU-68. Take a read of it. It's well worth it. A letter dated
78 May 11th, 2000, from the senior counsel of Newfoundland
79 Power to the senior counsel of Hydro indicating that it is
80 neither necessary, nor desirable, to introduce a demand
81 energy rate structure for wholesale power purchases, and
82 the primary reason appears to be that it will create volatility
83 in the earnings of both Hydro and Newfoundland Power
84 from year to year. Now doesn't that say it all?

85 They are very concerned about their own
86 backyards. So when they come here to pretend to act on
87 behalf of consumers, we just need to go back and take a
88 read of PU-68. That shows what their intention is. They
89 don't like the volatility themselves. They won't give
90 customers these options.

91 Our own expert, Doug Bowman, has travelled the
92 world assisting governments in rate design. I've given you
93 some of the countries which he's travelled, has stated at
94 page 15 of his evidence, that there are issues pertaining to
95 cross-subsidization among customer classes. Mr. Bowman
96 states that customers are currently paying between nine
97 and 334 percent of the cost of supply, see CA-70. This
98 represents substantial cross-subsidization between rate
99 classes, and I'm quoting Mr. Bowman now. Here's what he
100 says, "Not unlike what I have seen in a number of
101 developing countries".

102 There are issues pertaining to Labrador and we are
103 very interested in hearing from those communities,

1 particularly those who are not interconnected, those
2 subject to diesel generation. There are issues pertaining to
3 the retention by Hydro of preferential rates. It is our
4 position that preferential rates should be discontinued
5 now, as indeed, Hydro itself proposed they should be
6 discontinued, I believe it was the 1990 hearing. That was
7 Hydro's proposal then, that they be discontinued at that
8 time.

9 Our positions are in the evidence on the rate of
10 return. You have the evidence of Dr. Callaman and the
11 range he is suggesting, which is single digit. And before
12 closing I would like to address another issue. You
13 mentioned in your opening, Mr. Chairman, and requested
14 decorum and I know we're all capable of that, but I guess
15 we're all not capable of it too. But I urge that you don't be
16 fooled by the lawyers. We're all here to represent our
17 clients as best we can, but we've also been trained to leave
18 the matter in the hearing room. We're quite capable of
19 going out and having a coffee together, even though we
20 may be, from your perspective, at each other's throats from
21 time to time, and I would hope that you would not interpret
22 our comments from time to time as being unusually hostile,
23 and I know all counsel will want to assist the Board. I know
24 that you don't have a lawyer on your panel, and you're here
25 in front of eight lawyers here this morning, is it ... eight or
26 ten lawyers here this morning, and we all know our
27 professions just as I'm sure you know yours. I have
28 requested in the past that the Minister of Justice ensure
29 that a lawyer was always on the panel, particularly after the
30 1996 hearing, and this was dealt with, I think, by the
31 appointment at the time of Mr. Bill Finn, but I guess not
32 everyone is willing to serve. That's the other point of that,
33 but all counsel, I'm sure, professionally would want to
34 assist the Board. We want to assist you in every way.
35 We're not here to put one over on you, and when you have
36 consent of counsel, which is very difficult to get at any
37 particular time, I've found, when you have consent on a
38 procedural matter, such as the one which you've indicated
39 previously that you were willing to deal with, that's a good
40 signal, I think, that people are trying to assist in reference
41 to a particular matter, that people see a particular problem.
42 In this hearing where you have so many counsel, I think
43 your procedures should be very, very tight. So we're all
44 here to assist you in any way we can, as it is our function
45 to help create the body of evidence, as it's yours to
46 evaluate that and rule upon it.

47 I would like to thank Newfoundland Hydro,
48 particularly Maureen Greene. We have had very refreshing
49 communications from time to time. All our information
50 requests have been dealt with satisfactorily by
51 Newfoundland Hydro. It's a refreshing approach. We also
52 acknowledge the assistance of Mr. Terry O'Reilly. We were
53 unable to put our information requests in the format

54 requested by the Board, because we had, our computers are
55 not, were not geared for that, but we've sent them in a
56 different form and he has given us some advice as to how
57 to deal with that and has given us some assistance there
58 over the last few days. A lot of law firms have a budget.
59 They have a budget for computers, they have a budget for
60 this, they have a budget for that, and computers we're all
61 getting dinged with all of the time ... upgrade, do this, do
62 that, so some firms such as our own have frozen costs
63 related to computers while they're paying off existing loans.
64 It's as simple as that, so it's not that we were trying to be
65 difficult in that particular respect.

66 We look forward to this hearing. We look forward
67 to presenting our evidence, and we thank you for providing
68 us with this opportunity of an opening comment, thank you
69 very much.

70 MR. NOSEWORTHY, CHAIRPERSON: Thank you, Mr.
71 Browne. I'd like to move now to Mr. Hearn, Labrador City,
72 please?

73 MR. HEARN, Q.C.: Thank you, Mr. Chairman. Mr.
74 Chairman, Commissioners, I am appearing on behalf of the
75 Town of Labrador City for these hearings. We have a
76 somewhat minor role in this whole process, and we hope to
77 make our submission focused on the role that's limited to
78 the issues that affect the Labrador Interconnected system.
79 It is our view that there are sound historical reasons for
80 having different rates, even within the Labrador
81 Interconnected system for the Labrador City/Wabush area
82 and that there are also significant cost distribution
83 differences that warrant different rates within that system.

84 We will address this issue during the, principally
85 during the cost of service phase of the hearing and we
86 intend to call one expert in relation to the issues that we will
87 be addressing. We have pre-filed the evidence of Mark
88 Drayson (*phonetic*), a consultant in the field of public
89 utility economics with offices in Calgary and St. Louis.

90 In addition, Mr. Chairman, we would also like to
91 put on the record that we support the position of the
92 Consumer Advocate with respect to the rural rate subsidy
93 and for review of electrical policy within the province. It is
94 our view, as stated by the Consumer Advocate in some of
95 the pre-filed evidence, that the rural rate subsidy is more in
96 the nature of a tax and therefore more appropriately and
97 more efficiently accomplished by government legislation
98 directly, rather than imposed on domestic ratepayers. For
99 example, the province has the legislative option, if we were
100 to utilize the authority conferred by Section 92(a) of the
101 Canadian Constitution, to include Churchill Falls within
102 such a rate base, and thereby minimize the impact on
103 domestic ratepayers.

104 We would also point out that in this process we

1 have engaged effectively all of the collective wisdom,
 2 expertise, and experience of all those engaged in the
 3 electrical sector or electrical policy within the province, and
 4 it seems clear from, again, looking at Sectio 92(a) of the
 5 Canadian Constitution that the province has significant
 6 and non-utilized authority to alter the sale price of energy
 7 produced at Churchill Falls and to tax such output. It
 8 seems to me shortsighted to engage in such a wide and
 9 expansive hearing as this and not to give some
 10 consideration to those options since I think they can
 11 impact, not only on the financial integrity of the province,
 12 but also the financial integrity of Hydro and its necessity
 13 for funds from domestic ratepayers.

14 Those are all the submissions that we intend to
 15 make at the present time, Mr. Chairman, and since our role
 16 is limited we would not be present during most of the
 17 hearing. We intend to be monitoring, getting the daily
 18 transcripts, and when there is something that involves
 19 issues that affect the Labrador Interconnected system, we
 20 would expect to be present during that period of time,
 21 during principally the cost of service phase, which we
 22 anticipate to be in November. Thank you.

23 MR. NOSEWORTHY, CHAIRPERSON: Thank you very
 24 much. Probably just one comment is warranted in respect
 25 of Mr. Browne's earlier remarks. I, for one, facing nine or
 26 ten lawyers out there would have loved to have a lawyer on
 27 the Board quite frankly, given that this is my first hearing.
 28 Unfortunately both lawyers on the Board, including Mr.
 29 Finn, have relatively small law practices and they are part-
 30 time commissioners and certainly in such a lengthy hearing,
 31 were not able to serve. I would have certainly liked that, to
 32 see them serve on the panel, but I certainly understand the
 33 position they were in. Nevertheless, we had to move
 34 ahead. I think my colleagues may know a little bit more
 35 about administrative law than I, but I'm sure I will learn over
 36 the next several weeks as much as I need to know. It is an
 37 issue for the Board, quite frankly, looking ahead at such a
 38 large hearing that I would like to address some way, shape,
 39 or form, of ensuring that a lawyer would serve on the panel,
 40 and I plan to address that, but unfortunately it's not, we're
 41 not in a position to do that for this hearing.

42 Anyway, I thought I'd just like to comment on that
 43 for clarification as to why we don't at this point in time have
 44 a lawyer on the Board. Moving along, based on the
 45 agenda that we would have, or I would have outlined this
 46 morning, the next part of that agenda is really the
 47 presentation of Hydro's case, and I would ask Hydro's
 48 counsel if they are prepared to proceed with the first
 49 witness?

50 MS. GREENE, Q.C.: Yes, Mr. Chair, we are. As I indicated
 51 earlier, our first witness is Mr. William Wells, the President
 52 and Chief Executive Officer.

53 MR. NOSEWORTHY, CHAIRPERSON: If I could ask Mr.
 54 Wells to step forward and take the seat reserved at the
 55 witness table please? I'd like to welcome you, Mr. Wells.
 56 Could you take the Bible in your right hand please? Do
 57 you swear on this Bible that the evidence to be given by
 58 you shall be the truth, the whole truth, and nothing but the
 59 truth, so help you God?

60 MR. WELLS: I do.

61 **MR. WILLIAM WELLS, SWORN, X'D BY MS. GREENE,**
 62 **Q.C.**

63 MR. NOSEWORTHY, CHAIRPERSON: Thank you very
 64 much. You may proceed, Ms. Greene.

65 MS. GREENE, Q.C.: I'll just give Mr. Wells a moment to get
 66 ready there.

67 MR. NOSEWORTHY, CHAIRPERSON: Absolutely.

68 MS. GREENE, Q.C.: Mr. Wells, evidence was filed in your
 69 name with Hydro's pre-filed testimony on May 31st, 2001.
 70 Do you adopt the pre-filed evidence under your name as
 71 your evidence for the purpose of this hearing?

72 MR. WELLS: I do.

73 MS. GREENE, Q.C.: Do you have any additional comments
 74 that you would like to make to the Board and to the parties
 75 present today at this time?

76 MR. WELLS: Yes, I'd like to have an opening statement
 77 and I will confine my remarks to the statement and not to
 78 argument. Good morning, Chairman, or good afternoon
 79 now, and Commissioners, and ladies and gentlemen.
 80 Newfoundland and Labrador Hydro has not appeared
 81 before the Public Utilities Board on a general rate
 82 application since 1992. Since then Hydro's performance
 83 has been consistent with its mandate to provide reliable
 84 electrical power and energy at least cost. Hydro's
 85 customers have had the benefit of stable electricity rates,
 86 stable or declining real costs, and the benefits of a
 87 substantially improved system resulting from millions of
 88 dollars in capital expenditures. This has resulted in
 89 increased efficiencies in production and system
 90 improvements in transmission and distribution. Hydro's
 91 principal customer, Newfoundland Power, has not been
 92 subject to a rate increase since 1990, and our industrial
 93 customers currently have the benefit of the lowest
 94 industrial rates in Atlantic Canada.

95 The decade of the nineties has been a difficult and
 96 challenging economic period. Restraint, cost cutting, and
 97 reorganization have been constant throughout most of the
 98 decade. As well, Hydro has had to deal with the challenges
 99 resulting from the impact of technological change and the
 100 emergence of new public attitudes and expectations related
 101 to such issues as the reliability of service and

1 environmental performance.

2 The issues pertinent to this application arise from
3 a number of factors including the fluctuation in fuel prices
4 on a global scale, legislative requirements, Public Utility
5 Board's inquiries and studies, and the normal application of
6 regulatory requirements. The issues may be broadly
7 divided into categories. Costs, and as well the transfer of
8 costs and the allocation of costs respecting the rural
9 deficit. Rate issues per se, including preferential rates and
10 rate classes. For example, the Labrador Interconnected
11 system. Hydro's revenue requirement, and a determination
12 of the rate base and the appropriate return on rate base, and
13 Hydro's capital program for 2002, the test year. There is
14 one overriding fact with respect to costs in operating the
15 island system, and that is the price of Number 6 fuel. Fuel
16 costs are the principal driver of the rate increases proposed
17 by Hydro. The Holyrood thermal plant, dependent on
18 variations on hydrology and consumption, may consume
19 between 1,500,000 and 5,000,000 barrels of oil in a year to
20 meet system requirements. The forecast for 2002 is
21 3,500,000 barrels.

22 Hydro's rates are currently based on a price of
23 \$12.50 per barrel. The reality over the past year and a half
24 have been prices in excess of \$30.00 per barrel. The
25 forecast price for fuel, even in the most optimistic case is
26 mid to high twenties, and since the events of September the
27 11th, any forecast with respect to fuel prices is inherently
28 problematic.

29 No one should have any difficulty in accepting
30 the fact that a more realistic fuel price for Number 6 fuel
31 should be imbedded in Hydro's base rates. The price of
32 \$12.50 per barrel for Number 6 fuel currently in Hydro's
33 rates is less than half of the current price. The difference
34 between the prices paid and what is charged in Hydro's
35 rates is deferred to the Rate Stabilization Plan which is
36 forecast to exceed before the end of this year, the \$50
37 million cap set by the Board with respect to Newfoundland
38 Power.

