

1 MR. NOSEWORTHY, CHAIRMAN: Good morning,
2 everybody, and welcome to those who perhaps didn't,
3 weren't here yesterday for the beginning of the hearing. I'd
4 like to ... this is municipal elections day in the province, I
5 guess, and being a former Deputy Minister of Municipal
6 Affairs I know the results of good government and bad
7 government firsthand, so I'd like to encourage everybody
8 to vote today and I guess with that in mind (*laughter*) I'd
9 like to, for the benefit of the staff, I think the law dictates
10 that we require four clear hours to vote, so I will be trying
11 to clue up at or before promptly four o'clock this evening,
12 for the benefit of the staff in the room and others outside.
13 If that's possible, I'd like you to consider that as we go
14 through this evening.

15 The transcription services, I believe the e-mail
16 would have gone out at something like 12:22, not
17 suggesting that anybody was up at that hour or sitting in
18 front of their monitors waiting for the e-mail on the
19 transcription of the day's events, but I think that's quite a
20 reasonable turnaround time. If we can try and maintain that
21 at least it will be available for everybody early in the
22 morning to review their e-mail and with a view you should
23 have the paper copy by now as well, so I want to commend
24 the transcription people for that and hopefully we'll be able
25 to maintain that standard throughout this hearing.

26 That's all I would have. Is there anything else that
27 anybody would wish to raise before we begin this
28 morning? Okay. Having heard nothing, I would ... I
29 probably won't be asking that on every occasion every
30 morning. I would prefer perhaps if items that anybody
31 would wish to raise that they would bring them to the
32 attention of Board counsel prior to the start and we'll try
33 and deal with them then but I would not likely be asking
34 that every morning so that we can get right into the hearing
35 and proceed on with the matter at hand.

36 Okay. I'd like to continue on, I guess, from
37 yesterday, Mr. Wells and Newfoundland Power in terms of
38 their cross-examination, please. Ms. Butler.

39 MS. BUTLER, Q.C.: Thank you, Mr. Chairman. I should
40 say too that perhaps by the mid-morning break I can give
41 a revised projection as to how long I'll be with Mr. Wells
42 today.

43 MR. NOSEWORTHY, CHAIRMAN: That would be
44 appreciated. Thank you.

45 MS. BUTLER, Q.C.: For the benefit of the earlier break.

46 **MR. WILLIAME. WELLS, XX'D BY MS. BUTLER, Q.C.**
47 **(HEADING?)**

48 MS. BUTLER, Q.C.: Good morning, Mr. Wells.

49 MR. WELLS: Good morning.

50 MS. BUTLER, Q.C.: Yesterday I addressed the guarantee
51 fee in a general way. What I'd like to speak to you a little
52 bit about this morning is the, to focus on the guarantee fee
53 perhaps as a fixed cost of Hydro's and its relationship to
54 Hydro's target debt equity ratio. The evidence in the pre-
55 filed documents confirms that the Government charges
56 Hydro a guarantee fee of one percent.

57 MR. WELLS: Yes.

58 MS. BUTLER, Q.C.: I wonder, Mr. O'Reilly, can we look at
59 NP-77, to have some sense of what that has amounted to
60 over the last few years and projected? We should be able
61 to get all of that on the one screen. Can we enlarge it
62 slightly? That will have to go back a little bit. Yeah, okay.
63 Mr. Wells, as you can see from this page two of two, NP-
64 77, the guarantee fee has amounted to between 10, I'm
65 sorry, yeah, almost 10, 9.983 million is the lowest in 1994 to
66 11.223 million in the year 2000, and I see it's projected to be
67 12.336 million in 2001. Is that correct?

68 MR. WELLS: Yes.

69 MS. BUTLER, Q.C.: Now, would this document in front of
70 us ... I should tell you Newfoundland Power takes no issue
71 of course with the size of the guarantee fee while Hydro
72 currently has a debt equity ratio of 80/20, but your pre-filed
73 testimony suggests that Hydro strives to reduce your debt
74 equity ratio to 60/40.

75 MR. WELLS: Over a long-term. That's the
76 recommendation of our financial advisors and our expert
77 witnesses.

78 MS. BUTLER, Q.C.: Which recommendation Hydro has
79 accepted.

80 MR. WELLS: Which we concur, that would be the
81 desirable objective.

82 MS. BUTLER, Q.C.: And yesterday you confirmed your
83 evidence which had been in your pre-filed that the
84 Government guarantee of Hydro's debt permits Hydro to
85 operate with a different capital structure for its operations.

86 MR. WELLS: Yes.

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

88 MR. WELLS: It's one factor that certainly assists.

89 MS. BUTLER, Q.C.: I wonder if we might look at NP-74, the
90 last sentence. Okay. Mr. O'Reilly, maybe we could just see
91 the question there for Mr. Wells' benefit. Okay. The
92 question that was put to Hydro in this instance was to
93 provide documentation to support the assertion of the
94 movement towards debt equity ratio of 60/40 would result
95 in a change in the requirement for Hydro to pay a debt
96 guarantee fee to the Provincial Government.

1 MR. WELLS: That's a question of Mr. Hall. This is Mr.
2 Hall's pre-filed testimony.

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

4 MR. WELLS: Okay.

5 MS. BUTLER, Q.C.: I agree, but looking at the answer that
6 was given on behalf of Hydro, starting at line ten, "In
7 Canada there are many regulated businesses with an
8 investment grade rating that operates successfully and
9 access capital without Government assistance. In this
10 circumstance the Province and the Utility could consider
11 the removal of the guarantee and related fee with little or no
12 impact to the consumer." You accept, Mr. Wells, the link
13 between the guarantee fee and the debt equity ratio. I
14 understood that to be an admission you made yesterday.

15 MR. WELLS: There is a link, yes. It's a fact.

16 MS. BUTLER, Q.C.: It is a fact. In the financial plan that
17 we dealt with yesterday, which I don't think we need to get
18 up on the screen but if we do I can ask, can you tell me
19 whether the financial plan of Hydro contains any reference
20 to Hydro's intention to reduce the debt equity ratio to
21 60/40?

22 MR. WELLS: The five-year plan?

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

24 MR. WELLS: No.

25 MS. BUTLER, Q.C.: Given that it is, however, part of
26 Hydro's application in the sense that it is stated as Hydro's
27 long-term intention, can you tell the Board how the Board
28 can endorse the principle of improving the debt equity ratio
29 without knowing the impact on consumers?

30 MR. WELLS: Well if one were to look at the financial
31 entity, Newfoundland and Labrador Hydro, and, as I said
32 yesterday, in the first instance just look at that and be
33 indifferent to the actual ownership and then over time in
34 our society and financial structures there are set-ups which
35 describe how one can finance in the marketplace and at
36 what cost, and to what degree of risk are companies
37 exposed to, so Mr. Hall's evidence, and in part, and Ms.
38 McShane's, say that if you take that approach, then you
39 will get the true picture within our financial structures of
40 what the real cost is, what the risks are and what people
41 getting the service from that particular entity should expect
42 to pay. So the issue comes in two parts, the financial
43 structure of Hydro and then there are the consequent costs
44 of that with respect to ratepayers and rates, and in the case
45 of Hydro the issues of the cost that have nothing to do
46 with the capital structure such as the cost of fuel. There's
47 nothing more in this than that that we should have, that the
48 Board should have a good look at the kind of capital
49 structure that you would require to make sure that Hydro

50 is in keeping with the legislation as operating on a sound
51 financial basis, that's the requirement of the legislation, and
52 the financial experts can assist in defining what are the
53 things that you look at in determining that. Mr. Hall
54 particularly in his evidence, and he will be examined, can
55 best speak for himself, but he would say and has said in his
56 pre-filed testimony that if we had a 60/40 debt equity ratio
57 as a corporation we should be able to get an investment
58 grade rating in the capital markets, which would be, say,
59 Triple B, and then we would not be at issue with respect to
60 the financial requirements of the Government. It would
61 mean for certain that taxpayers are not subsidizing
62 ratepayers and we could not then have any effect on the
63 financial situation of the province or any negative impact.
64 We would be neutral. That's the world of which they are
65 speaking, the financial experts, and the issue for the
66 hearing is, we can't reach that world in the short-term, not
67 without having significant impact on ratepayers in light of
68 other things that are impacting the rates, so we say in the
69 longer term it would be desirable, but I think that Mr. Hall
70 and others may confirm to you that the Government
71 guarantee provides other good benefits to Hydro and
72 therefore to the cost of the system and to ratepayers
73 because we can access the capital markets pretty well at
74 any time with the Government guarantee. We have all the
75 expenses related to filing prospectuses and that taken off
76 our ... there's an advantage there. For that advantage we
77 pay one percent of the debt. It's a good deal. It's a good
78 deal, and, you know, if an investor (unintelligible) utility
79 could get that kind of a deal, it's not a bad deal, and the
80 benefits really do flow back to the consumers, our
81 industrial customers and Newfoundland Power and
82 Newfoundland Power's customers.

83 MS. BUTLER, Q.C.: So I was going to just take what
84 you've told me perhaps in small pieces. First of all, the debt
85 guarantee fee which is paid is for general credit support.

86 MR. WELLS: General credit support?

87 MS. BUTLER, Q.C.: Yes. That's the purpose of a debt
88 guarantee fee.

89 MR. WELLS: Yes.

90 MS. BUTLER, Q.C.: And for the period covered by the
91 financial plan, 2001-2005, I see no reference to the debt
92 guarantee fee disappearing, so it is a reality for that
93 financial planning period.

94 MR. WELLS: Oh, yes.

95 MS. BUTLER, Q.C.: Okay. And in that financial planning
96 period it is also a reality that Hydro is not forecasting the
97 debt equity ratio to go below the 80/20.

98 MR. WELLS: I don't think realistically that it's going, it
99 would be ... it'd depend on circumstances but highly

1 unlikely in that time frame.

2 MS. BUTLER, Q.C.: Well I think the plan that we saw
3 yesterday actually showed the debt equity ratios intended
4 and it did not drop below 80/20. What this expert on your
5 behalf will likely say if he stands by his testimony is that if
6 you could achieve 60/40 you may not have a debt equity,
7 I'm sorry, you may not have a guarantee fee at all.