39 The Rate Stabilization Plan has worked effectively
40 since its inception in stabilizing customers' bills and in
41 reducing the immediate impact of variations in fuel prices.
42 We have been fortunate in past years in having higher than
43 average inflows to Hydro's reservoirs which assisted in
44 reducing the amounts charged to the Rate Stabilization
45 Plan. I should also note that approximately two years ago
46 the price of fuel dipped below \$12.00 per barrel for one brief
47 period, and the generally lower prices at that time had a
48 very positive influence on the balance outstanding in the
49 Rate Stabilization Plan for both Newfoundland Power and
50 our industrial customers.

51 The Rate Stabilization Plan cannot operate

52 effectively as it was designed to do when there are huge
53 differences between the prices actually paid for Number 6
54 fuel, and the price set in base rates. In the current situation
55 and in order to reduce the impact on customer rates, Hydro
56 is proposing a two pronged approach. First of all,
57 increasing the fuel prices in Hydro's rates allows the plan
58 to work more effectively as it was originally designed to do
59 in decreasing the variations in customers' bills as a result of
60 the variability in fuel prices.

61 Second, increasing the cap from \$50 million to \$100
62 million assists in partially offsetting the immediate impact
63 of higher costs for ratepayers. I urge caution in any
64 approach that would change the concept of the plan or any
65 move to dispense with it. The fact is that on the island
66 portion of the province, our dependence on thermal power
67 is a reality and it must be accepted. It now accounts for
68 approximately 30 percent of our energy production on an
69 annual basis. The costs related to our Holyrood thermal
70 plant relate almost totally to the price for, and the
71 consumption of, Number 6 fuel. It is also a fact that on the
72 island portion of this province, that our competitive rates
73 within the Canadian and North American context are being
74 eroded by the impact of rising fuel prices and the costs
75 associated with the provision of additional capacity to meet
76 the system demand. Additional low cost hydro power on
77 the island is just not available to meet future requirements.

78 The rates proposed by Hydro as a result of this
79 application are as low as they could reasonably be in the
80 current circumstances, and they should be assessed from
81 two aspects. First the beneficial results to ratepayers over
82 the past ten years and second, the reality of the current
83 cost requirements of the system. In that context, the 6.7
84 percent increase proposed for Newfoundland Power, and
85 the resulting 3.7 percent increase to end-consumers are
86 really modest increases which offset the cost of fuel and
87 transfer a portion of the cost from the Rate Stabilization
88 Plan to Hydro's rates. Industrial customers will have their
89 rates increased by approximately 10.4 percent.

90 Should Hydro's proposal be accepted by the
91 Board, the rate reductions that our industrial customers
92 have received since 1992 result in their actually having to
93 pay approximately 3.5 percent more for their power and
94 energy received from Hydro in 2002 than they did in 1992.

95 There has also been comment that the increases
96 proposed in Hydro's rates are in addition to the
97 approximately six to seven percent increase in rates which
98 will result from the application of the Rate Stabilization Plan
99 in 2002. The outstanding balances in the Rate Stabilization
100 Plan confirm the fact that the real issue with respect to the
101 costs incurred in the system and the resulting impact on
102 the rates is the high cost of Number 6 fuel.

1 Hydro has no control over fuel prices, but it can
2 be justifiably proud of the management of the system
3 which has ensured that generation requirements were met
4 with the least amount of fuel consumption possible. The
5 increase in the rates proposed by Hydro in the proposal
6 with respect to an increase in the cap in the Rate
7 Stabilization Plan, as well as the balances that will be
8 outstanding in the Rate Stabilization Plan as of December
9 the 31st this year, all relate to one factor, the price of
10 Number 6 fuel.

11 Hydro's approach to the rate issues is to reduce
12 the impact of rate increases on customers while laying a
13 foundation for rate equity amongst all ratepayers. With
14 some patience, perseverance, and good fortune, we may be
15 able to absorb the shock of continuing higher oil prices
16 within the system and allow for a period of adjustment for
17 all ratepayers to accommodate their particular rate increase.

18 Hydro provides an essential service to all
19 Newfoundlanders and Labradorians. It is important that
20 Hydro be regarded as a commercial entity and that it be
21 kept on a sound financial footing in its own right. During
22 the course of this hearing we will be examining its capital
23 structure and operating requirements. Again, you will find
24 Hydro proposing innovative means to provide a solid
25 foundation for the future while minimizing the impact on
26 ratepayers. In order to reduce the rate impact on its
27 customers, Hydro is proposing in the short term a nominal
28 return on equity or rate base, provided that the normal and
29 appropriate return on equity for Hydro is clearly expressed
30 by the Board in its final decision. It is important that
31 everyone understand the basis upon which Hydro's capital
32 structure and financial operations will be founded in the
33 longer term. In the provision of an essential service,
34 predictability is all important and to the extent that the
35 situation is governable, we should ensure the removal of
36 uncertainties.

37 The regulatory process in the absence of
38 competition is intended to ensure that Hydro is held
39 accountable for the actions that it undertakes in pursuit of
40 its mandate. Unfortunately the overriding issue affecting
41 the rate increases proposed in this application relate to
42 those matters over which Hydro has no control, or at least
43 very little control. In matters over which Hydro does have
44 control, it is to be expected that we will be subject to a
45 critical review, the result of which should better enable
46 Hydro to meet its mandate and commitment to provide
47 reliable least-cost power.

48 One cannot embark on this process without
49 commenting on the cost of the process and the process
50 itself. This hearing is expected to continue for months, not
51 weeks. Hydro has answered all the requests for
52 information and stands ready to facilitate the process in

53 any way it can, to better enable an understanding by all of
54 the concerned parties of the facts underlying the provision
55 of electrical services in this province and Hydro's role in
56 that endeavour. It is recognized that intervenors,
57 customers, and the people have a right to be heard.
58 However, there is a challenge for everyone involved to do
59 the right thing to assist the Board in bringing these
60 proceedings to a timely conclusion. As part of the
61 regulatory process, this hearing will cost millions of dollars,
62 a significant amount of money related to the size of this
63 jurisdiction. That is why it is so important that everyone
64 involved be conscious of the fact that the object of the
65 exercise is to ensure least-cost rates to consumers.

66 Finally, the Board has to make its decision based
67 on the facts and the merits of the case. It must apply
68 regulatory principals and practices to the fact situation.
69 The Applicant, as well as the intervenors, to a certain
70 extent represent vested interests, and not necessarily the
71 interests of the whole of the power system of the province.
72 The Board will take the larger view of the total system and
73 weigh the overall benefits against any particular perceived
74 disadvantage. On behalf of Hydro and all of its dedicated
75 employees and our witnesses at this hearing, I pledge our
76 total commitment to this process, and that everyone
77 involved will be dealt with in an open, honest, and
78 forthright manner, to the best of our ability. Thank you.

79 MR. NOSEWORTHY, CHAIRPERSON: Thank you very
80 much for your opening statement, Mr. Wells. Ms. Greene?

81 MS. GREENE, Q.C.: Mr. Wells, does that conclude your
82 testimony at this time?

83 MR. WELLS: It does.

84 MS. GREENE, Q.C.: Mr. Chair, I have copies of Mr. Wells'
85 opening statement that I can distribute at this time so the
86 parties would have the opportunity over lunch to review
87 those. As I indicted earlier, it is our view there is no new
88 evidence filed in the opening statement, but it's a general
89 overview of our approach to the hearing, so I do have
90 copies that are available to be distributed now.

91 MR. NOSEWORTHY, CHAIRPERSON: Is it your intention
92 to proceed now with the questioning?

93 MS. GREENE, Q.C.: Mr. Chair, I am finished with the direct
94 examination of Mr. Wells, and at this point he would be
95 available for cross-examination from Newfoundland Power.

96 MR. NOSEWORTHY, CHAIRPERSON: Okay.

97 MS. GREENE, Q.C.: I don't know if this is a good time to
98 break now.

99 MR. NOSEWORTHY, CHAIRPERSON: Well, I think it
100 probably would be. We have less than ten minutes left,
101 and rather than perhaps begin now, we'll break for lunch

1 and we'll reconvene at 2:00. Thank you.

2 (break)

3 MR. NOSEWORTHY, CHAIRPERSON: Good afternoon.
4 Hopefully everybody had an enjoyable lunch. Over the
5 lunch hour the Board would have issued PU-23 of
6 2001/2002 which should address the specific requirements
7 contained in the Consumer Advocate's motion this morning
8 on redirect. In addition, I would draw your attention to two
9 other items. One, I did mention this morning in my opening
10 remarks, being that December 1st was indeed a Saturday, or
11 is a Saturday, and that would be a non-hearing day despite
12 it being mentioned, I think, in a reference in PU-18, so that's
13 been deleted, and contrary to what I had indicated this
14 morning, apparently the Labrador Inn in Goose Bay has
15 come back and indicated that they don't have sufficient
16 room available for us to undertake the hearing there, or the
17 room they have is unavailable, excuse me, and we will have
18 to look for another location which we will do as quickly as
19 possible and advise everybody accordingly, so I trust
20 that's satisfactory. We will proceed on now. Hydro would
21 have concluded the direct evidence from Mr. Wells this
22 morning, and we will begin with Newfoundland Power's
23 cross. Ms. Butler?

24 MS. BUTLER, Q.C.: Thank you, Mr. Chairman. I'm going
25 to be using information that has been pre-filed and stored
26 electronically to a large degree, so I guess we're all going to
27 very quickly get used to the system that's in front of us. I'd
28 ask Mr. O'Reilly first if we could have a look at IC-98. Mr.
29 Wells, in this question posed by the Industrial Customers,
30 Hydro was asked for 2002 cost of service, and if we could
31 just have a glance at the answer that was given, which I
32 think you have on your screen there, and which indicated
33 that the merging of some 2004 operation and financial data
34 with 2002 base data would not produce meaningful results.
35 A more reflective estimate is contained in the attached five
36 year plan. Can we look to page 2 of 11 to see the five year
37 plan? Okay, and if we could just go back to the cover
38 there, Mr. O'Reilly, and Mr. Wells can I ask you first, are
39 you familiar with this Newfoundland and Labrador Hydro
40 financial plan covering the period 2001 to 2005?

41 MR. WELLS: Somewhat.

42 MS. BUTLER, Q.C.: And can you tell us whether this
43 financial plan was actually approved by Hydro's board of
44 directors, or whether it was developed for the purposes of
45 this application only in answer to Industrial Customers'
46 question 98?

47 MR. WELLS: It wasn't developed specifically for this
48 hearing. Is that what you mean?

49 MS. BUTLER, Q.C.: Yes, was it approved by Hydro's board
50 of directors, Mr. Wells?

51 MR. WELLS: I think so, yes, because ... well we do a five
52 year ... it's a rolling average. We take off one year and add
53 another, so in each year we're doing a five year financial
54 plan.

55 MS. BUTLER, Q.C.: I wonder if we could look at the
56 executive summary of it which should be Roman numerals,
57 page iv, Roman numerals, four, and we'll have to enlarge
58 that, Mr. O'Reilly. Mr. Wells, I wonder if you would be kind
59 enough please to read for us under the reference to the
60 highlights are ...

61 MR. WELLS: The year 2001 is based on forecast results.

62 MS. BUTLER, Q.C.: I'm sorry, Mr. Wells, I've mislead you.
63 Can we scroll down, Mr. O'Reilly, please. There's a line
64 above this ... no, I'm sorry, scroll the other way. There's a
65 line above "the highlights are". Thank you. Can you just
66 read the opening statement under Executive Summary for
67 us?

68 MR. WELLS: Yes, this document outlines Newfoundland
69 and Labrador Hydro's financial plan for 2001 to 2005.

70 MS. BUTLER, Q.C.: Okay, thanks, and then to the very last
71 bullet at the bottom of the page, can you read that for me?

72 MR. WELLS: Excluding the effects of the Rate Stabilization
73 Plan, wholesale rates to Newfoundland Power and Island
74 Industrial rates are projected to an increase at an annual
75 compound rate of four percent over the planning period.

76 MS. BUTLER, Q.C.: Now combining those two statements
77 together, Mr. Wells, can I take it then that Hydro's plan,
78 financial plan, is to increase rates by an annual compound
79 rate of four percent over the period 2001 to 2005?

80 MR. WELLS: In the context of that's the financial plan, yes.
81 For financial planning purposes, not for setting of rates.

82 MS. BUTLER, Q.C.: For financial planning purposes.

83 MR. WELLS: Uh hum.

84 MS. BUTLER, Q.C.: And this relates primarily, I'm relying
85 on the evidence you have pre-filed and in your opening
86 statement this morning, to the price of Number 6 fuel?

87 MR. WELLS: No, there'd be a number of components that
88 they would have forecast would be in the cost base going
89 over time, and you predict, well we're talking about a
90 forecast in any event, but if there were additions to
91 generation capacity of the capital program and other things
92 that were, that would be put into the run for each particular
93 year in the five year period.