8 MR. WELLS: He would say one would not require it for the
9 purposes of obtaining an investment grade rating.

10 MS. BUTLER, Q.C.: Okay. So I think we're in agreement on
11 those basics. What I want to ask you about though is this,
12 when it is (phonetic) after 2005, as the level of equity
13 increases slowly, because you say this is a long-term goal,
14 do you agree that the amount of the guarantee fee can be
15 reduced to reflect the rate at which Hydro could borrow
16 independently in the capital markets?

17 MR. WELLS: As I understand it, and I'm not the best
18 witness for the Board on these matters, but we'll have
19 others, unless we had a 60/40 debt equity ratio, we're
20 unlikely to get an investment grade rating in our own right,
21 so even at 75/25 debt equity ratio and subject to the
22 confirmation of expert witnesses, I would not expect that
23 we could get an investment grade rating, you know,
24 without, in the absence of a government guarantee. The
25 evidence or the testimony and our briefings all relate to the
26 fact, and Ms. McShane and Mr. Hall, that you really got to
27 get to that 60/40 debt equity ratio to get the investment
28 grade rating, and therefore I conclude personally that 70/30
29 wouldn't cut it but I would prefer that you ask them that
30 question.

31 MS. BUTLER, Q.C.: I will but my, for today's purposes
32 then, what I hear you saying is that during the transition
33 period from 80/20 to 60/40 you would not expect any
34 reduction in the guarantee fee.

35 MR. WELLS: That would depend on the shareholder, but
36 they're providing the full guarantee and therefore why
37 would they reduce the percentage that they, you know, the
38 one percent for that guarantee, because they would have to
39 stand to the entire debt if called upon and therefore it's not
40 a situation of trying, or reducing their risk over time. The
41 debt will still be there and the full debt would be
42 guaranteed, therefore the full fee of one percent would be
43 presumably required.

44 MS. BUTLER, Q.C.: I wonder if we can just go back to that
45 screen which is NP-77, the actual amounts of the guarantee
46 fee paid out historically. Enlarge that to 125, I think. That's
47 what we saw last time. 130, okay. Thank you. One of the
48 questions that Newfoundland Power put to Hydro was
49 what would happen if you treated this guarantee fee as a
50 return on equity. Do you recall that question being put?

51 In other words ...

52 MR. WELLS: Yes. So it's all filed and the answer was, or,
53 is filed as well.

54 MS. BUTLER, Q.C.: The answer we can see at NP-80.
55 Treating the guarantee fee as a return on equity is
56 suggesting that the Government as shareholder is getting
57 the guarantee fee back of course as part of its investment
58 in Hydro. The answer that was given, okay, is attached in
59 a calculation, and I think it's suggesting that the difference
60 it makes is about 15 points on return on equity. It's shown
61 as the forecast in 2002. I'm sorry, five points.

62 MR. WELLS: Well the calculations would be as we have
63 provided. Perhaps the better witness would be either the
64 Controller or the Vice-President of Finance, you know, and
65 in terms, they provided the answer to that and the
66 calculation. Again, this is just a mathematical result.

67 MS. BUTLER, Q.C.: Mr. Wells, I wonder if you could tell
68 me specifically who you would prefer I defer that question
69 to?

70 MR. WELLS: It's really the Vice-President of Finance.

71 MS. BUTLER, Q.C.: And his name?

72 MR. WELLS: Mr. Osmond.

73 MS. BUTLER, Q.C.: Mr. Osmond?

74 MR. WELLS: Yeah.

75 MS. BUTLER, Q.C.: I'd like to turn now to just a very few
76 questions on the topic of operating expenses, Mr. Wells,
77 because I appreciate as President this is not necessarily
78 your area. But on the topic of permanent and temporary
79 staff positions you did mention to me yesterday some
80 downsizing in 1996. I wonder can we look at NP-6, page
81 two of four? Here we have staffing levels, permanent and
82 temporary, for Hydro for the period 1992 right through to
83 projected 2002. Let's start with 1995, Mr. Wells, because
84 the year you focused on yesterday was 1996. Okay. Do
85 you have a pen and paper in front of you?

86 MR. WELLS: Yes. Is this Mr. Roberts' testimony, pre-filed
87 testimony that you're looking at?

88 MS. BUTLER, Q.C.: I'm looking at NP-6 which was a
89 question put by ...

90 MR. WELLS: Oh, to ... after, yes, okay.

91 MS. BUTLER, Q.C.: Okay. And I'm addressing this with
92 you because you mentioned it specifically yesterday.
93 "1995 we had 961 permanents and 135 temporaries for a
94 total of 1,096," and then in the next year, which is the year
95 you focused on, 1996, we had 918 and 131 for a total of
96 1,049, so there is a reduction there of about 50 overall.

1 MR. WELLS: On these figures, yes, yes.

2 MS. BUTLER, Q.C.: Yes. 1997, 904 and 127 for a total of
3 1031, and in 1998 we see it starting to climb back up, 889
4 plus 169 for a total of 1058, and in 1999, 901 permanents
5 plus 184 temporaries for a total of 1,085, and finally in 2000,
6 the last full year for which we have figures, 891 plus 188 for
7 a total of 1,079. So my point, I guess, is that there was
8 some success in reducing the overall number of positions
9 from '95 to '96, '96 to '97, but then it started to climb back up
10 in '98, '99 and 2000, shows the numbers much the same
11 really, no great loss of jobs related to the exhibit. So can
12 you tell me how this relates to the evidence you gave
13 yesterday in terms of the Company's overall success?

14 MR. WELLS: Yes. As I mentioned yesterday, that there
15 had been a downsizing in 1996 in May and there had been
16 a continuous reduction since, as these figures will show, in
17 the number of permanent positions, not as many ... actually
18 in '96 I think it was 66 jobs that were reduced in May and
19 then there were other changes, and then in, and the full
20 impact of that was seen in 1997 because we paid off those
21 costs in 1996, associated with the reduction in the
22 permanent staff. In 1998 and 1999 we had more temporaries
23 coming on because we were in the process of what we
24 called our Project 2000 and the new computers we related to
25 the hardware acquisitions and the Y2K, so there was a lot
26 of backfilling and use of temporary people, and the other
27 thing, and I think Mr. Reeves would be best to ask about
28 that, but when you look at some of the numbers, it's broken
29 down into each division, and you'll see in TRO there is an
30 increased number of temporary employees and there are a
31 number of factors related to that where there were more
32 temporaries taken on which increased that number, but
33 actually that was beneficial in terms of the ongoing
34 reorganization of TRO, which is also described in the
35 evidence. We were holding permanent positions open and
36 using the temporary positions to allow us ... for instance in
37 this year, in the spring, we announced the removal of 41
38 positions from the, where there were 41 positions affected
39 in the complement, and the actual number of permanents in
40 terms of people in the position, it was much less than the
41 number in terms, the effect on permanent employees, the
42 positions were vacant and staffed by temporaries and it
43 had a lesser result, you know, in terms of impact on
44 permanent employees. So you will note, and as dependent
45 on the witness who's testifying on behalf of Hydro, why in
46 particular instances there were more temporaries on in a
47 particular year related to Project 2000 and the Y2K issue
48 related to the reorganization in TRO which in fact were, in
49 our view, more beneficial moves and helped us to achieve
50 our resulting cost reductions. The other thing that would
51 affect temporary employees depends on the nature of any
52 particular project that you're doing at a particular time, and
53 it would come out in that, and so I would suggest that you

54 can, when you look at production, finance and TRO, the
55 witnesses that represent those particular divisions can
56 speak to the temporary numbers fluctuation a little better
57 than I.

58 MS. BUTLER, Q.C.: Okay, I accept that. The exhibit
59 certainly reflects a decrease in permanents but an increase
60 in temporary staff over this period.

61 MR. WELLS: Yes. The figures will show that.

62 MS. BUTLER, Q.C.: Do you anticipate the reduction in
63 temporaries that you've ascribed to Project 2000 and the
64 J.D. Edward (phonetic) software now that that project is
65 installed?

66 MR. WELLS: Yeah, that's already occurred and you'd have
67 to look at ... that's why I say, when you look in, within each
68 department where the adjustments were ... the other thing
69 I should mention to you is that figures can be misleading
70 because you can reduce your permanent staff and contract
71 out work and then it'll never show on your temporary
72 numbers, and therefore when you're seeing what people or
73 companies are doing with respect to permanent staff, you
74 have to look, you should look at also, you know, how many
75 temporaries are coming on and for what purpose the Board
76 would be interested and what purpose were they brought
77 on and to, for what objective, but the whole figure won't tell
78 you much unless you said to somebody, well, are you
79 laying off permanent employees and contracting out your
80 work, and then your temporary figure would be low, your
81 permanent figure would be low, but the cost in terms of
82 getting the work done would still be there.

83 MS. BUTLER, Q.C.: What has Hydro's position been with
84 respect to contracting out work in this period?

85 MR. WELLS: We will contract out where we can work,
86 where we have the opportunity to contract out if it's
87 beneficial in terms of costs. One issue that we do have
88 that, in our collective agreements, there's a prohibition of
89 contracting out work which results in layoff of permanent
90 staff, and, you know, that has a restraint with respect to
91 contracting out of work.

92 MS. BUTLER, Q.C.: Mr. Wells, I'm going to turn now, if I
93 might ... well, actually before I do that can you let me know,
94 please, to whom you feel any questions in relation to the
95 details of staffing should be put?

96 MR. WELLS: Well, I think that Mr. Reeves for TRO. He's
97 the Vice-President of TRO so he could better explain, you
98 know, the ... because, as you'll note from figures in TRO,
99 the number of temporaries will vary. In Finance you'll see
100 a variation and to a much lesser extent in production. I
101 think that, and Mr. Henderson will be testifying later with
102 respect to production and, or Mr. Budgell, but when these
103 witnesses from each division appear, then you can deal

1 with the particulars and you would be, I think it would be
2 preferable and more pertinent than dealing with me on the
3 individual variations on temporary employees, but we agree
4 these are the figures.

5 MS. BUTLER, Q.C.: Mr. Wells, I'm pursuing this of course
6 because of the general statement that you made yesterday
7 in answer to another question. Before I leave it then for
8 particulars to another witness, can you just give me an
9 overall corporate summary of where the contracting out
10 might sit with the exhibit that we were provided with that
11 shows permanents and temporaries only?

12 MR. WELLS: Yes. Well I think that in terms of the cost
13 factors, that while we are contracting out, and there's a
14 great deal of consternation, you know, from our union with
15 respect to any contracting out because as any company
16 knows that employees, unionized employees don't like to
17 see contracting out that may affect their work, so, and we
18 cannot do it in contravention of our collective agreements,
19 but where the collective agreements are not preventing us
20 from contracting out, if we can find a more cost-effective
21 way to get the work done, we will contract out, and one of
22 the factors which will come through Mr. Henderson's
23 evidence is to be seen in the way we have operated the
24 Holyrood plant in the last, by contracting with the original
25 equipment manufacturer to do our major overhauls, and the
26 result has been quite dramatic. We have in excess last year
27 of a 75 percent availability of the plant, which was a target
28 we set, and we've increased the efficiency of the plant and
29 had a little celebration of the results of last year and gave
30 the employees all a jacket because the combination of
31 things, we had reduced the amount of fuel consumed and
32 saved a significant amount of money. So that contracting
33 out of necessary work was to our advantage, I think, of the
34 Corporation and to everybody who depends on it. It has
35 certainly been a sore point with the union which had a large
36 number of temporary employees who'd come on in the
37 summer to do these overhauls and so we've changed the
38 approach. Does that sort of answer in the area of what
39 you're looking for?

40 MS. BUTLER, Q.C.: Thank you. What I'm hearing is that
41 of course this exhibit does not reflect the contracted out
42 position.

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

44 MS. BUTLER, Q.C.: And generally can you just tell me
45 whether in the period '96 to 2000 the number of contracted
46 out positions at Hydro actually increased?

47 MR. WELLS: The number of contracts? I couldn't ... I can't
48 say they increased or decreased but I can say that in this
49 whole issue, our controllable costs, I mean, the pressure is
50 on everyone to ensure that we're doing things in the most
51 cost-effective manner and we can get that for you. I'm not

52 sure if the arithmetic number of the contracts is up or down.
53 It would depend on the requirements of a particular year.

54 MS. BUTLER, Q.C.: That's fine. I wonder though whether
55 I could ask you just to give me an undertaking to give me
56 that information?

57 MR. WELLS: Yes, we can provide that information, the
58 number of contracts that we've let.

59 MS. BUTLER, Q.C.: Okay, Mr. Wells, on the same topic of
60 permanent salaries, can we look also at NP-4 and here
61 Newfoundland Power noted that Hydro based its budget
62 for annual permanent salaries in 2002 on a full staffing
63 complement with an adjustment. If we can just go to page
64 two of three, Mr. O'Reilly, please? There you go. In
65 Category A ... thank you ... the first line is 44 million, 44.876
66 million, but then at the bottom line, Category A, we see a
67 vacancy adjustment of a million.

68 MR. WELLS: Yes.

69 MS. BUTLER, Q.C.: Okay. Now, historically, according to
70 the report of Mr. Brushett ... I think perhaps we should go
71 to that. That is on the screen or electronically stored, is it,
72 Mr. O'Reilly?

73 *(Discussion re location of documents. Speaker is away*
74 *from microphone.)*

75 MS. BUTLER, Q.C.: Thank you. Yes, and the top
76 paragraph ... oh, dear, I don't think we've got the same
77 document.

78 MR. KENNEDY: It's 25 of the PDF format. It's probably 26
79 or 27.

80 MS. BUTLER, Q.C.: The paragraph I'm looking for starts
81 with, "The Company budgets." There you go. Thank you
82 very much. Okay. Mr. Wells, I just draw your attention to
83 the opening paragraph of the Grant Thornton report for
84 2001 which indicates how the Company budgets its annual
85 permanent salaries. I wonder could you just read the
86 paragraph down to the reference to four percent, please?

87 MR. WELLS: "The Company budgets its annual
88 permanent salaries using the full staffing complement as
89 opposed to the number of filled positions. Based on our
90 review of prior years, Hydro generally never reaches its full
91 complement during the year, therefore it is likely that
92 salaries will come in under budget. Per our review of actual
93 and budgeted permanent salaries from 1997 to 2000, Hydro
94 has over-budgeted this category on average by four
95 percent." May I read the next sentence?

96 MS. BUTLER, Q.C.: Sure, go ahead.

97 MR. WELLS: "To compensate for this potential over-
98 budgeting, Hydro budgets a vacancy credit which is
99 included in the Finance Department forecast. The credited

1 budget," or "The credit budgeted for both 2001 and 2002 is
2 \$1 million."

3 MS. BUTLER, Q.C.: Now the Grant Thornton report goes
4 on to assess the reasonableness of the 2001 forecast for
5 permanent salaries. What I want to ask you is, looking
6 back, please, given the reference here to four percent as
7 being the historical over-budgeting, go back now to the
8 exhibit that we were looking at, which was NP-4, page two
9 of three ... there you go ... we have permanent salaries of
10 44.876 million and a vacancy adjustment of one million, but
11 using the Grant Thornton figure of four percent, what I'm
12 suggesting to you is that the vacancy adjustment should
13 actually be 1.8 million. Do you accept that that, according
14 to Grant Thornton's report ...

15 MR. WELLS: I think if I heard you correctly the Grant
16 Thornton review said four percent was the average. In any
17 particular year it may vary because the vacancy allowance
18 is not set at four percent. It's ... there's a different
19 percentage in each year but what we did do in 2001 and
20 2002 was use the \$1 million figure against a different top
21 line figure, so the percentage even there would change, so
22 I don't accept your, if you're asking me whether this should
23 be four percent here instead of the one million, I would say,
24 no, and I don't think that Grant Thornton review would
25 suggest that it's four percent. The percentage is derived
26 from the numbers of the permanent salaries and the
27 vacancy adjustment and then you'll find out in a year what
28 that percent was, and I think their report says the average
29 was four percent.

30 MS. BUTLER, Q.C.: I agree with your interpretation of the
31 report. The report says that historically in that earlier
32 period Hydro had over-budgeted by four percent. My
33 question to you was, if four percent turns out to be correct
34 for the forecast year, the vacancy adjustment would be 1.8
35 million instead of one.

36 MR. WELLS: If the average were applicable to that
37 particular year but averages are particular to many years
38 over which you determine an average. I don't think we're
39 going anywhere with this.

40 MS. BUTLER, Q.C.: Okay. We obviously will have to
41 agree to disagree on the point, but mathematically you
42 have no difficulty with my calculation of 1.8.

43 MR. WELLS: The math is correct. The problem is that the
44 amounts are arbitrarily determined, one could say, and then
45 you derive from that the math and the math over a number
46 of years will give you an average but the average doesn't
47 mean anything in any one year.

48 MS. BUTLER, Q.C.: No, but the amount of one million was
49 arbitrary too wasn't it?

50 MR. WELLS: Yes, but the point being that, and one of our

51 difficulties, and we are going to change that, is having full-
52 time equivalents, but the ... nobody is prejudiced by
53 putting in, as you say, over-budgeting 44 ... you know,
54 permanent salaries are over-budgeted, but everybody gets
55 the benefit of the vacancy adjustment. Nobody is over-
56 charged for permanent salaries. We put in an adjustment
57 to that and that will be corrected in the books over, you
58 know ... there's nothing untoward here, but if we had a
59 system of, for full-time equivalents, working it that way,
60 maybe we could eliminate this part of the process, and
61 again I defer to Mr. Osmond and Mr. Roberts and how
62 they, how that would work out.

63 MS. BUTLER, Q.C.: Okay. I'll leave that topic and move
64 now to the subsidy. Mr. Wells, then in your evidence at
65 page 19, and we can provide this for you on the screen, I
66 think, line four ...

67 MR. WELLS: Page?

68 MS. BUTLER, Q.C.: Page 19. Okay, line four. Thank you.
69 You say, "As the Board is aware, Hydro operates the rural
70 isolated and island rural interconnected systems at a loss."
71 The actual figure given in other evidence, not your own,
72 was that the amount of the deficit is \$26 million. Do you
73 accept that?

74 MR. WELLS: Yes. That's the figure we filed with the
75 Board.

76 MS. BUTLER, Q.C.: And the \$26 million of course is
77 subsidized by other ratepayers.

78 MR. WELLS: Yes.

79 MS. BUTLER, Q.C.: Okay. I'd like to ask you about
80 Hydro's inclusion of the deficit totalling \$26 million as part
81 of the revenue requirement for Newfoundland Power and
82 the Labrador interconnected customers. Hydro in this
83 application is seeking three percent return on equity short-
84 term.

85 MR. WELLS: Yes.

86 MS. BUTLER, Q.C.: And 11.25 return on equity mid-term.

87 MR. WELLS: Let me just clarify that. For the purposes of
88 this rate application we're seeking a three percent return on
89 equity. We are not asking the Board for a particular
90 defined percent of return for any year beyond the rates that
91 are affected by this application. The way we've put it to the
92 Board is that it would be wrong for everybody in the
93 financial community to have an understanding that the
94 Public Utilities Board of Newfoundland accepts three
95 percent rate of return for any utility as an appropriate return
96 and that they should indicate to the rest of the world why
97 we accept, if the Board does, because we don't know what
98 the Board is going to do yet, but if the Board accepted our
99 three percent for the purpose of setting rates for the next

1 couple of years, they would also say as an aside to the rest
2 of the world and the financial community, we think that the
3 appropriate rate of return in normal circumstances is "X,"
4 and I'm pretty confident that that "X" won't be three
5 percent, so we're not asking the Board to commit to
6 something that will adjust or affect Hydro's rates beyond
7 what we intend would be the term of the rates for this
8 hearing, and we've already filed and indicated in our pre-
9 filed testimony that we will be back to the Board in 2003 for
10 a 2004 test year. That seems to be essential and dictated by
11 the facts of the matter. So it ... and somebody mentioned
12 that yesterday, either in the opening statements or not, we
13 are not asking the Board to commit to Hydro any rate of
14 return beyond three percent for a defined period. We are
15 saying to the Board, and for the protection of the Board
16 and every Newfoundlander, that you really have to turn
17 and indicate to the rest of the world what, you know, where
18 one could expect this regulatory authority to look in terms
19 of rate of return for a regulated entity under its jurisdiction,
20 and of course our expert witnesses and others will debate
21 that and try to influence the Board as to what that should
22 be, but the Board will, in its own good judgement,
23 determine that.