94 MS. BUTLER, Q.C.: Would it be fair to say that ...

95 MR. WELLS: And including the price of Number 6 fuel,
96 yes.

1 MS. BUTLER, Q.C.: That would be a significant element of
2 it?

3 MR. WELLS: Uh hum.

4 MS. BUTLER, Q.C.: Okay, now I wonder, can we look at
5 page 14 of the document which has a table, and this is a
6 revised table, so I want to make sure we hit the right one.
7 Thank you. I'll just give you a moment, Mr. Wells, to
8 familiarize yourself with that Table 8. Does this table
9 suggest that it is Hydro's plan to increase its rates in the
10 period 2001 to 2005 before the effects of the Rate
11 Stabilization Plan by 22 percent, and I take that to be 55.1
12 shown in column 2005, over 45 shown in the column 2001.

13 MR. WELLS: And you said the percentage was?

14 MS. BUTLER, Q.C.: 22 percent. I'm sorry?

15 MR. WELLS: You asked me if it were 22 percent.

16 MS. BUTLER, Q.C.: Well, I can give you the calculations
17 ...

18 MR. WELLS: I didn't do the calculation here but ...

19 MS. BUTLER, Q.C.: That's fine. If you'll accept my math
20 on it for the moment.

21 MR. WELLS: Uh hum.

22 MS. BUTLER, Q.C.: Does this table contained in your
23 financial report suggest that the plan in this period is to
24 increase the wholesale rate from the 2001 figure shown as
25 45 to the 2005 figure shown, which is 55, which I calculate
26 is an increase of 22 percent?

27 MR. WELLS: Based on the assumptions within the
28 financial planning plan, then that's what, obviously what ...
29 the figures are part of the plan, yes.

30 MS. BUTLER, Q.C.: Thank you, and after adjustment for
31 the Rate Stabilization Plan, using the same figures, the plan
32 is to increase the wholesale rate from 46.7 to 58.9 which I
33 calculate at 26 percent. Is that also correct?

34 MR. WELLS: I'll accept that, yes.

35 MS. BUTLER, Q.C.: So perhaps this is the message, Mr.
36 Wells, that the Newfoundland consumers need to hear first,
37 that the plan in this period, 2001 to 2005, is to increase
38 those wholesale rates by 22 and 26 percent respectively in
39 that four year period. Are you satisfied, Mr. Wells, as
40 President, that Hydro has done all it can to keep rate
41 increases as low as possible in the period covered by your
42 financial plan?

43 MR. WELLS: May I say this? That the financial plan that
44 we maintain, and it's required in the system, although I
45 personally have a great deal of difficulty with five year
46 plans in this day and age, is done for financial planning

47 purposes only. It's not to set rates and I would be very
48 uncomfortable to take the projections in the financial plan
49 and take them out to consumers as some sort of forecast
50 that this is what you can expect. But the only way we can
51 prepare a financial plan over a five year period is to make
52 certain assumptions and then the math with all the
53 components of the plan, as obviously you've seen, gives
54 you certain results, but again, I stress that this is not the
55 basis on which you would set rates. It's a forecast of
56 financial requirements based on the assumptions of the
57 day, and they will change in 2002 and the next five year
58 plan will have something in it that may be quite different.

59 MS. BUTLER, Q.C.: Well, I'll come back and readdress the
60 question, but I want you to remember that this plan was
61 provided in response to the question for your 2002 cost of
62 service, and the answer that was given was that the most
63 reflective estimate of that was in this financial report.

64 MR. WELLS: That was the only thing available to show
65 you. I forget the question now, your original one, but the,
66 what was shared with you was all that we had available in
67 projections going forward, and assumptions that were
68 made as opposed to the cost of service study.

69 MS. BUTLER, Q.C.: Correct. I guess my point is only that
70 since this is what was provided, and since I'm asking you
71 questions about the documents provided by Hydro in
72 answer to that question. Are you satisfied as President
73 that this financial plan does reflect an attempt to keep rate
74 increases as low as possible in that period?

75 MR. WELLS: Well that's certainly Hydro's objective as
76 you can see by our application, yes.

77 MS. BUTLER, Q.C.: I take that as a yes? Sorry?

78 MR. WELLS: That's Hydro's whole objective, is to try to
79 minimize the impact of rate increases over a period of time.

80 MS. BUTLER, Q.C.: I accept that that's Hydro's objective,
81 but I'm asking you personally if you're satisfied as
82 President that every effort was done in the preparation of
83 this financial plan?

84 MR. WELLS: Because ... yes, well to the extent that these
85 plans are prepared based on assumptions and you're
86 bringing the whole of the operation into some kind of a
87 focus, but there's so many assumptions and each year as
88 you go out further, then they become less and less reliable,
89 and again, I say that this is not the real focus when you
90 discuss things with Hydro with respect to rates, but I
91 suspect that it was the only document that we could
92 provide in answer to the question about the cost of service
93 for 2002.

94 MS. BUTLER, Q.C.: I'll move then if I can back to the
95 Roman numerals, page four of the revised answer, Mr.

1 O'Reilly please, and turning now for the moment to
2 operating expenses. I wonder, could you read the seventh
3 bullet there please?

4 MR. WELLS: Other than exceptional items operating and
5 maintenance expenses are predicted to increase by the rate
6 of inflation after 2002.

7 MS. BUTLER, Q.C.: Okay, so again, with the planning
8 period, 2001 to 2005, Hydro's financial plan is suggesting
9 that operating and maintenance expenses will increase at
10 the rate of inflation after 2002?

11 MR. WELLS: That was the assumption used to complete
12 that aspect of the plan.

13 MS. BUTLER, Q.C.: Okay, now what you're addressing
14 here are costs, operating and maintenance expenses, which
15 I believe you referred to in your evidence pre-filed as those
16 that are controllable, is that correct?

17 MR. WELLS: In my pre-filed ... in my statement?

18 MS. BUTLER, Q.C.: Pre-filed evidence, yes. Are operating
19 and maintenance expenses those that you deal with as the
20 controllable type of expenses as opposed to the fixed type
21 of expenses?

22 MR. WELLS: To a certain extent, but I'm not sure if I can
23 say that that includes every expense that would fall in that
24 category.

25 MS. BUTLER, Q.C.: Well ...

26 MR. WELLS: Certain operating expenses, I'm not sure that
27 we can control them.

28 MS. BUTLER, Q.C.: Okay.

29 MR. WELLS: But we just used the rate of inflation as the
30 basis for an assumption to be able to adjust the figures
31 over that period of time you're forecasting.

32 MS. BUTLER, Q.C.: Alright, is it fair to say, Mr. Wells, that
33 operating and maintenance expenses do differ from fixed
34 expenses such as the price of fuel?

35 MR. WELLS: That would not be included in that.

36 MS. BUTLER, Q.C.: Yes, correct, so we're talking about
37 expenses here over which Hydro has some element of
38 control?

39 MR. WELLS: For the purpose of the proceeding, let's
40 assume that, yes.

41 MS. BUTLER, Q.C.: Okay, great, for example, travel or
42 conferences.

43 MR. WELLS: Obviously.

44 MS. BUTLER, Q.C.: Okay, now looking, if we might, to
45 page two of three. Sorry, I'm sorry, Mr. Wells, I've misled

46 you here. One second. I'm sorry, Mr. O'Reilly, I went a
47 little too far ahead. Mr. Wells, back to the entry that we
48 were just discussing in terms of operating and maintenance
49 expenses. The prediction or forecast assumption that was
50 used was that these would increase at the rate of inflation
51 after 2002. Can I ask you, given the size of the rate increase
52 that we saw referred to in the financial plan a moment ago,
53 that was 22 percent over the period 2001 to 2005, before
54 effects of the RSP and 26 percent after, are you satisfied
55 that Hydro is doing enough to influence its controllable
56 expenses in the same period?

57 MR. WELLS: Yes, I am, and I'm sure that we will continue
58 to do so over that time (inaudible) having been tested for
59 the 2003/2004 period yet, but the issue of being
60 accountable for what we can control in trying to reduce
61 expenses, it never leaves us, it's a constant.

62 MS. BUTLER, Q.C.: I'm going to ask Mr. O'Reilly now if we
63 can have a look at NP-3, which I believe are Hydro's
64 revenue requirements from '92 to 2002. You'll see there on
65 your screen, Mr. Wells, Hydro was asked to provide details
66 of the revenue requirements for each of those ten years and
67 they are attached at page two of three.

68 MR. WELLS: I've got these damned continuous bifocals.
69 I'm having a bit of a problem here ... and age. I'm sorry,
70 your question?

71 MS. BUTLER, Q.C.: I'm going to get Mr. O'Reilly now to
72 put up page two of three for you, and Mr. O'Reilly, for the
73 benefit of those of us who are trying to read this and get it
74 enlarged, it's line 17. There you go. Now at line 17 of this
75 document we'll see a reference to other costs, from 18 to 28
76 you'll see the subsections of those other costs referred to,
77 and they include things such as travel and conferences,
78 etcetera. Are these the same operating and maintenance
79 costs which were referred to in your financial plan a
80 moment ago, indicated to ...

81 MR. WELLS: Yeah, it's ...

82 MS. BUTLER, Q.C.: Increased at the rate of inflation for the
83 years 2001 ... I'm sorry, after 2002?

84 MR. WELLS: Yes, in the absence of looking at the plan,
85 you know, in front of me, the question is what is the
86 assumptions that were used going through, you know, the
87 piece. Actually these are back, you're going back, aren't
88 you? Yeah.

89 MS. BUTLER, Q.C.: No, no, I wasn't going to ask you
90 about the assumptions used. I just want to make sure that
91 we're talking about an apple, and comparing it to an apple.
92 When we say other costs here, and you can see what kind
93 of other costs ...

94 MR. WELLS: These are all, this is what we refer to as the

1 30 percent of our controllable ...

2 MS. BUTLER, Q.C.: Yes.

3 MR. WELLS: Yeah, costs or ...

4 MS. BUTLER, Q.C.: Operation and maintenance.

5 MR. WELLS: Yeah, these are the ... the salaries and fringe
6 benefits, and system/equipment maintenance are the bulk
7 of the costs over which we have some control.

8 MS. BUTLER, Q.C.: And these are the costs over which
9 the plan suggested were forecast to increase by the rate of
10 inflation after 2002.

11 MR. WELLS: Yes.

12 MS. BUTLER, Q.C.: And these are costs, we can look at
13 them here on the screen, which ... correct me if I'm wrong,
14 but should not be materially affected by the cost of Number
15 6 fuel.

16 MR. WELLS: No, that's correct.

17 MR. NOSEWORTHY, CHAIRPERSON: Excuse me, Mr.
18 Wells. Would it be of any help if the monitor was moved
19 closer. It will come out of that seat and it can be rested on
20 the top of the desk. Would that be of any benefit or
21 advantage?

22 MR. WELLS: I'm getting used to it.

23 MR. NOSEWORTHY, CHAIRPERSON: Well, if that will be
24 of any benefit we can move it.

25 MS. BUTLER, Q.C.: Can we look at the column on page
26 two of three, which has as its heading, 1997, please? Okay,
27 in 1997, Mr. Wells, these other costs totalled \$83.421
28 million, am I correct?

29 MR. WELLS: That's right.

30 MS. BUTLER, Q.C.: For the 2002 test year we're going to
31 have to go to page three, Mr. O'Reilly, line 17. I'm sorry, it's
32 not line 17, is it? My figure is 97.394. Is that correct?

33 MR. WELLS: Uh hum.

34 MS. BUTLER, Q.C.: Okay, there's a forecast increase then
35 from 1997 to 2002 for the operating and maintenance cost
36 you described as controllable, of approximately \$14 million,
37 is that correct?

38 MR. WELLS: That's the difference between the 2001 figure
39 and the ...

40 MS. BUTLER, Q.C.: Sorry, 2002.

41 MR. WELLS: And ...

42 MS. BUTLER, Q.C.: And 1997.

43 MR. WELLS: No, that can't be right. I thought you
44 mentioned the figure of 83.421.

45 MS. BUTLER, Q.C.: I did.

46 MR. WELLS: Which is the year ...

47 MS. BUTLER, Q.C.: 1997.

48 MR. WELLS: Yeah.

49 MS. BUTLER, Q.C.: Unfortunately we can't get them both
50 on the same ...

51 MR. WELLS: Would it be more helpful to us and expedite
52 the thing if I could actually dig out the financial plan?

53 MS. BUTLER, Q.C.: The hard copy, yeah.

54 MR. WELLS: Which is in IC ...

55 MS. BUTLER, Q.C.: IC-98. Cheryl, he will also need NP-3
56 though. Mr. Wells, to assist you for the moment, the one
57 that's on the screen is NP-3, not IC-98. Page 2 of 3, and 3 of
58 3.

59 MR. WELLS: Anyway, the point that we're trying to get to
60 is that in 1997 the balance was \$83 million, and in 2002 it's
61 forecast to be 97.

62 MS. BUTLER, Q.C.: 97.4, a difference of \$14 million in that
63 five year period.

64 MR. WELLS: Yes, okay, yeah.

65 MS. BUTLER, Q.C.: Okay, thank you. In your testimony
66 generally, that's the pre-filed testimony revised, Mr. Wells,
67 you spoke to us generally about the initiatives that Hydro
68 had taken to control or reduce expenses such as the
69 operating and maintenance, those controllable expenses.
70 Do you agree generally that your evidence spoke about
71 that?