24 MS. BUTLER, Q.C.: Thank you for clarifying that. As a
25 matter of public or social policy there is a \$26 million deficit
26 which is incurred at the request of your shareholder, the
27 Government.

28 MR. WELLS: Yes.

29 MS. BUTLER, Q.C.: And that is recovered as a subsidy
30 from other ratepayers rather than recovering the cost of
31 service from the customers.

32 MR. WELLS: Yes.

33 MS. BUTLER, Q.C.: Okay. If the \$26 million that we're
34 talking about was treated as a return to shareholder rather
35 than a cost to be recovered from Newfoundland Power and
36 the Labrador interconnected customers, it would result in
37 a higher return on equity.

38 MR. WELLS: Yes.

39 MS. BUTLER, Q.C.: Okay. And that would be of course
40 consistent with one of Hydro's objectives, which is to
41 improve the debt equity ratio.

42 MR. WELLS: Yes, the mathematics will produce a certain
43 result where you're attributing ... the \$26 million deficit is
44 really a benefit to the shareholder and what it incorporated
45 in the debt equity structure of the Corporation, so what
46 you're saying is right. I don't want to be implicated in your
47 thoughts that I might be agreeing with you that that's the
48 proper approach.

49 MS. BUTLER, Q.C.: I didn't ask you that. I'm going to turn

50 now, Mr. Wells, to progress in reducing the rural deficit, if
51 I could.

52 MR. WELLS: Yes.

53 MS. BUTLER, Q.C.: The report on rural rates, July 29th,
54 1996, and, Mr. O'Reilly, I don't know where you have this
55 stored. I'm looking for the report, pages 32 ... don't have it?
56 I'm going to ask you some questions about it that perhaps
57 you may be able to answer from memory. I don't ... I won't
58 get into specific quotes that may require you to have a hard
59 copy. We know from your evidence of course that you
60 accept that the Board at that time recommended that
61 preferential rates be phased out.

62 MR. WELLS: Yes.

63 MS. BUTLER, Q.C.: Okay. And the phase-out period that
64 they indicated at that time was to be five years.

65 MR. WELLS: Yes.

66 MS. BUTLER, Q.C.: As a separate recommendation the
67 Board recommended that a new rate be designed for federal
68 and provincial departments and agencies.

69 MR. WELLS: Yes.

70 MS. BUTLER, Q.C.: And that those rates also be phased
71 in over five years.

72 MR. WELLS: Yes.

73 MS. BUTLER, Q.C.: To recover full costs, 100 percent cost
74 recovery. Do I understand your evidence correctly, Mr.
75 Wells, that at this point Hydro has done neither?

76 MR. WELLS: To this point.

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

78 MR. WELLS: Yes.

79 MS. BUTLER, Q.C.: And in this ...

80 MR. WELLS: We do have a proposal ...

81 MS. BUTLER, Q.C.: Yes, I see that, yeah.

82 MR. WELLS: ... in our application.

83 MS. BUTLER, Q.C.: Yeah. In this hearing Hydro is
84 proposing a 20 percent increase in the 2002 Government
85 rates, but again not to full cost of service. Is that correct?

86 MR. WELLS: That's correct. That would be inconsistent
87 with the Board's recommendation that it be phased in over
88 five years.

89 MS. BUTLER, Q.C.: Are you suggesting that the 20
90 percent increase will give you the full cost of service?

91 MR. WELLS: No.

92 MS. BUTLER, Q.C.: No?

1 MR. WELLS: I'm suggesting ... you said ... responding to
2 your comment or question that what we propose in this
3 application is a 20 percent increase to the Government
4 rates, preferential rates. The Board's recommendation was
5 that the full cost of service be applied to that class of
6 customer and that it be phased in over a five-year period.
7 What we are proposing in our application is an initial 20
8 percent and then we said we would give the Board a rate
9 structure over a five-year period at our next application
10 which would then become effective, for argument's sake, in
11 2004, and that's a bit of a departure from what the Board
12 had recommended like a continuum of increases over a five-
13 year period, and the only reason we're suggesting that to
14 the Board who will decide the issue was because of the
15 overall magnitude of the increases that are going to occur
16 as a result of the impact of No. 6 fuel costs on the system.
17 The Board will decide that. We are just suggesting an
18 approach that if we charge the two governments, who have
19 the benefit of preferential rates today, 20 percent now and
20 then in a five-year period commencing in 2004, we would
21 eliminate that deficit. That would, I guess, be a little
22 inconsistent from the Board's taking a five-year period in
23 the first instance, and the Board can assess that in the
24 reasonableness of the overall rate increases. The second
25 point of course is that while the Board made that
26 recommendation in its '96 report, it was to be something
27 that brought to it in the course of a general rate application
28 by Hydro, so this was the first opportunity that we had in
29 terms of a general rate application to bring this issue back
30 and consider the Board's direction.

31 MS. BUTLER, Q.C.: The proposal that Hydro has put in
32 the application, that this await Hydro's next application,
33 Hydro's next application in 2003?

34 MR. WELLS: Yes. We anticipate that we will have to file
35 a rate application in 2003 which, and which would result in
36 a test year of 2004 and new rates effective then.

37 MS. BUTLER, Q.C.: Now, Mr. Wells, your testimony, and
38 we'll get Mr. O'Reilly to put that up, page 14, I'm looking for
39 line 28, and I think you might have mentioned this this
40 morning too ... scroll down a little further there. Thank you.
41 You're talking about again the debt equity ratio, but the
42 statement is made there, line 28, 29, "The taxpayers
43 implicitly are subsidizing ratepayers to some degree."
44 What I want to ask you about in relation to this issue, and
45 that is the Government rates being less than full cost of
46 service, is this, in this particular example, isn't it the
47 opposite?

48 MR. WELLS: To the extent that, yes, in that particular
49 example for those preferential rates which apply to
50 Government operations in certainly rural areas of the
51 province where these rates apply, that would be true, but
52 if you took the total dollars of the return to Government on

53 these rates and the, and then the total of Hydro's
54 operations and the ... you won't get the same result. But
55 these preferential rates are, for the classes that are
56 encompassed, are something that came out of the history.
57 I mean, I don't think ... these are something that we now
58 have to deal with that are part of passage of time and
59 circumstances of another day and the Board has clearly
60 expressed their view as to what should happen here.
61 Government has not made any, is absolutely passive on the
62 issue, they're not involved, and we have filed an approach
63 to it that, depending on your point of view, you might think
64 is appropriate or inappropriate, and the issue will be
65 corrected, but it's a very small, in the context of the total.
66 In principle what you're saying is the Government does
67 have a little benefit here, particularly the Federal
68 Government.

69 MS. BUTLER, Q.C.: So on this particular issue we accept,
70 it seems that you're agreeing with me, that the ratepayers
71 are subsidizing Government.

72 MR. WELLS: On those particular rates to the extent of
73 what is it, \$2 million or \$1.5 million a year.

74 MS. BUTLER, Q.C.: Okay. And would you agree, Mr.
75 Wells, that it is generally more common and reasonable to
76 have Government customers paying either 100 percent of
77 the cost of service or actually subsidizing ratepayers?

78 MR. WELLS: Well for the actual service supplied by the
79 Utility, yes, of course, I think that's the Board's view and
80 there is no reason why there should be a preference. It's
81 certainly not apparent and nobody is arguing that it should
82 be now, but it's not apparent to anyone in this room, I'm
83 sure, why there should be any subsidy of Government
84 rates, federal or provincial.

85 MS. BUTLER, Q.C.: Okay, thank you. Now, I guess one of
86 the other points I want to make about this is that this is
87 happening, this \$2.6 million that ratepayers are subsidizing
88 Government for in this area ...

89 MR. WELLS: No, that's the total of the preferential rate bill,
90 2.6.

91 MS. BUTLER, Q.C.: I'm sorry, you're correct. But this is
92 occurring at the same time that Government has requested
93 and, from what we can see, will likely receive a dividend
94 this year, I'm sorry, in the test year of \$70 million.

95 MR. WELLS: Yes. The Government is contemplating
96 receiving a dividend of that amount. I'm sure that in the
97 mind of Government, that's quite a phrase, that there's not
98 an overt thought that we're asking for \$70 million on one
99 side, in the meantime we're asking for a \$1.5 million subsidy
100 on rates. I mean, that hasn't occurred within, I'm sure, the
101 mind of Government.

1 MS. BUTLER, Q.C.: But that is the reality.
2 MR. WELLS: The reality, yes, but as I say, the Government
3 is quite prepared I'm sure to accept the decision of the
4 Board with respect to preferential rates.

5 MS. BUTLER, Q.C.: My, I guess, I think, my final question
6 in this area is this, there has been a recommendation
7 actually from one of Newfoundland Power's experts that
8 Hydro should propose a five-year plan at this hearing for
9 the elimination of these rates. Do you accept that as a
10 reasonable recommendation for this Board?