72 MR. WELLS: Yes.

73 MS. BUTLER, Q.C.: Alright, despite these initiatives, it
74 seems to me, looking at the figures I've just referred you to,
75 that there's a growth of \$14 million forecast, because I agree
76 we're looking into 2002, over a five year period in expenses
77 which you agree are controllable. My question to you, as
78 President of Hydro, is whether you are satisfied that Hydro
79 has done everything possible to keep these operating and
80 maintenance expenses as low as possible, between '97 and
81 2000, which are the years we have complete figures on, and
82 to keep the forecast as low as possible for 2001 and 2002?

83 MR. WELLS: Well, I can ... the big items here that are in
84 those figures to which you refer are salaries and fringe
85 benefits and systems, equipment maintenance, and coming
86 back to system, equipment and maintenance, if you go
87 back, and you can go back here to figures back to 1992, and
88 see the range of what is happening with respect to system,
89 equipment and maintenance, and it varies, but the trends

1 laterally, if you look at the 2000 figures, 2001, and 2002 are
2 a little higher on average than those that have occurred
3 previously, and system, equipment and maintenance
4 logically in an aging, with plan ... you know, just the issue
5 of the number of things that you require to maintain the
6 system and as age is a factor here, and costs, you would
7 expect that to go up. The projections are only projections,
8 but the effort ... and in terms of controllability, if we find out
9 that we have something with respect to our systems that is
10 an essential, that it must be there to maintain the reliability
11 of service, to maintain the service, then we don't have much
12 choice when you say that are these categories that are
13 options that we can exercise choice. We can make some
14 value judgements between one expenditure and another,
15 but in the end there are elements in those expenditures that
16 are not a matter of choice. They're a matter of necessity,
17 and that figure which is a matter of discussion within
18 Hydro is, and amongst management of Hydro, it's not, it's
19 not something over which we can say for sure that we can
20 control precisely, but we do exercise a great deal of
21 judgement with respect to that, and that's one of the
22 difficulties when you sort of ask me for a black and white
23 answer in matters of choice. Now if we come to salaries
24 and fringe benefits, one could say that management has
25 some choice or some option and to an extent we do have,
26 and to that extent we do exercise control over salaries and
27 fringe benefits, but it's not a unilateral decision by any
28 respect, and mindful of the fact that we have bargaining
29 units and we bargain wages and salaries, and we have
30 other actions that we've taken with respect to that issue to
31 keep those costs down.

32 MS. BUTLER, Q.C.: Mr. Wells, can I just go back to the
33 question though, because I've listened carefully to your
34 answer, and I accept that there are judgements to be
35 exercised and choices to be made, but what I had asked
36 you whether you were personally satisfied that Hydro had
37 done everything it could to keep these costs, the operating
38 and maintenance costs, as low as possible between '97 and
39 2000?

40 MR. WELLS: Yes.

41 MS. BUTLER, Q.C.: And can I ask you then, are you
42 satisfied that it's doing all that it can to ensure that the
43 same category of costs is kept as low as possible for
44 forecast 2001 and 2?

45 MR. WELLS: Yes.

46 MS. BUTLER, Q.C.: Thank you. Because you see Hydro
47 is looking for \$18 million on this application, and the focus
48 has been on the price of Number 6 fuel, correct?

49 MR. WELLS: That's correct.

50 MS. BUTLER, Q.C.: And what I see here is \$14 million

51 between 1997 and 2002 which is not materially affected at all
52 by the price of Number 6 fuel, correct?

53 MR. WELLS: That's correct.

54 MS. BUTLER, Q.C.: And \$14 million is almost all of the
55 increase that Hydro is seeking on this application, correct?

56 MR. WELLS: But the \$14 million you talk about are
57 projections over a period of five years and let's assume that
58 inflation, if someone were to say today that inflation is two
59 percent a year, and actually it's running a little higher than
60 that now and approaching three in the latest figures, that at
61 2 1/2 percent a year we would just be matching inflation
62 with those costs, so these costs are not extraordinary. The
63 bottom line dollars we're talking about are not really the
64 dollars that are affecting this rate application. It's really,
65 Hydro operates on three pillars and one pillar is the cost of
66 fuel, which is like a hundred million dollar item. We have
67 our interest costs which thankfully have been lower. That's
68 another sort of hundred million dollar item, and then you
69 have what's left in between, and so that the real issue
70 which is evidenced by what the balance in the Rate
71 Stabilization Plan is, and is about to become, that's totally
72 really, other than the hydrology, the effect of that which we
73 can calculate, is really the substantial difference between
74 what we're getting in our rates, \$12.50, and the fact that
75 we've been paying \$31.00. So I'm mindful, and I think that,
76 you know, in my time since we came to Hydro, or I came to
77 Hydro in 1996, we had a downsizing in May. We've had
78 any number of reorganizations and job reductions which
79 are, the whole thrust of that is to deal with that top line
80 issue of salaries and fringe benefits. The company was
81 under a wage freeze from 1992 onward as part of the
82 government wage freeze. We came out of the wage freeze
83 at the end of '95. The increases in the bargaining unit were
84 2 1/2 percent. After three years that put our linemen on the
85 same level as Newfoundland Power's linemen at that time,
86 and we were trying to sort of catch up at the 2 1/2 percent
87 interval, and the pressure has been on to reduce the costs
88 that we can control, and if ... I mean all I have from my
89 perspective are complaints from the representatives of the
90 bargaining unit, the paid staff of the IBEW have taken me
91 to task and management in no uncertain terms, about the
92 kind of brutal treatment they've been receiving over the
93 past five years, and this has also become a subject of
94 comment in various communities in Newfoundland. When
95 we lay off employees or move employees, or reduce, we are
96 always subjected to criticism and comment of the effect that
97 we're having in areas of Newfoundland where Hydro
98 people are employed, so I mean I'll say it to you and to the
99 Board that in terms of holding that salary line. We've taken
100 out over the period since the last rate application 159 jobs.
101 Now we could take out, say, if we could, take out another
102 100 jobs. That would be worth \$5 million on our bottom

1 line roughly, say at \$50,000 a job. But if we buy an extra
2 million barrels of oil next year and it's \$20.00 more than what
3 we're paying in the Rate Stabilization Plan, we're looking at
4 a \$20 million tag over which we have no control, compared
5 to the \$5 million if we were to take out another hundred
6 jobs. So you know, between the bifocals and the
7 confusion, the whole point of what you're talking about is
8 a fact within the Hydro operation that you could almost say
9 that 80 percent of our costs are not controllable, and of the
10 80 percent or 70 percent that are not controllable, and of
11 that 70 percent another 70 to 75 or 80 percent is system,
12 equipment, maintenance, and salaries, so we're very
13 conscious of that line in these categories of expenses.
14 Salaries and fringe benefits, and system, equipment
15 maintenance, and you know, I will stand on the record ...
16 you can go back to 1992 and take those numbers forward,
17 and you can take the projection over the next five years of
18 14, and it's going to be very difficult to challenge the fact
19 that what is contemplated here, these expenses going up
20 by something like two percent a year, or two and a half
21 percent a year, which would just reflect the inflationary
22 factor, and we would have to do ... I don't think we have the
23 option to take out millions. You know, we might get
24 \$100,000 here or \$200,000 there, or half a million here on
25 system, equipment maintenance, depending on
26 circumstance. To recover this from employees, we'd have
27 to start looking at maybe 100 or 150 to 200 employees going
28 out of the system, and before this hearing is over I think we
29 should be able to establish with the Board, in the nature of
30 our operation, that's not on, that can't happen in the nature
31 of our operation, when we look at our generation, our
32 transmission, our distribution, and our isolated diesel
33 systems, and look at Hydro Place. While we are
34 endeavouring at all times to make sure that we're cost
35 effective with respect to personnel planning, we can't solve
36 the problem that everybody in this room confronts, and
37 rate increases on the backs of employees of Hydro. It ain't
38 there.

39 MS. BUTLER, Q.C.: I'm going to go back if I might though
40 to my question, partly in which you've given me an answer
41 that suggests that Hydro has, as you say, three pillars, the
42 fuel, the interest, and the other, and just to remind you, Mr.
43 Wells, that I was only asking you about the other for the
44 moment, and I don't think we can change the figures here.
45 The exhibit speaks for itself in the sense that we are talking
46 about a growth of \$14 million in the other controllable
47 expenses over the five year period, correct? From \$83 to
48 \$97 million?

49 MR. WELLS: Yes.

50 MS. BUTLER, Q.C.: Okay, and that does happen to be
51 almost all of the rate increase that's sought, which is \$18
52 million.

53 MR. WELLS: The rate increase, with respect, is required
54 for next year in terms of our revenue requirement, not five
55 years from now.

56 MS. BUTLER, Q.C.: No, that's true.

57 MR. WELLS: So you're talking dollars per annum ...

58 MS. BUTLER, Q.C.: Operating costs have increased by \$14
59 million.

60 MR. WELLS: Yes.

61 MS. BUTLER, Q.C.: And you're looking to recover \$18
62 million from the consumers. I would like to look now too,
63 at what's forecast between 2002 and 2005, if we could look
64 to page 16 of the IC-98, Mr. O'Reilly please. You might
65 want to go to the hard copy of the financial plan, Mr.
66 Wells.

67 MR. WELLS: Page 16?

68 MS. BUTLER, Q.C.: Thank you. In the line, Expenses,
69 Operating and Administration, do you have that page, Mr.
70 Wells?

71 MR. WELLS: Yes.

72 MS. BUTLER, Q.C.: Okay, thank you. Looking at the
73 column for 2002 which shows \$89.1 million, and the column
74 for 2005 shows \$95.1 million, so a growth of \$6 million in the
75 operating and administration expenses forecast for Hydro
76 in that period.

77 MR. WELLS: Yes.

78 MS. BUTLER, Q.C.: Okay, in the total period now, 1997 to
79 2005, we're talking about a growth of \$20 million in
80 operating and maintenance expenses. Let's deal first ...

81 MR. WELLS: Over the eight year period.

82 MS. BUTLER, Q.C.: Yes, let's deal first with the \$6 million
83 shown on the screen for the period 2002 to 2005. Because
84 you speak from the highest level of Hydro, Mr. Wells, can
85 you tell me what are you doing now and what are you
86 planning to do in the future to reduce the \$6 million
87 forecast increase in those operating and maintenance
88 expenses for the period 2002 to 2005?

89 MR. WELLS: You're assuming that we haven't taken into
90 account actions that will keep this figure where it is.

91 MS. BUTLER, Q.C.: Well you can give me the full answer.

92 MR. WELLS: Well, I mean, again, you're ... if you want to
93 look at those other, the operations and administration
94 costs, and we'll share with everybody else in the room
95 what's there, you know, the loss or gain on disposable
96 capital assets, your miscellaneous equipment rentals,
97 travel, professional services ... our professional services
98 dollar I'll tell you has certainly increased this year as a

1 result of this hearing ... building rentals, maintenance, office
2 supplies, transportation, insurance, and systems equipment
3 maintenance, now these are the items that we're discussing,
4 and salaries and fringe benefits, we've used a 2 1/2 percent
5 multiplier, I think, if you project those figures out, and
6 looking forward at that particular column, so when you use
7 a dollar value going back to '97 and ending in 2005 of some
8 \$18 million, but each year our revenue requirement is a
9 distinct issue and the issue of the costs in operating in
10 each particular year are far more affected by the price of fuel
11 and fuel consumption than anything to which we refer, and
12 could also be affected far, far more by interest rates if they
13 were to increase by two or three percent, then the figures
14 that we're talking about here are not as relevant, but I mean
15 if you, if you want me to confirm that we have taken a 2 1/2
16 percent inflator and put it out over the forecast period, and
17 you look back at the figure as it came forward from '97, if
18 you go back to '96, we took certain actions in '96, that '97
19 was our best year when everything we had at that point in
20 terms of our costs got into the bottom of the graph. Then
21 we had some problems that we recognized ... we had issues
22 that we had to deal with in '98 and '99 where we had more
23 operations and administrative costs than we wanted to
24 have, but there were certain factors that explained that at
25 least to us in terms of our trying to cope with Y2K, and we
26 had a major change out in our computer hardware and
27 software, and we had to employ people and backfill
28 positions to do that, and there was an increase again. But
29 in terms of the total controllable in that area going back to
30 1992, I think the figures speak for themselves. I mean I ...
31 you can say the dollar value is \$14 million, but I could say
32 that over a five year period we could spend another \$100
33 million in fuel that's not contemplated today.

34 MS. BUTLER, Q.C.: Well, again, we weren't going back as
35 far as 1992. The question was for 1997 forward.

36 MR. WELLS: Well, you know, I know you weren't.

37 MS. BUTLER, Q.C.: And Mr. Wells, the reason why I'm
38 asking you this question is because as president, I'm
39 wondering whether you can enlighten us on whether there
40 is a particular plan in place to keep what we see as a
41 forecast \$6 million growth in this type of controllable
42 expenses down.