11 MR. WELLS: Yeah, and, well, there's no disagreement I
12 don't think on the issue. It's a question of timing. The only
13 reason we're not proposing it at the moment, whether we're
14 right or wrong, is that we looked at the issue of the impact
15 on ratepayers, including even those in the residential, or
16 preferential rates, and put in a little slower time frame. We
17 may not be right on that. We're not being argumentative
18 that the Board should not consider anything else. When
19 you look at other classes in that preferential rate thing and
20 the 2.6 million, which I'm sure that everybody would like to
21 see come out of the subsidy, we're talking the other class
22 of preferential rates, like churches, schools, fish plants, the
23 Burgeo Library, and we look at them. We said, well, for the
24 \$500,000 that's there and to hit them on top of the rate
25 increase now, that's not going to change the water on the
26 beans with respect to this total application, because you
27 know where I stand on this. Our big problem is the \$60
28 million balance in the Rate Stabilization Plan which comes
29 from No. 6 fuel. This \$500,000, every dollar counts, I
30 suppose, for the industrial customers and others, but, you
31 know, these are decisions that the Board can make. The
32 facts are clear. The Board's preference has been made
33 known to us and maybe we're just too soft on trying to hit
34 customers. Our whole thrust in this application is to try to
35 reduce the impact on customers of precipitous rate
36 increases. The Consumer Advocate has already
37 questioned that and I don't find any, I don't disagree that
38 that's not an issue that could be debated. You know, we
39 have to recognize the costs that are impacting the system
40 and to the extent that we defer those costs then we don't
41 want to get too far in the world of self-delusion.

42 MS. BUTLER, Q.C.: I'm going to turn now to another issue
43 which I think amounts to essentially \$800,000 which can
44 potentially be saved, and that is the point of recall sales.
45 As I understand this, Mr. Wells, Hydro receives income
46 from the non-regulated sale of re-call energy to Hydro
47 Quebec.

48 MR. WELLS: Yes.

49 MS. BUTLER, Q.C.: And in the test year I understand that
50 Hydro has adjusted its interest expense related to this
51 revenue.

52 MR. WELLS: Adjusted its interest expense to the effect ...
53 on this hearing or ...

54 MS. BUTLER, Q.C.: Yes. Can we have a look at PU-56, .1
55 actually. This was a question that was put to Hydro from
56 the Public Utilities Board of course, page two of four. 56.1,
57 Mr. O'Reilly. There you go. Thank you. Now, let's see.
58 On the topic of interest expense ... you have to go down to
59 line 32. Mr. O'Reilly, I wonder is it possible to get the
60 whole page on the screen there? Well let's just hold it still
61 for one moment. The column I want of course to look at is
62 the financial statement column at line 32, the revenue
63 requirement column for the same line and the decrease or
64 increase that's shown. So as we can ...

65 MR. WELLS: Yes, I understand.

66 MS. BUTLER, Q.C.: Okay. The financial statements show
67 your interest expense to be \$92.784 million?

68 MR. WELLS: In 2000 and?

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

70 MR. WELLS: 2, right.

71 MS. BUTLER, Q.C.: And the revenue requirement is
72 adjusted to 93.584 million for that year with a difference of
73 \$800,000.

74 MR. WELLS: And what are you asking, what is that
75 \$800,000 attributable to?

76 MS. BUTLER, Q.C.: Actually I think we do know that as a
77 result of some questions. If you can tell me yourself what
78 you understand the adjustment refers to or relates to, I'd
79 appreciate it.

80 MR. WELLS: Well I want to get it right ...

81 MS. BUTLER, Q.C.: Okay. My understanding is, Mr.
82 Wells, let me just put this to you, that this is an accounting
83 adjustment only ...

84 MR. WELLS: That's right.

85 MS. BUTLER, Q.C.: ... and that ...

86 MR. WELLS: And it's related to our income, you're saying,
87 from the unregulated sales.

88 MS. BUTLER, Q.C.: Right. In other words ...

89 MR. WELLS: And so all I can say right now is that, and I'm
90 sure ... is this a detriment to ratepayers? We're not ...

91 MS. BUTLER, Q.C.: As I understand it, the revenue
92 requirement in the test year is being increased by \$800,000
93 that's not actually paid.

94 MR. WELLS: And it's attributed to unregulated sales.

95 MS. BUTLER, Q.C.: Well, for the moment can you just go

1 back to the first part of the question because I think it's
2 going to get complicated?

3 MR. WELLS: There's \$800,000 there, there's no doubt
4 about it, yes.

5 MS. BUTLER, Q.C.: \$800,000 is shown and to your
6 knowledge it's \$800,000 that is not actually paid.

7 MR. WELLS: It will not be paid out.

8 MS. BUTLER, Q.C.: Right. It's simply an accounting
9 adjustment.

10 MR. WELLS: Yes. Oh, yes, okay.

11 MS. BUTLER, Q.C.: And do you know under what
12 authority or on what basis Hydro seeks to recover that
13 additional \$800,000 that's not actually paid from
14 consumers?

15 MR. WELLS: How do we propose to recover it from
16 consumers?

17 MS. BUTLER, Q.C.: Why are you proposing to recover it
18 from consumers as a revenue requirement in your test year?

19 MR. WELLS: If we are recovering it from consumers, then
20 it's attributable to our regulated activity. Otherwise we
21 would not be trying to recover it from consumers.

22 MS. BUTLER, Q.C.: And are you able to tell me how the
23 \$800,000 ...

24 MR. WELLS: I think ... just so we don't mislead the Board,
25 and I'm not trying to duck, because our financial statements
26 are ... I think our Controller, Mr. Roberts, will give you, you
27 know, in one second a quick answer and rather than me
28 trying not to make an inadvertent mistake, but I can say as
29 a principle that in our unregulated activity those costs are
30 not going to be attributed to our regulated activity, and I'm
31 sure Mr. Roberts has the explanation.

32 MS. BUTLER, Q.C.: I will follow that up then with Mr.
33 Roberts. Can you just give me a moment so I can make a
34 note? Okay, Mr. Wells, I'm going to turn now, if I might, to
35 the issue of Hydro's hydraulic forecast. Mr. Chairman,
36 what was the time that you anticipated the morning break?

37 MR. NOSEWORTHY, CHAIRMAN: 11:00.

38 MS. BUTLER, Q.C.: 11:00, that's fine. I should get through
39 this area then. Hydro's island interconnected system is a
40 mix of hydroelectric and thermal generation.

41 MR. WELLS: Yes.

42 MS. BUTLER, Q.C.: And Mr. Henderson on your
43 company's behalf has explained that Hydro dispatches the
44 entire system such that the maximum load and energy
45 possible is met by the hydroelectric generation.

46 MR. WELLS: That's the operating procedure, yes.

47 MS. BUTLER, Q.C.: Thermal from Holyrood generation
48 dispatched to supply energy that can't be met by
49 hydroelectric sources.

50 MR. WELLS: Yes.

51 MS. BUTLER, Q.C.: Okay. Now, you're aware, obviously,
52 that hydrology is a big issue in these proceedings. A
53 number of intervenors have taken issue with hydrology.

54 MR. WELLS: Yes.

55 MS. BUTLER, Q.C.: Because water is free and fuel is not,
56 using a low hydraulic forecast results in a higher thermal
57 forecast and thus a higher revenue requirement for the test
58 year.

59 MR. WELLS: This is only an aside. Sometimes water is not
60 free. We have to contain it and manage it and control it
61 and we spend a fair amount of effort on water. It's there if
62 you can get your hands on it. It's ... yes. That is ... I'm
63 sorry, I didn't mean to interrupt your line of questioning,
64 so.

65 MS. BUTLER, Q.C.: But my premise is correct.

66 MR. WELLS: What you're saying is that, well you're really
67 alluding to the fact that if we were to increase or decrease
68 our hydraulic forecasts and inflate our thermal forecasts,
69 that we would be taking advantage of the situation.

70 MS. BUTLER, Q.C.: Oh, no. Let me ...

71 MR. WELLS: Or, no, no, could be. It would make our
72 figures look like we need a bigger revenue requirement.

73 MS. BUTLER, Q.C.: No. Let me just make sure that you
74 understand the question.

75 MR. WELLS: Yeah.

76 MS. BUTLER, Q.C.: For the public's benefit ...

77 MR. WELLS: Yeah.

78 MS. BUTLER, Q.C.: ... given a fixed forecast, if hydrology
79 is lower than thermal or if thermal is lower than hydrology,
80 but the forecast remains the same, and because water is free
81 and because Hydro has to pay a fixed price for a barrel of
82 fuel, the lower the hydrology the lower, I'm sorry, the lower
83 the hydrology and the higher the thermal, the higher your
84 revenue requirement in the test year.

85 MR. WELLS: Yes. That would affect the revenue
86 requirement in the test year.

87 MS. BUTLER, Q.C.: And given past experience, approved
88 rates that flow from the test year could be in place for a
89 long time. I know it's your intention to have an application
90 in 2003 with a test year 2004, but rates could be in place for

1 a long time.

2 MR. WELLS: Not in the circumstances now, but I
3 understand the premise of what you're saying but we don't
4 anticipate any more than two years here in this instance.

5 MS. BUTLER, Q.C.: Can I just ask you before I get into
6 perhaps my plan flow (phonetic) cross-examination, do you
7 know what happened to the price of fuel yesterday in the
8 world markets?

9 MR. WELLS: If it was not yesterday, it was the day before,
10 it dropped. Fluctuates ... maybe it was yesterday. I can't ...

11 MS. BUTLER, Q.C.: I thought so.

12 MR. WELLS: It went down \$3 a barrel. Was that
13 yesterday?

14 MS. BUTLER, Q.C.: I thought it was yesterday. Can we
15 see, Mr. O'Reilly, NP-45? This is Hydro's 10-year
16 production and 50-year historic inflow (phonetic) data.
17 Page two of four first. Okay. See if we got the right ...
18 yeah. This document unfortunately, Mr. Wells, is going to
19 have to come up in three separate screens. What we have
20 in front of us is '91 to '95.

21 MR. WELLS: Are we looking at NP-45, page two of four?

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

23 MR. WELLS: Okay.

24 MS. BUTLER, Q.C.: And then when we put up the next one
25 you'll see it goes from '95 to, say, '98 or so.

26 MR. WELLS: Uh hum.

27 MS. BUTLER, Q.C.: So we'll just take it slowly, and if
28 you've got a pencil it might help you. The actual hydraulic
29 data, '91 was 4.2. I'm sorry, I'm sorry, that's '92. '92 is 4.2, '93
30 is 4.4, '93 ...

31 MR. WELLS: We're talking gigawatt hours here.

32 MS. BUTLER, Q.C.: Yeah, gigawatt hours. '94 is 5.0. In
33 terms of actual gigawatt hours we're talking about 4,211, I'm
34 sorry, 4,221 for the first figure, 4 ...

35 MR. WELLS: Yes, I see the figures and you want to go
36 from '91 through to ...

37 MS. BUTLER, Q.C.: Yes, if you don't mind, and because we
38 have to go to another ...

39 MR. WELLS: That's no problem, yeah.

40 MS. BUTLER, Q.C.: ... screen we'll have to write them
41 down. Okay. So 4,221, 4,439, 5,043, 4,392. Am I correct for
42 the actual hydraulic figures?

43 MR. WELLS: Yes. You're reading the table, yes.

44 MS. BUTLER, Q.C.: Yeah. Can we go to the next screen
45 then, page three of four? '96 is 4,573, '97 is 4,629, '98 is
46 4,262, '99 is 4,802 and 2000 is 5,016. That's the last full year
47 that we know.

48 MR. WELLS: Yes.

49 MS. BUTLER, Q.C.: Okay, thank you.

50 MR. WELLS: These are facts filed, yeah.

51 MS. BUTLER, Q.C.: Two points that I want to make from
52 this exhibit, Mr. Wells, and the first is that the eight-year
53 trend, if you plotted it, has been increasing hydraulic and
54 not decreasing hydraulic. Do you agree with that as the
55 general trend?

56 MR. WELLS: That's what these figures show, yes.

57 MS. BUTLER, Q.C.: The second is that Hydro has,
58 according to the Grant Thornton report, always under-
59 forecast hydraulic and over-forecast thermal. Can we look
60 at the Grant Thornton report 2001, page 23? Is that page
61 23? Yeah, okay. Thank you. Third paragraph on that
62 page. Okay.

63 MR. WELLS: The one that says, "Based on"?

64 MS. BUTLER, Q.C.: I believe so. I'll find the actual quote
65 here for you. "Based on our analysis of the cost of No. 6
66 fuel from '97 to 2000, Hydro's actual costs have always been
67 less than budget."

68 MR. WELLS: From 1997 to 2000, yes.

69 MS. BUTLER, Q.C.: In doing the forecast for the hydraulic
70 projection for the test year, Hydro has used 4,271. We can
71 go back to that exhibit if you'd like. It's ...

72 MR. WELLS: No, that's fine.

73 MS. BUTLER, Q.C.: Okay. Whereas as we saw the 2000
74 figure was 5,016. Now I appreciate the forecast figure of
75 4,271 was selected on the basis, I believe, of the 50-year
76 average.

77 MR. WELLS: 50-year average, yes.

78 MS. BUTLER, Q.C.: Now Newfoundland Power of course
79 is proposing a different method, but what I want to turn to,
80 I think, is how it was that Hydro came to select 4,271
81 gigawatt hours for the hydraulic production in the test
82 year. Given Mr. Brushett's comment in the Grant Thornton
83 report, we're suggesting that it is subject to doubt.

84 MR. WELLS: The first answer, the first comment I must
85 make is that the explanation for this is, for the benefit of
86 everyone, will be Mr. Henderson who manages our energy
87 system, is responsible for that, who will describe the
88 variations in hydraulic and actual and why we chose a
89 particular figure for the year, and, you know, it'll be, that's
90 the definitive spokesperson for Hydro on this issue and he

1 has the better understanding of it, because the only
2 comment, and again I don't want to avoid your question
3 but the actual hydrology will change in every year, but we
4 have had some good fortune. From my perspective, in my
5 job since '96, I've been very thankful that we've had these
6 wetter than average years and it's certainly helped us to
7 manage the effect of the Rate Stabilization Plan and keep
8 the balances, because oil prices have gone higher up in the
9 mid-20 range and we've still been able to manage the
10 system through without letting the balances get totally out
11 of sight because of the benefits of hydrology. The other
12 thing is the, we have to base things on an average water
13 year.

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

15 MR. WELLS: And our forecast requirements are based on,
16 in large measure, what our customer requirements are and
17 so therefore the industrial customers will state in terms of
18 their forecast what they expect in the run of a year. So
19 when you look at the line of questioning you're pursuing,
20 we better sit with the experts like Mr. Henderson who can
21 give you the hydrology of our main system, like the Bay
22 D'Espoir system and the other systems why we forecast the
23 way we do, and it's true in the period 1997 to now we've
24 had wet years, and I think 2000 was the wettest year in
25 forecast in our experience, but we can't predict what the
26 rainfall will be in Newfoundland, you know, in advance, and
27 we also can't predict with 100 percent accuracy what the
28 load forecast will be, but we have to ensure that we always
29 have the capability for a firm supply of power, and this is
30 going to be very much part of Mr. Henderson's evidence in
31 terms of hydrology and Mr. Budgell's evidence in terms of
32 the requirements of the system. That's where you have the
33 best opportunity for all the intervenors to question them on
34 that issue. Grant Thornton is recording the appropriate
35 facts but there are very good reasons, that's all I can say, as
36 to why these technical experts operate the system in
37 accordance with sound utility practice.

38 MS. BUTLER, Q.C.: I have no difficulty whatsoever
39 deferring most of these questions to Mr. Henderson based
40 on what you've told me, however, there was a statement
41 made by you directly on this point.

42 MR. WELLS: Yes, in confirmation of ... yes.

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

44 MR. WELLS: Do you want to go back to my evidence?

45 MS. BUTLER, Q.C.: Well, actually I want to refer you to a
46 document that may or may not be in the system actually.
47 My point of course is that we're looking at a forecast of
48 4,271 which is 800 gigawatt hours less than the 2000 actual
49 figure, which was 5,016. Sorry, yes?

50 MR. WELLS: Yes.

51 MS. BUTLER, Q.C.: Yes. And in your annual report for
52 2000, which is dated February 2001, at page four, you as
53 President of Hydro made a comment on the reservoir levels.
54 My colleague, Mr. Alteen, is going to actually pass out the
55 portion of the annual report because I doubt that it's in the
56 system, Mr. Wells. Okay, great. Thank you.

57 MR. WELLS: What page?

58 MS. BUTLER, Q.C.: Four. The page should start with,
59 "Commitment to competence." Is that a statement which
60 was written either for you or by you, Mr. Wells?

61 MR. WELLS: I stand by it.

62 MS. BUTLER, Q.C.: Okay, thank you. Under the heading
63 of "Energy Production" ...

64 MR. WELLS: Yes.

65 MS. BUTLER, Q.C.: ... maybe you can just read that
66 paragraph, please, the first paragraph.

67 MR. WELLS: "Hydraulic production for 2000 was the
68 second highest on record. Large inflows into the Bay
69 D'Espoir reservoir system, coupled with mild winter
70 temperatures, enabled us to limit production from the
71 Holyrood thermal generating plant." Go on?

72 MS. BUTLER, Q.C.: Oh, keep going, yes.

73 MR. WELLS: "Reservoir levels remained high at the end of
74 the year. As a result, production from hydro generation is
75 expected to continue at high levels, therefore, production
76 from Holyrood during the 2000-2001 winter is expected to
77 remain lower than normal, reducing consumption of No. 6
78 fuel at a time when prices are extremely high." Certainly
79 would be consistent with our objectives.

80 MS. BUTLER, Q.C.: Consistent with your objective but I'm
81 not certain that they're consistent with your forecast.

82 MR. WELLS: Oh, because this said the second highest
83 instead of the best?

84 MS. BUTLER, Q.C.: No, because it's talking about what
85 you predict. Production from Holyrood during 2000-2001
86 winter, which would take you into the 2001.

87 MR. WELLS: Yes.

88 MS. BUTLER, Q.C.: Expected to remain lower than normal,
89 reducing consumption of No. 6 fuel.

90 MR. WELLS: That didn't turn out is (inaudible).

91 MS. BUTLER, Q.C.: I guess what my point is, that for the
92 year 2001, the forecast, for the year 2002 forecast, you're
93 using lower figures.

94 MR. WELLS: Well, you know, timing is everything. I
95 mentioned that yesterday. At the time now when fuel

1 prices are spiking and staying up there, and I shouldn't use
2 the term "spiking," what's different, we've had spikes in the
3 past but they've gone back down. This time it looks like
4 they're staying up and it comes at a very inopportune time
5 for us that we're going, it looks as though we're having
6 lower water than higher water, and Mr. Henderson will
7 explain how the guide curve ... one thing we do, I must say
8 very well, our people, is manage that water system and with
9 the cooperation of our industrial customers who have
10 hydraulic production as well, the whole system, including
11 Newfoundland ... the whole system is very well managed
12 within the province, and this is the wrong time for us to
13 have lower water levels in Newfoundland when we have
14 higher oil prices, but our experience so far this year and the
15 results of the guide curve to date are that we are running
16 under the guide curve and it all changed suddenly. For
17 instance, it would have helped, this recent big rainfall in St.
18 John's, was a very ... it didn't happen in Bay D'Espoir. If it
19 had happened in Bay D'Espoir, something like that, could
20 result in savings of millions of dollars, you know, in terms
21 of oil, but it didn't happen there, so Mr. Henderson will be
22 able to take you through the variations in how this whole
23 system is managed and how we keep track of the water, but
24 I can't ... I think I can confirm safely that the good
25 experience of '97 on, which has been reflected in the Grant
26 Thornton report, is now, the pendulum is swinging the
27 other way against us on water. That may change but we
28 did not get the results that we had hoped for this year in
29 terms of water and it's a fairly distinct change from what
30 happened in the previous, you know, five or six years.