43 MR. WELLS: Yes, but ...

44 MS. BUTLER, Q.C.: Does Hydro have such a plan?

45 MR. WELLS: Some of what you're looking at on the
46 projections forward, also includes ... some of that is
47 activities that we have ongoing and will have an effect on
48 some aspects of this, but if you ... one thing I will not do is
49 sort of share with you that we have some great overall plan
50 for a reduction in staff. I mean that would be totally
51 inappropriate for me here at this time and on this occasion

52 to deal with that type of personnel issue (inaudible), you
53 know, our thousand employees in some way, but the
54 options with respect to reducing some of those line items,
55 like salaries and fringe benefits, are pretty limited, but we
56 have taken ... certainly if you go back to '97 and if you took
57 '96 as your base, and '97 was the result, there's been a
58 significant number of people that have left Hydro and the
59 issue is not the 2 1/2 percent factor we're looking at going
60 forward. The issue from my perspective is what would it
61 have been had we not taken those decisions or taken the
62 initiatives that are ongoing.

63 MS. BUTLER, Q.C.: Are these the initiatives that are
64 referred to in your testimony?

65 MR. WELLS: That's right.

66 MS. BUTLER, Q.C.: Okay.

67 MR. WELLS: Certainly some of them.

68 MS. BUTLER, Q.C.: Alright, are there any other initiatives
69 not referred to in your testimony that you want to refer to
70 in answer to my question?

71 MR. WELLS: Well one of the things that we are ... we now
72 have our new computer system in and up and running and
73 one of the challenges going forward is in terms of that we'll
74 be examining all of our processes within Hydro within the
75 next year, and looking at the way that the technology can
76 assist us in reducing costs. We haven't been able as yet to
77 take full advantage of that, and therefore there is maybe
78 some leeway that we can help reduce the forecast 2 1/2
79 percent. But you know, to be of the same mind as you on
80 this line of questioning, we're forecasting 2 1/2 percent here
81 going forward, which again, is recognizing the cost of
82 inflation. I don't think it's ... it's a wrong figure to be using,
83 a figure that would provoke you to say that it's so
84 unreasonable.

85 MS. BUTLER, Q.C.: Well, I was trying to put this in terms
86 that the consumer might appreciate better, and that was the
87 \$6 million as opposed to 2.2 percent as the rate of inflation,
88 although I accept that that's what the executive summary
89 suggested, but I think ...

90 MR. WELLS: When you're spending at a level starting at
91 \$80 million a year, and you're saying at 2 percent and in five
92 years you're going to be spending, you know, another \$6
93 million, you've got to put it in the context, in that five year
94 period we will have spent over \$400 million on these items
95 and you're talking about another six resulting from a 2 1/2
96 percent inflation factor. This to me is not material.

97 MS. BUTLER, Q.C.: So you are satisfied that you have
98 done all you can to keep these down?

99 MR. WELLS: No, I think that we are satisfied with what we
100 have done up to this point in time. We are never satisfied,

1 and when we, you know, get back at the job we will be
2 doing as much as we can to reduce the costs over which
3 we have control, as we have been doing. I mean certainly
4 Hydro, I think, took that approach back in '92 when things
5 were getting rough in the economy and everybody had to
6 do that, every company and entity, and certainly since I
7 was there since '96, that's the constant focus of attention,
8 cutbacks, costs, reduction, reducing expenses here,
9 reducing there, and I thought that the figures were ... by
10 and large we had been fairly successful, and not without a
11 lot of controversy.

12 MS. BUTLER, Q.C.: The details perhaps will come up in
13 another section of your evidence, but what I'd like to do
14 now is turn, if I might, to what you refer to in your
15 testimony as Hydro's longer term financial targets, and I
16 wonder could we see Mr. Wells' testimony, page 13. Do
17 you want the hard copy of your testimony too, Mr. Wells.

18 MR. WELLS: I have that.

19 MS. BUTLER, Q.C.: You have that, okay.

20 MR. WELLS: That's the one thing I have with me.

21 MS. BUTLER, Q.C.: Alright, page 13, line 7 to 12. Perhaps,
22 Mr. Wells, could you read for the benefit of us all the
23 paragraph that starts at line 7, "Hydro will propose"?

24 MR. WELLS: Yes, in answer to the question we say Hydro
25 will propose a rate of return on rate base and return on
26 equity which it believes is necessary for Hydro to achieve
27 in the longer term in order for the Corporation to comply
28 with the requirements of the EPCA. Hydro's immediate
29 financial objectives will be explained in the context of the
30 longer term financial targets which Hydro and its financial
31 advisors believe are essential for Hydro to obtain.

32 MS. BUTLER, Q.C.: Okay, there's also another quote from
33 your evidence I wanted to look at at the moment and it
34 relates to this, and it's at page six, if I might, lines 20 to 22.
35 The legislative amendments, can you just read that one for
36 me?

37 MR. WELLS: Yes. The legislative amendments indicate
38 that as a matter of public policy, Hydro is intended to
39 operate as a fully regulated utility more similar to that of an
40 investor owned utility than had been previously been the
41 case.

42 MS. BUTLER, Q.C.: And then I'll leave your testimony for
43 the moment with that background and look if I might at NP-
44 75(b), page five of six. Newfoundland Power asked Hydro
45 about that particular portion of your testimony, and the
46 question itself, perhaps not apparent on that page ... page
47 five of six, Terry? Yeah, you have to go to (b) as in baby
48 there. There you go. Okay, so what I'm dealing with is
49 your statement, Mr. Wells, that Hydro was intended to

50 operate as a fully regulated utility similar to an investor-
51 owned, and your answer here, perhaps you might read for
52 us ... Hydro views the following similarities.

53 MR. WELLS: The answer, Hydro views the following
54 similarities between the way Hydro was intended to operate
55 and the matter in which an investor-owned utility operates,
56 and there's three bullets. Operate in an efficient and least
57 cost basis, and achieve an appropriate return on rate base,
58 achieve an appropriate return on equity.

59 MS. BUTLER, Q.C.: I believe it goes on to the next page
60 there, yeah, thanks.

61 MR. WELLS: Achieve appropriate debt/equity ratios,
62 provide an appropriate dividend (inaudible).

63 MS. BUTLER, Q.C.: So do you accept, Mr. Wells, that this
64 means Hydro should have an investment grade rating and
65 financial targets similar to an investor-owned utility?

66 MR. WELLS: Certainly.

67 MS. BUTLER, Q.C.: Okay, and do you also agree that that
68 also means that Hydro must behave in all other respects as
69 an investor-owned utility?

70 MR. WELLS: Unless prescribed by some matter of
71 legislation or public policy.

72 MS. BUTLER, Q.C.: I believe these were also dealt with in
73 your evidence, because Hydro is currently government
74 owned, of course, and you raise certain facts in NP-76
75 which were relevant to that ownership, and perhaps that
76 flowed from the legislation. If we could just go to NP-76.
77 Starting at line five you indicated there the main
78 differences, so I will come back to those differences in a
79 moment, but ...

80 MR. WELLS: Yes, the ... do you wish me to read those?

81 MS. BUTLER, Q.C.: No, I think that's fine, we can leave
82 them there on the screen. Perhaps consistent with what
83 was indicated here, Hydro has the benefit of a guarantee by
84 the Government of Newfoundland, correct?

85 MR. WELLS: That's correct.

86 MS. BUTLER, Q.C.: Alright, and this is provided, I believe,
87 under Section 28 of the Hydro Corporation Act, do you
88 agree that's the case?

89 MR. WELLS: Uh hum.

90 MS. BUTLER, Q.C.: Alright, do you accept, Mr. Wells, that
91 this guarantee allows Hydro to achieve and maintain a
92 sound credit rating in the financial markets of the world?

93 MR. WELLS: That of itself would not do that in terms of its
94 capital structure, but the benefit ... that ... the guarantee of
95 itself is not going to make Hydro necessarily have the right

1 capital structure in operating as an investor-owned utility
2 or as a good operating entity. What the government
3 guarantee does is it gives Hydro the opportunity to obtain
4 effectively, say a Triple B in investment grade rating when
5 it goes into the bond markets, and it also saves us probably
6 a hundred basis points than we otherwise would have to
7 pay, and that, of course, is offset too because we also pay
8 a guarantee fee to the government, so these, as is outlined
9 in the evidence of our witnesses, particularly our expert
10 witnesses, the factor, the positive factor of the government
11 guarantee fee to the extent that you can apply it to the
12 issue that you seem to be talking about, but it is an aspect
13 in terms of the financing of Hydro and its capital structure,
14 which is extremely helpful, and for which the guarantee fee
15 seems to be by all accounts a reasonable payment for that.

16 MS. BUTLER, Q.C.: Perhaps to rephrase my question then,
17 I think you're agreeing that the existence of the guarantee
18 by the government contributes to Hydro's ability to
19 achieve and maintain a sound credit rating.

20 MR. WELLS: Uh hum.

21 MS. BUTLER, Q.C.: Okay, and in relation to the fee that's
22 paid for this, which I believe to be one percent,
23 approximately \$11 or \$12 million a year.

24 MR. WELLS: Uh hum.

25 MS. BUTLER, Q.C.: Okay, do you accept, Mr. Wells, that
26 the existence of the guarantee and the payment of the
27 guarantee fee are, of course, significant matters for this
28 Board in determining Hydro's financial targets?

29 MR. WELLS: They are part of the issues that will be
30 discussed when you look at the appropriate financial
31 targets for Hydro, but the financial targets must be
32 assessed in light of the capital structure and the risk that
33 the utility confronts, and the best way I can put that to you
34 from my perspective, or that maybe of our witnesses, is that
35 in its initial consideration of the capital structure of Hydro,
36 the Board and everybody in the room really should be
37 indifferent as to who owns the entity, whether it be
38 government, an individual or investor-owned. The issue is
39 in determination of the entity itself, the financial entity,
40 what should be the appropriate capital structure, what
41 should be the percentage of debt to equity. If you have
42 that particular percentage of debt to equity, what does that
43 mean in terms of its financial viability and its capability to
44 borrow at what cost, and if you look at it in that light, and
45 have the benefit of your expert testimony and the question
46 then becomes, in my mind, what is it that would provoke
47 the Board or compel the Board to differentiate Hydro from
48 what we will call a normal entity confronted with the risks
49 that confront Hydro, and then you may deviate from that,
50 you know, absolutely pure ... or certainly we have in our
51 own application, but you should look at it in that light, and

52 one of the factors that you would look at is that our ability
53 to borrow is enhanced by the guarantee fee, but then that,
54 that gives us access to the capital markets when we require
55 as we pointed out in our pre-filed testimony, it gives us
56 certain advantages, and it gives us an investment grade
57 rating. To the benefit of our industrial customers and
58 Newfoundland Power, and all consumers in Newfoundland,
59 it helps us to exist as we are and we can make, we have
60 more flexibility to entertain, say, an 83 percent debt ratio for
61 a short period of time, but the principle which we will all
62 have to come to grips with at this hearing is that because
63 Hydro is Crown corporation does not mean that the
64 government or the people of Newfoundland as owner, and
65 that hat, should use that to subsidize the operations and
66 the rates and everything else that Hydro is connected with,
67 and it is to the advantage of everybody, particularly when
68 we're talking about some price signals and other things,
69 that people understand what it costs to have the operation
70 as we know it to generate and transmit, and a limited
71 amount of distribution of energy. I think that's what the
72 thrust of our evidence is and the, we have put forward
73 things that are desirable and credible through our expert
74 witnesses. Now this is tempered by the fact that in the
75 circumstances of the day we can exercise value judgements.
76 We've already exercised it. We are here arguing that we
77 want the Board to send a message to the financial
78 institutions and the financial community in Canada and
79 abroad, that we view this utility as such and such, and it
80 should have a return on equity of such and such. In the
81 meantime, we've turned around and asked for basically a
82 nominal rate of return of three percent. Why did we do
83 that? When you're confronted with this factor of oil price
84 increases, and the significant increase, and worse than that,
85 a significant increase that's not forecast to decrease. We've
86 had significant increases before, but it always dropped
87 back again, and as I said earlier, two years ago \$11.00 a
88 barrel, so we started to bring down the balance in the Rate
89 Stabilization dramatically. But in light of that, the three
90 percent is a no brainer. I mean nobody can be seriously in
91 this room arguing that a three percent rate of return for
92 Hydro is excessive. On the other hand, look at the signal
93 we send from Newfoundland and from our regulatory
94 agency, if we were to say that three percent rate of return to
95 this utility is where the Board would see the utility forever
96 and a day in the future, an entity that could never be
97 financially viable under any circumstance, an entity that
98 could not stand on its own two feet, an entity that would
99 inevitably impact on the credit rating of the province, we're
100 12 percent of the provincial debt. So it's desirable for a
101 variety of reasons if the people of Newfoundland and
102 Labrador own a utility that is structured and operates much
103 the same as any other business entity, but there are some
104 variations that you can put in on this short-term and maybe
105 even for the longer term. But, you know, the fact that the

1 government guarantees a fee, the debt is just one aspect of
2 that, just one aspect.

3 MS. BUTLER, Q.C.: I think though, Mr. Wells, in listening
4 to your answer to my question, that we are in fundamental
5 agreement on two points. Bear with me. One, that your
6 ability to borrow, Hydro's ability to borrow is enhanced by
7 the guarantee, which happens to be from the Government
8 of Newfoundland, correct?

9 MR. WELLS: We would ... yes ...

10 MS. BUTLER, Q.C.: Sorry, am I right?

11 MR. WELLS: Well that is the route we use now, rather
12 than say a 60/40 debt/equity ratio which we would require
13 to get to a Triple B rating, which is what we're getting with
14 government.

15 MS. BUTLER, Q.C.: Exactly.

16 MR. WELLS: Yeah.

17 MS. BUTLER, Q.C.: And my second point was going to be
18 that the guarantee, the existence of the guarantee which is
19 obviously compensated for by a guarantee fee, does affect
20 your debt/equity ratio.

21 MR. WELLS: That guarantees our debt.

22 MS. BUTLER, Q.C.: Yes, so the debt/equity ratio is
23 affected by the existence of the guarantee.

24 MR. WELLS: Not necessarily, it may or may not be,
25 depending on ... there are other factors in your debt/equity
26 ratio that don't relate necessarily to the guarantee.

27 MS. BUTLER, Q.C.: Well let me put it slightly differently.
28 Do you agree that the existence of the guarantee allows
29 you to operate with a higher debt/equity ratio, lower than
30 it would be without it?

31 MR. WELLS: Yes, and obtain the same favourable, if you
32 call it favourable, pricing of our debentures in the
33 marketplace, yes.

34 MS. BUTLER, Q.C.: Okay, so back to the original question
35 then, the existence of the guarantee is one of the various
36 matters of some significance for this Board in determining
37 Hydro's financial targets?

38 MR. WELLS: Yes, the Board should consider that aspect
39 of how we obtain our financing.

40 MS. BUTLER, Q.C.: Now you also answered NP-76 by
41 reference to social policy, social or public policy
42 considerations not in conflict with legislation, and the only
43 issue I want to follow up with here is that of the deficit and
44 its subsidization by Hydro's retail customers. Do you agree
45 that the subsidization of the deficit which is incurred in
46 some areas by other customers is a matter of social policy
47 directed to you by government?

48 MR. WELLS: Oh definitely, yeah, it's the government that
49 made that decision.

50 MS. BUTLER, Q.C.: Right.

51 MR. WELLS: For everybody, yes.

52 MS. BUTLER, Q.C.: Yeah, and the subsidization to the
53 extent that you run a deficit but it is completely covered is
54 also relevant, significant for this Board to consider in
55 establishing your financial targets?

56 MR. WELLS: Let me put it this way, it opens a basis for
57 argument which I'm sure you will take advantage of before
58 the hearing is over, but you can argue that one both ways.
59 It is an item for discussion and it will be put into play, I'm
60 sure by the intervenors, and it will be discussed and
61 debated, and it will be decided by the Board. It's an issue
62 that the Board will, obviously from the tenor of the
63 responses, will have to deal with.

64 MS. BUTLER, Q.C.: Mr. Chairman, were you planning on
65 taking a break this afternoon, or do we just go straight
66 through to 4:00?

67 MR. NOSEWORTHY, CHAIRPERSON: I was planning on
68 taking a short break at 3:15.

69 MS. BUTLER, Q.C.: Okay, because I'm just finished a
70 particular section and moving into another, so that would
71 be fine.

72 MR. NOSEWORTHY, CHAIRPERSON: Okay.

73 MS. BUTLER, Q.C.: Thank you, Mr. Wells.

74 MR. NOSEWORTHY, CHAIRPERSON: We'll take just a ten
75 minute break until 3:15, thank you.

76 *(break)*

77 MR. NOSEWORTHY, CHAIRMAN: Thank you. Just a
78 comment before we proceed. On the breaks it will be my
79 intention to take breaks around, as I indicated this morning,
80 11:00 and 3:15, if not for any of us necessarily in this room
81 other than the witness. I think it would be welcomed by the
82 witness. It would be my intention to do that, and I would
83 appreciate if taking the leave from the questioning counsel
84 as to timing, five or ten minutes one way or the other, I
85 thank you very much and if you could advise me at a point
86 in time when it might be more appropriate rather than the
87 designated 11:00 and 3:15, we'd certainly try and
88 accommodate that as well, so I would appreciate that. And
89 even at the end, if you feel another five minutes or so at the
90 end of the day would be more appropriate, that's fine as
91 well, we can do that, so we're fairly flexible in that regard.
92 Thank you, you may proceed.

93 MS. BUTLER, Q.C.: Thank you Mr. Chair. Mr. Wells I

1 want to turn now to a different area, and I think we've
2 established that the existence of a guarantee allows Hydro
3 to operate with a higher debt/equity ratio. Specifically do
4 you accept that existence of Hydro's corporate guarantee
5 allows Hydro to operate with a current debt/equity ratio of
6 83% debt, 17% equity?

7 MR. WELLS: What it really means is that it doesn't affect
8 the cost of your borrowing.

9 MS. BUTLER, Q.C.: Is your current ... sorry.

10 MR. WELLS: It guarantees the means that we can borrow
11 at rates that are equivalent to a company that had a capital
12 structure say of 60/40 debt/equity ratio.

13 MS. BUTLER, Q.C.: But your debt/equity ratio currently is
14 83 and 17.

15 MR. WELLS: Yes.

16 MS. BUTLER, Q.C.: That's fine.

17 MR. WELLS: It will be.

18 MS. BUTLER, Q.C.: It will be?

19 MR. WELLS: Under, for the 2002 test year it would go to
20 83, its not there yet.

21 MS. BUTLER, Q.C.: The last time this Board looked into
22 the issue in 1992 I understand it recommended that Hydro
23 move to an 80/20 debt/equity ratio. I believe you referred
24 to that in your testimony. Is that correct?

25 MR. WELLS: Yes, that's true.

26 MS. BUTLER, Q.C.: To your knowledge, Mr. Wells, has
27 Hydro's operation with a debt/equity ratio of 80/20, or
28 83/17, had any negative impact on the credit rating of the
29 Province.

30 MR. WELLS: No, nor should it at that level, for that term.

31 MS. BUTLER, Q.C.: I know, Mr. Wells, you are likely
32 familiar with Section 5.1 of The Electrical Power Control
33 Act, and I think for the benefit of the group assembled here
34 I'll have it handed out. I just want to refer you to that
35 section. Okay?

36 MR. WELLS: Yes.

37 MS. BUTLER, Q.C.: This is the section which allows the
38 Government to direct the Public Utilities Board on various
39 matters but including the direction of the fixing of the
40 debt/equity ratio for Hydro. My only purpose in putting
41 this in front of you is to ask you whether Government has
42 specifically directed the Public Utilities Board on the fixing
43 of the debt/equity ratio for Hydro.

44 MR. WELLS: I'm not aware of any such action.

45 MS. BUTLER, Q.C.: I wonder in keeping with that since it's

46 a matter now for judgement for this Board to determine
47 what is appropriate debt/equity ratio for Hydro if we could
48 look at Hydro's dividend policy. If you would like to refer
49 to the hard copy that's fine, but I'll ask Mr. O'Reilly to put
50 up IC-276 and I believe this was also revised. It should be
51 the second attachment. Mr. O'Reilly, are they not
52 electronically entered.

53 MR. O'REILLY: Correct.

54 MS. BUTLER, Q.C.: Okay. Do you have your hard copy
55 provided to you yet, Mr. Wells?

56 MR. WELLS: Of?

57 MS. BUTLER, Q.C.: IC-276. Mr. O'Reilly, maybe while
58 we're waiting for that could you put on the screen please
59 Mr. Wells' testimony, page 16. Mr. Wells, do you have the
60 dividend policy in front of you? There's one for 1995 and
61 one for 2000, I believe.

62 MR. WELLS: Yes.

63 MS. BUTLER, Q.C.: Okay. Take a moment to refresh your
64 memory on them, but clearly the one I need to ask you
65 about is the one that's dated May 12, 2000.

66 MR. WELLS: Uh hum.

67 MS. BUTLER, Q.C.: Okay. The dividend policy dated May
68 12, 2000 indicates that Hydro could pay each year to its
69 shareholder, the Government, dividends of up to 75% of
70 the Corporation's net operating income before net recall
71 revenue, plus 100% of net recall revenues. Is that correct?

72 MR. WELLS: That's correct.

73 MS. BUTLER, Q.C.: Alright. In looking at your evidence
74 page 16, lines 4 to 8, can you tell me please, is this the
75 dividend policy that you're referring to when you say that
76 following the requirement of Hydro to pay dividends in '95
77 the Board established the dividend policy of payment of
78 75% of the net operating income provided it did not
79 negatively impact the debt/equity ratio.

80 MR. WELLS: You have, if you just look at line 4 there it
81 says following the requirement of Hydro to pay dividends
82 in 1995.

83 MS. BUTLER, Q.C.: Uh hum.

84 MR. WELLS: I think in that answer there is trying to
85 compact the two. In 1995, in the first go at this, the Board
86 said that 75% of net income provided that it did not
87 negatively impact the debt/equity ratio of the Corporation.

88 MS. BUTLER, Q.C.: Right.

89 MR. WELLS: Subsequent to that, after the recall and the
90 sales of recall power came into Hydro's revenues the
91 Government in effect wanted a hundred percent flow

1 through of those revenues so the Board then amended the
2 original minute and ... to reflect 75% of the Corporation's
3 net operating income before net recall of revenue for that
4 year plus 100% of the net recall revenue. So the ... and then
5 the modification is that due consideration had been given
6 by the Board of the impact of the debt/equity ratio on the
7 Corporation.

8 MS. BUTLER, Q.C.: Yes, it was the proviso that I wanted
9 to ask you a few questions about, but are we speaking
10 basically in your evidence of the dividend policy at the
11 Corporation as it exists since 2000?

12 MR. WELLS: As it exists today, yes.

13 MS. BUTLER, Q.C.: Thank you. So the proviso is that
14 provided that such payment shall only be made after due
15 consideration has been given by the Board of the impact of
16 such payment on the debt/equity ratio of the Corporation.
17 Ultimately, Mr. Wells, the amount of the dividend paid in
18 any given year is subject to the will of the board of
19 directors, correct?

20 MR. WELLS: To the ...

21 MS. BUTLER, Q.C.: The decision of the board of directors.

22 MR. WELLS: Yes.

23 MS. BUTLER, Q.C.: But the amount paid does have a
24 direct impact on the debt/equity ratio?

25 MR. WELLS: It can have, yes.

26 MS. BUTLER, Q.C.: Yes, and as I understand it, without
27 the dividend proposed there's been some evidence to
28 suggest that the debt/equity ratio of Hydro would be
29 75/25?

30 MR. WELLS: I'm not sure if that's in our pre-filed
31 testimony. We were below 80/20 and we're projecting, as
32 you already referred to, what would happen if our
33 proposals are accepted we would go higher again and then
34 back down but the, from the board of directors point of
35 view going back to 1996, I can attest to that I am member of
36 the board, we were focusing on 80/20 and one of the
37 reasons at that time the last recommendation of the Public
38 Utilities Board had been that Hydro work slowly toward an
39 80/20 debt/equity ratio and that was one of the flags that
40 one would look at when you are assessing the debt/equity
41 ratio. The Board, we can move around the debt/equity
42 ratio to some extent depending on what your other objectives
43 are, our first objective is to cope with the issue of rates and
44 impact of oil prices, so as we understand it from our
45 financial advisors, this would not negatively impact the
46 Corporation's or the view in the financial markets of the
47 Corporation or the Government if we were to drift upwards
48 to the 83% or 84%, providing that it didn't become chronic
49 and our objective would be to move the debt/equity ratio

50 towards the targets in the longer term, mindful of the other
51 factors that impinge on your decision making process, but
52 the Board certainly, dividends came into being in 1995, and
53 the Board's first reaction to that was to certainly try to track
54 the then more recent you know, the latest pronouncement
55 from the Public Utilities Board was track that 80-20 target
56 and to the extent we were above it, well we try and get
57 down to it, if you got down to that you would set your
58 sights for something lower.

59 MS. BUTLER, Q.C.: Ok, well let's follow up from that then.
60 We know that the last directive from this Board to Hydro
61 on the topic of the debt/equity ratio was move slowly
62 towards it. But is it not accurate that the dividend
63 proposed by Hydro in this proceeding will take Hydro to a
64 debt/equity ratio of 85/15.

65 MR. WELLS: What, what ... we haven't as a Board, the
66 Hydro board has made no decision. What we are
67 indicating is a projection from the Government of a
68 requirement that they have of dividends of Hydro and that,
69 and the level of the dividends, and if that were to come to
70 pass, then that would have the effect, yes, the number you
71 mentioned would, it's just the mathematics.

72 MS. BUTLER, Q.C.: Okay, are you aware that there has
73 been some pre-filed evidence that suggests that without
74 the dividends the debt/equity ratio would be 75/25?

75 MR. WELLS: Yes, if you can see it there it is probably ...
76 I'm not sure if it got that low, but, because that is a
77 secondary target as well as opposed to the say 60/40, but
78 75 is another benchmark.

79 MS. BUTLER, Q.C.: Mr. O'Reilly can show you, if its
80 entered IC-66 revised, and that might reflect this. Just bear
81 with me one moment, Mr. O'Reilly, and we'll see.