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

32 MS. GREENE, Q.C.: Excuse me, Mr. Chairman, I think it may
33 be helpful if I said at this time that Hydro does plan to file
34 supplementary evidence from Mr. Henderson with respect
35 to the appropriate hydrological record to be used for this,
36 for our purposes. I had not anticipated that Newfoundland
37 Power would be asking the President and CEO detailed
38 questions on what we believe are within areas of an expert,
39 so I had hoped to have it available by this afternoon, and
40 that might be helpful. I thought it might be helpful if I
41 indicated now to Newfoundland Power, but we do plan to
42 file supplementary evidence with respect to the appropriate
43 hydrological records. It became clear to us from reading
44 Mr. Brockman's pre-filed, supplementary evidence of
45 September 12th and as well as yesterday that this would be
46 an issue, so we will be filing that from Mr. Henderson and
47 hopefully will be available to circulate if not late this
48 afternoon, first thing in the morning, and it would be
49 (inaudible) time before he becomes a witness for the
50 hearing. The other thing I should indicate is we also plan
51 to file supplementary evidence with respect to the
52 prudence of the Great Northern Peninsula interconnection,
53 because again based on the supplementary evidence that

54 was filed by industrial customers by Mr. Osler (phonetic)
55 as well as the comments by Mr. Hutchings yesterday, it has
56 become clear that that also is an issue that we would like to
57 file supplementary evidence on, so that will be filed again
58 hopefully late this afternoon or early tomorrow morning,
59 again in sufficient time before Mr. Budgell, who is the
60 witness who will speak to that issue, will be appearing, and
61 I guess the date of Mr. Henderson and Mr. Budgell's
62 appearance depends really on the other parties to the
63 hearing. And the third thing that at this point in time we
64 know that we will be filing supplementary evidence on is
65 with respect to an allocation of cost issue that came to our
66 attention late last week, and we worked on it over the
67 weekend. That will be filed by Mr. Reeves and spoken to
68 by Mr. Reeves. I had planned to indicate to the Board
69 when I had the evidence available, which I had hoped it
70 may be as early as this afternoon with respect to the first
71 two, but certainly hopefully by tomorrow.

72 MR. NOSEWORTHY, CHAIRMAN: Thank you very much
73 for that information.

74 MR. KENNEDY: Mr. Chair, I'm wondering whether we need
75 to label these as an exhibit in light of the fact that they were
76 drawn to the attention of the witness. I'm not sure if the
77 financial is part of a reply to an RFI.

78 MR. ALTEEN: CA-101.

79 MR. KENNEDY: Okay. So in that case we'll just refer to an
80 excerpt from CA-101.

81 MR. NOSEWORTHY, CHAIRMAN: I'll ask Board counsel
82 if there are any references that aren't contained in the
83 evidence in terms of exhibits, I know there were one, if not
84 two, circulated yesterday, would they be classified as
85 exhibits and recorded as ...

86 MS. BUTLER, Q.C.: The only one yesterday actually was
87 reference to the legislation which I don't think needs to be
88 marked as an exhibit.

89 MR. NOSEWORTHY, CHAIRMAN: Okay. By the normal
90 matter of course that will be done though?

91 MR. KENNEDY:

92 That's correct.

93 MR. NOSEWORTHY, CHAIRMAN:

94 Okay, thank you.

95 MS. BUTLER, Q.C.:

96 Mr. Chairman, that would be a good place to break, if you
97 don't mind.

98 MR. NOSEWORTHY, CHAIRMAN:

99 Okay, thank you very much. We'll reconvene in 15

1 minutes at 10 after. Thank you.

2 (break)

3 MR. NOSEWORTHY, CHAIRPERSON: Are you ready to
4 proceed, Ms. Butler?

5 MS. BUTLER, Q.C.: I am, Mr. Chairman. Mr. Wells, I
6 should have concluded the issue of hydrology perhaps
7 before the break. I appreciate that there's new figures
8 coming and that this is the technical area of Mr.
9 Henderson, so believe me when I tell you I will pursue it
10 with him. However, I think I should make the point that
11 Newfoundland Power is recommending the use of a 30 year
12 moving average in the calculation of the forecast number
13 for the gigawatt hours on hydraulic production. Are you
14 aware of that?

15 MR. WELLS: I'm aware of that.

16 MS. BUTLER, Q.C.: Okay, and currently the figure being
17 proposed by Hydro is a 50 year average, or close to a 50
18 year average?

19 MR. WELLS: Yes.

20 MS. BUTLER, Q.C.: Are you aware from the expert's report
21 Newfoundland Power filed, that by our calculation, using
22 the current hydrology, the difference would mean a
23 reduction in revenue requirement of \$6.6 million in the test
24 year?

25 MR. WELLS: I'm aware of the fact that if you accepted
26 Newfoundland Power's approach, it would be a reduction
27 in the revenue requirement. The exact amount I'll take your
28 ...

29 MS. BUTLER, Q.C.: Okay, thank you.

30 MR. WELLS: And my only comment on that, and again, I'm
31 not an expert, but I had been under the impression since
32 being with Hydro, that the longer the term that you could
33 assess the better. You know, the longer the hydraulic
34 period that I ... I just assumed that everybody would want
35 the longest set of numbers on which to base your forecast
36 and I know ...

37 MS. BUTLER, Q.C.: I'll just follow up on that because
38 you've offered it, but when was Bay d'Espoir put on
39 stream?

40 MR. WELLS: 19 ...

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

42 MR. WELLS: 1975?

43 MS. BUTLER, Q.C.: Would it be fair to say a 50 year ...

44 MR. WELLS: '65, no Bay d'Espoir is, Bay d'Espoir is ... I'm
45 sorry, I was out of the province when they were building
46 Bay d'Espoir.

47 MS. BUTLER, Q.C.: That's okay, I don't know the year
48 either.

49 MR. WELLS: Somebody can say that in the room.

50 MR. BROWNE, Q.C.: I fished off that dam with my father
51 in 1965.

52 MR. WELLS: Yeah, '65. Yeah, no, I'm sorry, a lot of people
53 that I work with went to Bay d'Espoir in '65, and that's the
54 period, yeah.

55 MS. BUTLER, Q.C.: Okay, so if we go back 50 years we're
56 going to be catching a good many years that pre-date the
57 Bay d'Espoir project.

58 MR. WELLS: But as I, again, understand it, as a layman,
59 that it doesn't matter, because a manmade object there or
60 not, you're looking for precipitation and inflows would be
61 affected. How you contain it ...

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

63 MR. WELLS: And really I shouldn't comment, but I mean
64 I understand, like in what I hear and the developments of
65 Gull Island and that ... everybody is looking for the longest
66 hydrology and flows that you can get your hands on to be
67 sure as best you can. But that's ...

68 MS. BUTLER, Q.C.: We'll leave the point on this note. You
69 know that Newfoundland Power's suggestion flows from
70 Mr. Brockman's report.

71 MR. WELLS: As I understand it, yes.

72 MS. BUTLER, Q.C.: Okay, and that will become a battle for
73 those experts, I presume, at that level. I'll turn now if I can,
74 Mr. Wells, very briefly to the Rate Stabilization Plan. Is it
75 correct to say that there's been no review of the Rate
76 Stabilization Plan fuel price assumptions by this Board
77 since 1992?

78 MR. WELLS: Yes.

79 MS. BUTLER, Q.C.: And I gather from your public
80 statement and your pre-filed evidence, you are satisfied
81 that the Rate Stabilization Plan has served its purpose well?

82 MR. WELLS: Yes, I have stated that and my
83 understanding of its purpose and the benefit of the Rate
84 Stabilization Plan with respect to variations in customers'
85 bills, it does smooth it out. It's a natural, it's almost like a
86 hedge with respect to oil prices, and my understanding also
87 of the Rate Stabilization Plan, which I'm certainly not a
88 hundred percent ... there's only about a few people that
89 understand the thing completely, and they will testify, but
90 the ... it works best if it could work around a mean, so if the
91 price of oil in, say, Hydro's rates were X, and at various
92 times you would be X plus in actual prices, and X minus, so
93 the balances in the plan would come near even, that we'd

1 owe the customers, or the customers would owe us, and it
2 never gets too far away from the median, the problem we've
3 most recently experienced at \$12.50 against \$30.00, that's
4 where the balances are going, all in one direction, but
5 because of hydrology, because of demand, and because of
6 the prices going up and down, since 1992 the plan has
7 worked, I think, very very well. Up till now the balances are
8 ... well it's beyond the cap set by the Board.

9 MS. BUTLER, Q.C.: Now within the Rate Stabilization Plan
10 there's actually two sections, there's the retail and there's
11 the industrial customers, correct?

12 MR. WELLS: Yes.

13 MS. BUTLER, Q.C.: Sorry, when I ask you a question,
14 unfortunately for the purposes of the transcript I've got to
15 get an answer rather than a nod.

16 MR. WELLS: I'm sorry, I have a tendency just to nod my
17 head.

18 MS. BUTLER, Q.C.: I know. Hydro is seeking to double
19 the retail Rate Stabilization Plan cap which is used to trigger
20 review by the PUB from \$50 million to \$100 million.

21 MR. WELLS: Yes.

22 MS. BUTLER, Q.C.: Okay, thank you. And Hydro is
23 otherwise seeking to operate the Rate Stabilization Plan as
24 it has with automatic rate adjustment each year to collect
25 one third of the balance in the Rate Stabilization Plan?

26 MR. WELLS: Yes.

27 MS. BUTLER, Q.C.: Okay, now on behalf of Newfoundland
28 Power, Mr. Brockman's recommendation on the RSP is to
29 leave the cap at \$50 million and allow Hydro to bank the
30 additional deficit but if it wishes to apply balances greater
31 than \$50 million to Newfoundland Power's customers, it
32 should seek approval in a separate application. I wonder,
33 as President, if you could comment on that principle or
34 recommendation?

35 MR. WELLS: I don't like it.

36 MS. BUTLER, Q.C.: Can I have the long answer?
37 *(laughter)*

38 MR. WELLS: The issue of the Rate Stabilization Plan is to,
39 again, to allow for some averaging over time, about ebbs
40 and flows in oil prices, and this is not to the benefit of
41 Hydro, or to the detriment of its customers. We are
42 deferring costs and in principle, the Rate Stabilization Plan
43 as we know it today, if you want that to be applied and we
44 have not sought to change it, we have suggested to
45 everyone at this application that we take two approaches
46 with respect to fuel ... increase the price in Hydro's rates
47 from \$12.50 to \$20.00, and then increase the cap in the Rate
48 Stabilization Plan to accommodate the differences that we

49 know are forecast to exist. The beauty of the plan is if we're
50 wrong on oil prices or hydrology, the benefits flow to the
51 customers anyway. Any money we make in excess will pay
52 down the balance, so to that extent, putting a further
53 contrivance on the plan as suggested by your expert, and
54 leaving it open to Hydro as to whether, you know, we'd
55 have to come back to the Board to say we want to apply
56 this amount to the balance and it will result in something in
57 excess of \$50 million is absolutely unnecessary and time
58 consuming when X number of barrels of oil, times X dollars
59 in price, will give you the figure, and we can tell you today
60 that unless the price of oil goes down substantially we're
61 going over the \$50 million even probably before the Board
62 has an opportunity to issue an order from this hearing. It
63 would take really a fortuitous turn of events in terms of
64 hydrology and price to reverse the trend before the end of
65 the year.