82 MR. WELLS: IC-66?

83 MS. BUTLER, Q.C.: Yes, 1(d), I think, was the question
84 that the industrial customers put in the development, what
85 would the utility's 2002 test year capital structure if no
86 dividends been declared to date and none were declared for
87 2002 and the answer Mr. O'Reilly, is in a schedule. Mr.
88 Wells, it is on the screen if it's any help to you. 2002 as
89 filed in the application, I'm sorry can you ... yeah, okay.

90 MR. WELLS: And it shows what the debt/equity ratio
91 would be.

92 MS. BUTLER, Q.C.: Yes, as filed 85.51 revised 74.89.

93 MR. WELLS: Yes, if those things, what that question ...

94 MS. BUTLER, Q.C.: Yeah.

95 MR. WELLS: ... if it went that way that's what would
96 happen. Okay, I accept that.

1 MS. BUTLER, Q.C.: Thank you.

2 MR. WELLS: The other little confusion now is employee
3 future benefits are shown as a separate line.

4 MS. BUTLER, Q.C.: Okay, another round of questions
5 which I don't want to get into right now, but let me just see
6 if I can carry through my logic on this for a moment.
7 Management's decision on the dividend to be paid in a test
8 year will have an impact on revenue requirements.

9 MR. WELLS: You say management's decision ...

10 MS. BUTLER, Q.C.: Well, I'll rephrase that.

11 MR. WELLS: Yeah, you'll have to rephrase that.

12 MS. BUTLER, Q.C.: The amount of dividend paid in a test
13 year will have an effect on revenue requirements.

14 MR. WELLS: The dividend might be paid would have an
15 effect on it.

16 MS. BUTLER, Q.C.: And revenue requirements, of course,
17 have an impact on consumers cause they have to meet
18 your revenue requirements, right? The ratepayer, correct?

19 MR. WELLS: Yes. I haven't conceded the amount of that
20 impact.

21 MS. BUTLER, Q.C.: No. I wonder if I might look at, back to
22 your financial plan, the hard copy of your financial plan
23 that I referred you to earlier in my cross-examination, IC-98,
24 page 4.

25 MR. WELLS: Sorry, I put that away.

26 MS. BUTLER, Q.C.: That's okay. Actually number four,
27 not Roman numerals four, and can you enlarge that please?
28 Thank you.

29 MR. WELLS: Did you say (inaudible) four?

30 MS. BUTLER, Q.C.: Yes. What we have here in Table 1,
31 Key Financial Assumptions, show that the bottom line debt
32 to capital ratio for the years 2001, 2, 3, 4 and 5. Do I
33 understand, Mr. Wells, that based on the Company's
34 current financial plan that with the dividend paid you
35 would still only have recovered your debt/equity ratio to
36 82% by the year 2005?

37 MR. WELLS: In that exercise that's what it shows, yes.

38 MS. BUTLER, Q.C.: Okay, and now with this on the screen
39 I just want to ask you, of course, and this is despite the fact
40 that this Board has recommended to your Company in the
41 past that this debt/equity ratio be aimed at 80/20?

42 MR. WELLS: Yes.

43 MS. BUTLER, Q.C.: Right. If the dividend of 75% of net
44 operating income was declared and paid, by my
45 calculations we are talking about payment of \$7.2 million

46 approximately.

47 MR. WELLS: In 2002?

48 MS. BUTLER, Q.C.: Yes.

49 MR. WELLS: Yes, I think you're right.

50 MS. BUTLER, Q.C.: But in the test year Hydro proposes to
51 pay a dividend of 730 percent of net operating income
52 which would amount to a dividend of \$70 million, am I
53 accurate?

54 MR. WELLS: That's right.

55 MS. BUTLER, Q.C.: I wonder, Mr. O'Reilly, can you get
56 NP-72 on the screen for Mr. Wells. You'll see a schedule at
57 the bottom of that page, I believe. Page 2 of 2. There you
58 go. Thank you. I just want to hold that screen in front of
59 us for the moment because this answer to question NP-72
60 shows the dividends paid during various years and their
61 percentage of net operating income.

62 MR. WELLS: That's right, yes.

63 MS. BUTLER, Q.C.: Okay, the payment of the \$70 million
64 dividend which represents 730% of net operating income is
65 what drives your debt/equity ratio to 85/15 in the test year,
66 correct?

67 MR. WELLS: It assists in that regard, yes, it has an effect.
68 It goes with our three percent return on equity.

69 MS. BUTLER, Q.C.: I wonder ... just keeping that on the
70 screen for a moment, I'll just check the hard copy of
71 McShane's testimony, page 23. Yes, Ms. McShane says at
72 page 24 of her testimony, and she is one of the experts
73 being called by Newfoundland Hydro, starting at line 30 ...
74 I'm sorry, page 23, line 30. Thank you. Do you see right at
75 the bottom there Mr. Wells?

76 MR. WELLS: Uh hum.

77 MS. BUTLER, Q.C.: The dividend of \$105 million, \$70
78 million of which is attributable to regulated earnings to be
79 paid in 2002, is a key factor accounting for a forecast test
80 year utility common equity ratio of 15.3%.

81 MR. WELLS: Uh hum.

82 MS. BUTLER, Q.C.: Okay, so you accept that?

83 MR. WELLS: Yes.

84 MS. BUTLER, Q.C.: Thank you, Mr. O'Reilly. Now go back
85 to that screen. Just keep that up for a moment. Mr. Wells,
86 in your evidence you spoke generally of the desire to move
87 towards a 60/40 debt/equity ratio over the longer term. Do
88 you recall that?

89 MR. WELLS: Yes.

90 MS. BUTLER, Q.C.: And 80/20 short term, but on the other

1 hand your evidence supports payment of a dividend of \$70
2 million in the test year which has the effect which we've
3 just seen from Ms. McShane of driving your debt/equity
4 ratio in the opposite direction to 85/15. I just wonder if you
5 might at this time rationalize the inconsistency that I see
6 there.

7 MR. WELLS: Yes, well there is two decision making
8 processes under ... reflected here. One is the shareholder,
9 and you will note from the table that you now have on the
10 screen that while the Hydro board had set a 75% of net
11 income policy for dividends, in '95, in fact, only 64% was
12 paid; in '96, 47%; and in '97, 39%; in '98, 42%; and in 1999,
13 10%, and what the Government had communicated to us
14 through the Department of Finance in terms of dividend
15 payments it, it could have taken more but it was holding
16 back. If the Government, for whatever reason, in its own
17 circumstance, did not require the dividend in the fiscal year
18 of Government, then they took less and that reserve, as
19 you can see, the 172% paid out in 2000 still put us if you
20 averaged over the years at a 75% or less dividend payout
21 from net income. What Government has advised us now
22 and it was in the last budget speech was that they would
23 be looking for a fairly significant payment by Hydro, and
24 it's certainly not related to net income, it's more taking out
25 retained earnings of the Company, to meet its fiscal
26 requirements in the current budget which will, in the
27 Government's fiscal year that ends March 31st next. If
28 some great fortune were to befall the Government of
29 Newfoundland and Labrador, you know, in the next,
30 between now and that time, then I would suggest that the
31 notice they put us on is to the revenue requirement that
32 they have, that that would not materialize. Much in the
33 way that the lesser dividend payments are shown in the
34 preceding years. But that is not, that decision is not made
35 by the Hydro board nor the management of Hydro, it is a
36 Government decision related to its own fiscal requirements
37 and its capabilities, and as you can see they've, in terms of
38 an appetite for Hydro dividends they haven't taken out in
39 the four year period, one, two, three, four, five years, what
40 the, what could have been paid as per Board policies. So
41 that would assist the debt/equity ratio of the Corporation,
42 and then when they did make a larger move it was just
43 taking the cumulative amounts left over, is the way I put it,
44 in layman's terms, and we have to face the fact that the
45 shareholder is projecting that this dividend requirement is
46 there. Now having said that, and that relates to the
47 Government's fiscal position, the board of directors of
48 Hydro, and they should, have a dividend policy related to
49 net income, that's the only thing that they can look at, and
50 the objective of the exercise for the board and for the
51 management, and maybe even for Government, is to bring
52 the debt/equity ratio in line ... it's certainly not to be
53 affected by untoward dividends or taking of retained

54 earnings. But the Government as a shareholder has every
55 right to do that if it so wishes and, of course, in its own
56 jurisdiction its sovereign.

57 MS. BUTLER, Q.C.: Two questions flowing from that.
58 First, Newfoundland Power does not question a
59 shareholder's right or management's right to declare and
60 payout a dividend in any amount it chooses. However, do
61 you accept that the ratepayers of this Province should not
62 be billed for anything more than this Board determines as
63 a reasonable capital structure.

64 MR. WELLS: Well again, if you, you have to weigh
65 everything in balance. It's the Government that set up
66 Hydro in the first instance, it's the Government support
67 over the time, including the debt guarantee fee, that
68 allowed retained earnings to accumulate and for years in
69 Hydro's operation, the shareholder took no return. So now
70 the shareholder is taking something back out of the
71 Corporation which you can say is a detriment to ratepayers
72 for the moment. But if you look at the other side of the coin
73 you have to look in balance over the years that Hydro's
74 been in operation what benefit that the ratepayers derived
75 from Government actions in leaving retained earnings in
76 Hydro and in not taking any dividend, and you'd have to
77 work out, you know, I have to assume, you know, it may be
78 a large assumption on my part, that the only reason that
79 Government is asking for extraordinary dividend at this time
80 is to meet with its own extraordinary fiscal requirements.
81 Obviously that level of payout cannot continue, nor is
82 there any reason to believe that Government contemplates
83 that it would. In my experience since I've been with Hydro,
84 each year they forecasted a dividend, forecasted a dividend
85 higher than they actually took in any of those years that
86 are shown on the screen, and you'd have to wait to find out
87 exactly what they did want, but it was always, anytime the
88 Government had other sources of revenue that become
89 available to it, then we were put on the back burner and the
90 only thing, and we might as well get it on the plate today
91 for everybody on this dividend issue, is that the dividend
92 has not happened as yet. The reason why we have
93 included, we have a clear indication from Government that
94 this year you may expect that what we are asking for is
95 going to come true, they've declared it as part of their
96 budget, and we can't ignore it. You know, if we came to the
97 Board and didn't include such a significant item with
98 respect to the test year, now the timing is, timing is
99 everything, but we had no idea that the Government was
100 going to require an extraordinary dividend in our test year
101 nor did they think of our test year in looking for it. It's
102 circumstance.

103 MS. BUTLER, Q.C.: Okay, but ultimately it is this Board
104 which has the final say on the size of the dividend which
105 becomes relevant to the ratepayers of the Province.

- 1 MR. WELLS: The Board has the final decision with respect
2 to rates, yes, not necessarily the dividend, but the rates.
- 3 MS. BUTLER, Q.C.: I think I'm going to move away from
4 that screen for the moment and go back if I might to NP-
5 72(c). Can we just scroll up so that Mr. Wells can see the
6 question there please, okay. Mr. Wells, the question asked
7 here was for Hydro to provide the estimated impact on
8 revenue requirement for the test year of financing the \$70
9 million dividend shown in the projected statement of cash
10 flows, and the answer given was that the revenue
11 requirement would be reduced by \$1.7 million if the \$70
12 million dividend were eliminated.
- 13 MR. WELLS: Yes.
- 14 MS. BUTLER, Q.C.: This is almost one-tenth of the rate
15 increase that Hydro is seeking.
- 16 MR. WELLS: Uh hum.
- 17 MS. BUTLER, Q.C.: Which is a substantial amount of
18 money for ratepayers.
- 19 MR. WELLS: It's \$1.7 million. It's the arithmetic of the fact
20 that the dividend, if it were or were not taken out, yes.
- 21 MS. BUTLER, Q.C.: If I might, I wonder if might look now
22 to NP-169. Again, a question put by Newfoundland Power
23 to Hydro. You asked to provide studies, surveys, reports
24 or other evidence that supported the establishment of the
25 dividend payment policy in 1995 and what was given was
26 a letter from Scotia McLeod of April 24, '95. First of all, Mr.
27 Wells, we can look to the letter, Mr. O'Reilly please, but are
28 you familiar with the letter, Mr. Wells?
- 29 MR. WELLS: Would that be the one signed by Mr.
30 Carmichael?
- 31 MS. BUTLER, Q.C.: No, its signed by Theresa McLeod, I
32 thought.
- 33 MR. WELLS: Oh.
- 34 MS. BUTLER, Q.C.: The signatures page is ... there you go,
35 325.
- 36 MR. WELLS: This is a letter to Mr. Osmond recommending
37 ...
- 38 MS. BUTLER, Q.C.: The dividend policy.
- 39 MR. WELLS: ... various payout ratios.
- 40 MS. BUTLER, Q.C.: And the dividend policy, I believe.
- 41 MR. WELLS: Of other utilities. I haven't ...
- 42 MS. BUTLER, Q.C.: Let's scroll back to the first page of
43 that, okay, April 24, '95 and the opening paragraph.
- 44 MR. WELLS: This is before I came with Hydro, '95.
- 45 MS. BUTLER, Q.C.: When was it you actually joined
46 Hydro?
- 47 MR. WELLS: January 1, '96.
- 48 MS. BUTLER, Q.C.: Okay. At that point the dividend
49 policy which we saw a moment ago that was subsequently
50 revised in 2000 had, of course, been declared, that was
51 declared in November of '95, I believe.
- 52 MR. WELLS: Yes, before I got there, yeah.
- 53 MS. BUTLER, Q.C.: So you were aware that that dividend
54 policy was in place. Were you aware that this letter had
55 some involvement in the establishment of a dividend policy
56 for Hydro?
- 57 MR. WELLS: Not in the particular ... unless I assumed that
58 in the file somewhere and certainly I was acquainted with
59 what the dividend policy of Hydro was when I arrived on
60 the scene, you know.
- 61 MS. BUTLER, Q.C.: Okay. Well first of all let's just scroll
62 up to the top of the letter so we can see who it's, the firm
63 that it's from. Scotia McLeod. Mr. Wells, what is Hydro's
64 relationship with Scotia McLeod?
- 65 MR. WELLS: Scotia McLeod is one of the financial
66 advisors to Hydro.
- 67 MS. BUTLER, Q.C.: Okay, and Theresa McLeod, in
68 particular, do you know what position she takes with Scotia
69 McLeod?
- 70 MR. WELLS: No, I don't know the lady.
- 71 MS. BUTLER, Q.C.: I wonder if we could look at page 3 of
72 11, which is the second last paragraph, there you go, the
73 paragraph starting with "we suggest that Hydro institute a
74 dividend policy". I wonder Mr. Wells if you might read
75 that for me right to end of the letter which really isn't very
76 long.
- 77 MR. WELLS: Yes. "We suggest that Hydro institute a
78 dividend policy which will govern all future dividends. The
79 policy should have both a maximum debt to capital
80 structure test and a target payout ratio with respect to
81 earnings. We believe that the capital structure should re-
82 leverage no greater than 80% debt to 20% equity.
83 Therefore, no dividend would be payable if the posted
84 dividend ratio exceeds this level. By instituting this cap
85 Hydro will mitigate the negative effect that the payment of
86 a large dividend might have on the rating agencies and the
87 bondholders. The dividend policy should also include a
88 target payout level of 75% of net income. It might be
89 desirable to segregate the income of Hydro and CF(L)Co
90 for purposes of this test in order to ensure that CF(L)Co
91 retains some cash for debt retirement". Continue?
- 92 MS. BUTLER, Q.C.: Thank you, yeah.

1 MR. WELLS: "For comparative purposes it is worth noting
2 that the payout ratios for Canadian utilities, Nova Scotia
3 Power and Trans Alta, are 66%, 71%, and 83% respectively.
4 Those ratios for the investor-owned electric utilities are
5 broadly in line with the 75% payout ratio we feel would be
6 appropriate for Hydro. We recommend that these two
7 ratios provide the basis for any dividend policy instituted
8 by Hydro. This payout structure will be competitive to all
9 other provincial-owned utilities and therefore should be
10 quite acceptable by the Province of Newfoundland.
11 Indeed, the test suggested would result in a payment for
12 the current year which corresponds closely to the figure
13 quoted in the budget speech".

14 MS. BUTLER, Q.C.: I think that's fine.

15 MR. WELLS: Okay.

16 MS. BUTLER, Q.C.: We don't need the last part there.
17 Thank you.

18 MR. WELLS: And obviously the Board was influenced by
19 that opinion.

20 MS. BUTLER, Q.C.: Clearly, yeah, because this is April '95
21 and the policy was passed in November '95, consistent with
22 it.

23 MR. WELLS: Yeah.

24 MS. BUTLER, Q.C.: The Scotia McLeod's letter, as I
25 understand it Mr. Wells, is about total return to
26 shareholders and I want to refer you back to the first page
27 of the letter, last paragraph, there you go. Last paragraph
28 of that page. It says "it was found that dividends were not
29 the only form of monetary transfer to the provinces.
30 Several of the utilities, like Hydro, paid guaranteed fees on
31 the long term debt and some also paid water rental fees.
32 Therefore, we believe that one of the most relevant figures
33 is the total amount of transfers to the Province as a
34 percentage of book equity." And I think we've established
35 today, Mr. Wells, that in this particular case we have
36 dividends proposed for the test year of \$70 million and we
37 also have, of course, the debt guarantee fee to the Province
38 which is not anticipated to disappear of 1% or about \$11 -
39 12 million.

40 MR. WELLS: Yes. Uh hum.

41 MS. BUTLER, Q.C.: Thank you. At 75% we saw from this
42 letter that Scotia McLeod's recommendation was consistent
43 with other publicly owned utilities. Do you accept that?

44 MR. WELLS: They listed some. It's certainly not
45 consistent with the couple of utilities that come to mind.
46 BC Hydro, I think would have a far higher payout ratio.
47 Manitoba Hydro and New Brunswick Power's debt/equity
48 ratio I think is 99-1.

49 MS. BUTLER, Q.C.: As President of Hydro, can you refer
50 me to any other utility, publicly or privately owned, that is
51 paying out a dividend of 730%?

52 MR. WELLS: Not to my knowledge.

53 MS. BUTLER, Q.C.: And you agree with me also that the
54 payment of the 730% dividend, that's the \$70 million in this
55 test year, is more than enough to catch up for the years
56 that dividends less than 75% were paid out.

57 MR. WELLS: It will exceed, yeah.

58 MS. BUTLER, Q.C.: It will far exceed it, yeah.

59 MR. WELLS: Uh hum.

60 MS. BUTLER, Q.C.: Now on behalf of Newfoundland
61 Power one of the experts we engaged has made a
62 recommendation that if this Board considers 730% or \$70
63 million to be excessive, it can deem a capital structure for
64 rate setting purposes that assumes that only a reasonable
65 dividend is paid. Were you aware of this recommendation?

66 MR. WELLS: I'm aware, but I've read, don't ask me the
67 particular sentence but I am aware of that recommendation.
68 Yes.

69 MS. BUTLER, Q.C.: Okay, thank you. Do you accept that
70 recommendation as reasonable?

71 MR. WELLS: Well it's a matter of opinion. It's an opinion.

72 MS. BUTLER, Q.C.: What's yours?

73 MR. WELLS: My opinion is that it depends entirely on
74 what the Government as shareholder, the circumstances
75 that it's in and what it sees for the future in terms of
76 dividends from Hydro. If this is a one time, one shot deal at
77 these levels and the previous five, six years are more
78 reflective of where the Government sits with respect to
79 dividends then I don't think that this is an aberration that
80 will (a) contravene the Board's objective, the Public Utilities
81 Board 80/20; or contravene Hydro's Board to get at least to
82 that and then move beyond it, or convene what I've
83 expressed in my evidence on behalf of Hydro and Mr.
84 Osmond that we should be targeting over the longer term
85 at least 75/25 and then the 60/40. I think, in the pre-filed
86 testimony of Mr. Osmond he addresses this in the
87 particular and suggests that we should look for some
88 (inaudible) government policy before embarking on rates
89 that would lead us to that objective of 60/40, so we're
90 talking much, we're talking longer term here for that 60/40
91 objective, but that should not negate the principle that I
92 referred to earlier that, and there will be debate and
93 argument on it that Hydro in the first instance should be
94 looked as an entity indifferent with respect to who the
95 shareholder is and see what should apply to Hydro in the
96 normal course of circumstances and what factors you

1 would use to adjust from there.

2 MS. BUTLER, Q.C.: In listening to your answer, I gather
3 that what you're suggesting is that provided this is a one
4 time only, you don't necessarily speak against the payment
5 of the \$70 million dividend. Is that what your saying?

6 MR. WELLS: Yeah, well I mean, actually I got very little
7 say in the matter, in terms ... only as a member of the board.
8 The shareholder you know determines that requirement.
9 The shareholder is entitled to recapture retained earnings,
10 but I think that, you know, being practical about all of this,
11 this is obviously an issue related to the fiscal position of
12 the Province. I mean, unlike an investor-owned utility, if we
13 do make money it will go into one of two things. It will
14 either go to retire our debt or it will go to the taxpayers of
15 the Province. And, you know, it's one way or the other,
16 and what we're trying to get in balance here in terms of the
17 board of Hydro or the management of Hydro is to run the
18 utility to the best of our ability as a normal commercial
19 entity and treat it as an investor-owned utility which the
20 legislation as we've indicated seems to suggest.

21 MS. BUTLER, Q.C.: So that we're clear though Mr. Wells,
22 Newfoundland Power takes no issue with management's
23 ability to declare a dividend. Newfoundland Power takes
24 issue with the rate impact of the payout of the dividend.

25 MR. WELLS: I appreciate that. I appreciate the intervenors
26 would take that position.

27 MS. BUTLER, Q.C.: Right, and when you talk about the
28 dividend, perhaps being a one time only I wonder just look
29 at NP-72, page 2 of 2 again, and while that's coming up on
30 the screen, do you recall that Ms. McShane, one of your
31 experts, has said, or recommended that the dividend policy
32 should be supportive and predictable?

33 MR. WELLS: Yes, I'm well aware of that.

34 MS. BUTLER, Q.C.: And looking at the screen, as you can
35 see from the last column, with percentages ranging from 10
36 to 730% of net regulated operating income, it seems to me
37 that the dividend policy is hardly predictable.

38 MR. WELLS: Yeah, it ...

39 MS. BUTLER, Q.C.: Do you agree with that?

40 MR. WELLS: Well I understand the circumstances that the
41 government of the day is saying to us each and every year
42 but it provides a certain amount of concentration for
43 somebody like Mr. Osmond who is Vice-President of
44 Finance to be, and in our budgets and everything else, you
45 know, we would like predictability and I think that Ms.
46 McShane's comments reflect what you would normally
47 hope for. The other thing, all I can say is that it depends
48 on the circumstances with the shareholder and I don't read
49 into the fact that the current issue given the track record

50 over the brief period of dividends and the many years when
51 there were no dividends requested that we can't get into a
52 stable and predictable pattern with Government. I mean, at
53 that rate of recapture there is going to be very little equity
54 left in the company and then you can't get a return on non-
55 existent equity. So obviously minds are going to be, advert
56 to these factors in future and may already have. We just
57 don't know.

58 MS. BUTLER, Q.C.: Before I conclude then today I wonder
59 if I might just look at one final slide and Mr. Wells that is
60 IC-207, page 1 of 2. Can you scroll down please? There
61 you go. At line 18, Mr. Wells, you were asked, or Hydro
62 was asked under what, if any, conditions Hydro's Board of
63 Directors would limit or stop paying dividends in order to
64 advance towards achievement of its financial targets with
65 respect to the debt/equity ratio and the answer given was
66 that the dividend policy requires that such dividend shall
67 only be made after due consideration of the as being given
68 by the Board of the impact of such payment of the
69 debt/equity ratio. I'm not really certain that's an answer to
70 the question, so let me try again. Under what
71 circumstances would Hydro limit the dividend in order to
72 achieve a better debt/equity ratio?

73 MR. WELLS: What that question, you have to look at the
74 other questions preceding, I already referred to one and
75 Mr. Osmond's comment about the dividend level. The
76 board of directors have clearly set out a dividend policy of
77 the board in length in the first instance in '95 and in the
78 second instance to accommodate the Government request
79 with respect to export sales which seems reasonable and
80 mindful, based on presumably the advice that you've
81 already put forward, certainly part of the advice from the
82 financial advisors, of what they wanted to achieve in the
83 dividends and debt/equity ratios is on their mind. Now the
84 board has not changed its approach to this. The board has
85 not made a decision with respect to the declaration of
86 dividends that fall with the 2002 test year, nor has the
87 Government finally, finally, finally, confirmed that level of
88 dividends. Although it would be fair to say that they have,
89 under current circumstances, given no indication that there
90 may be any relief from what they've stated and whereas in
91 other years you'd pick up vibes that you know we're
92 looking for such and such but it may not have to be. So we
93 have to assume that that's it and the board will have to on
94 a certain day meet and declare the dividend and make, you
95 know, any modification of their policy or confirmation of
96 their policy at that time, because as I've indicated my
97 feeling on that is if this is a one time, one shot deal then
98 everything that our financial advisors have suggested and
99 from what we ourselves know that this movement upwards
100 in the percentage of debt is not going to have a negative
101 effect and that we can recover over a period of time going
102 forward and go towards our objectives. We have two, from

1 our point of view since we are not the actors in the case we,
2 this causes a problem in the sense of what your trying to
3 achieve in the same sense that the tremendous increase in
4 oil prices is a problem that we are trying to get over and
5 we're trying to reduce the impact on ratepayers by not
6 looking for the monies that oil is actually costing us today.
7 We're trying to smooth it out.

8 MS. BUTLER, Q.C.: But ultimately the payment of the
9 dividends in the test year have an affect on the ratepayers.

10 MR. WELLS: Yes, I agree then to the extent you stipulated,
11 yes.

12 MS. BUTLER, Q.C.: Thank you, Mr. Wells. Mr. Chairman
13 that would be a good place to stop if I might.

14 MR. NOSEWORTHY, CHAIRMAN: Thank you very much.
15 We'll conclude today's hearings and we'll reconvene this
16 hearing at 9:30 tomorrow morning.

17 *(hearing adjourned to September 25, 2001)*

18