66 MS. BUTLER, Q.C.: Now the effect of what we're speaking
67 of here is the 3.4 percent increase to consumers directly
68 later in 2002?

69 MR. WELLS: Yes.

70 MS. BUTLER, Q.C.: Thank you. The effect of Mr.
71 Brockman's recommendation is simply that Hydro has
72 increased regulatory scrutiny.

73 MR. WELLS: With respect to the ... as I understand it, he
74 is ... extra regulatory scrutiny with respect to the operation
75 of the plan, that's all, but if the plan has been in operation
76 since 1992, and basically I'm sure the Board and everybody
77 involved understand the rudiments of the plan to the extent
78 that you would need to, and to me it's an unnecessary
79 administrative expense and burden to deal with the
80 obvious. Let the Board make the decision now. We're not
81 going to increase the cap, in which case prices in our rates
82 would have to go higher, or we are going to increase the
83 cap, in which case you don't need this extra step that you
84 suggest. I don't see the benefit, and this is my view of it, I
85 don't see that poking around in the Rate Stabilization plan
86 ... now the industrial customers have certainly questioned
87 how this whole ... it's difficult to understand how it
88 operates fully in its detail, and I think there's about four
89 binders that we responded to industrial customers' requests
90 trying to explain to them the Rate Stabilization Plan, but if
91 you're going to adjust the plan then let's do it now as a
92 result of this hearing and not say that if something goes
93 over the plan, well let's have another hearing to see if we
94 should put the balance back in. Honestly, I just don't see
95 the efficacy of that, and that's not to say ... there are people
96 in Hydro that fully understand the Rate Stabilization Plan.
97 The issue would be can we get it explained to everybody's
98 satisfaction. There's a good logic to it. It works in a certain
99 way, and the broad principles, which I never go below that,
100 as I know that it's all based on demand, hydrology, and the

1 price of fuel, and I don't have to know anything more than
2 that, and the balances that are owing to each ... you know,
3 one way or the other. The principle is very good and that's
4 why I said in my opening statement, I caution anybody.
5 Before you start to throw out the Rate Stabilization Plan, it
6 has been of good benefit to everyone, it really has,
7 including Newfoundland Power.

8 MS. BUTLER, Q.C.: Well, don't get me wrong, of course
9 Newfoundland Power, I thought we made it clear in the
10 opening statement, supports the Rate Stabilization Plan
11 itself and maintains that it has served its customers well.
12 However, this particular recommendation for the working or
13 the mechanics of the plan was something that I wanted to
14 put to you and I've recorded your answer.

15 MR. WELLS: My real response to you then, without being
16 flippant, is that we should work out the details of the plan
17 and the mechanics and let it apply, not keep the plan as is
18 and then say we'll go through another step that if you go
19 over the balance in the plan, let's have another review
20 related to the workings of the plan. Let's agree on the plan
21 and how it works, and then let the consequences fall where
22 they may. That would be my position.

23 MS. BUTLER, Q.C.: Can I just have you look at NP-50,
24 which is the retail RSP balances reflected for a number of
25 years. We heard in other evidence, Mr. Wells, perhaps
26 even yours yesterday, certainly in the pre-filed, that the
27 RSP balance was forecast to exceed \$50 million in 2001, but
28 it was my understanding that it was forecast to be below
29 \$50 million by 2004.

30 MR. WELLS: Yes, that's for Newfoundland Power's
31 customers.

32 MS. BUTLER, Q.C.: The retail RSP cap, we have here for
33 2003 a forecast of \$62 million.

34 MR. WELLS: Yes.

35 MS. BUTLER, Q.C.: But for 2004 a retail balance of \$37
36 million.

37 MR. WELLS: Yes.

38 MS. BUTLER, Q.C.: Okay. Looking at that screen then, my
39 question is will the concern over the RSP balance and
40 therefore the suggestion for an increased cap not be
41 eliminated by your forecast by the year 2004.

42 MR. WELLS: The need to have such a high cap hopefully
43 will be eliminated but we have to deal with the fact that the
44 Board has stated what the cap is now and we think we're
45 going to exceed it. We pretty well know we are and that's
46 why I say our whole, if we're ... our whole approach to this
47 has been, again, two-pronged, and we can ... if this is, if this
48 materializes, and the Board increases the cap, we ride up
49 the excess over the \$50 million, and then we say over time

50 we'll bring it down again and get us back into more or less
51 equilibrium. That would all depend, in a great measure, on
52 where the price of Number 6 fuel is going and the exchange
53 rate, but I mean there was a method to our approach.

54 MS. BUTLER, Q.C.: Which of your witnesses, Mr. Wells,
55 do you defer to the details of the RSP?

56 MR. WELLS: Mr. Osmond, I guess, the Vice-President of
57 Finance. He's the one that we all will stick with that
58 responsibility when we come before the Board here in our
59 quarterly reports. He's somewhat reluctant but he'll do it.
60 *(laughter)*

61 MS. BUTLER, Q.C.: I'm going to turn now, Mr. Wells, if I
62 might, to your capital budget, 2002, approval for which is
63 also sought in this application, and if possible, Mr. O'Reilly,
64 can you get up Schedule E to the application itself?

65 MR. O'REILLY: Would you like the revision to ...

66 MS. BUTLER, Q.C.: Yes, please, if Schedule E was revised.
67 You're going to have to enlarge that. Okay, looking at the
68 bottom line of the spreadsheet, total capital expenditures
69 for Hydro between 1996 and 2001.

70 MR. WELLS: Yes.

71 MS. BUTLER, Q.C.: Okay, these range, of course, from \$28
72 million to \$55.9 million actually in 2001. We calculated the
73 average there of the total capital expenditures to be \$42
74 million, and your budget for 2002 is coming in at \$48 million.
75 You might just, if you could, Mr. Wells, explain for the
76 benefit of those of us who weren't here why \$55.9 million
77 was your budget for 2001 which is sort of considerably
78 higher than the previous five years.

79 MR. WELLS: Again, we're dealing with averages and the
80 ... I shouldn't speak to the detail of the capital budget but
81 we do have specified in our capital budget submission the
82 major areas of expenditure, and if you're looking at the year
83 2001, you will see the expenditures with respect to our
84 construction projects, and our general properties budget,
85 and the detail of all that has been set out in the capital
86 budget itself, and I would prefer, if you don't mind, on the
87 details of what's in that 16,228 in general properties, that
88 somebody else will deal with that?

89 MS. BUTLER, Q.C.: No problem.

90 MR. WELLS: Yes.

91 MS. BUTLER, Q.C.: I just wondered whether the year 2001
92 was unusual in some sense.

93 MR. WELLS: No, it's just we have certain ... because of ...
94 this is detailed and I don't have this in front of me, but there
95 are expenditures there that are falling in a sequence, and
96 they just happen to fall into the 2001 period. In our
97 unregulated activity, of course, there's a whole other bunch

1 of capital expenditures and one of the things that is ...
2 because the requirements will change, one of the things
3 that you would note if you examined our capital budget in
4 the last year or two or three, is the major effort we're making
5 in TRO in the upgrade of the transmission lines and that
6 produced a bubble in our capital expenditures that flows
7 through, and I'm not sure, some of that I still think is ... we
8 have major upgradings to do in 2002. That's in part and we
9 also have in our telecontrol IT expenses, there's a bubble
10 flowing through of expenses, and others can talk about
11 that. That's ... these are the two major items other than
12 what you'd see in general.

13 MS. BUTLER, Q.C.: I wonder, you might just make a note,
14 because I'm going to take that screen down now in a
15 moment. The total capital expenditures were 28, 30, 32, 36,
16 38, 56, and are now projected to be 48 in this capital budget
17 approval application. Mr. Brushett on behalf of the Public
18 Utilities Board has spoken about Hydro's capital budget,
19 and I wonder if we can have a look at his report at page 14.
20 Mr. O'Reilly, it was under Grant Thornton, GT.

21 MR. O'REILLY: (inaudible).

22 MS. BUTLER, Q.C.: 2001, the body of the report, right
23 down at the bottom, yeah. Thank you. Now your page
24 numbers may be different. I'm looking at page 14. Can you
25 try 15 for me? Okay, that's the table I'm looking for, thank
26 you. Thank you very much. Mr. Wells, I wonder if you'd
27 be kind enough to read for the benefit of those of us in the
28 room what Grant Thornton indicates in the opening
29 sentence or sentences before the table under capital
30 expenditures.

31 MR. WELLS: Yes, I'm reading from the report, from 1996 to
32 2000, total capital expenditures have been lower than
33 budget by an average of 15 percent (high in 1996 of 23.10
34 percent; low in 1997 of 4.82 percent). The following table
35 details the variance percentage of actual capital
36 expenditures to budget for each category of the capital
37 budget.

38 MS. BUTLER, Q.C.: Alright, looking at the capital budget
39 that Hydro had proposed for 2002, which is \$48 million,
40 assuming the history of the overbudgeting by 15 percent
41 applies, do you accept that this would result in a reduced
42 revenue requirement for 2002?

43 MR. WELLS: No, and I should explain why. I think a
44 further analysis of our capital budget expenditures, or
45 capital expenditures against budget, if you took out
46 projects that were cancelled or projects that were carried
47 over, the range would be more the 1.8 to 7.1 percent ...
48 actually on average ... and this is taking out carry overs and
49 cancellations, the actual average would be 4.4 percent.
50 Now that's just a mathematical calculation. The difficulty
51 here, and I think Newfoundland Power, the other regulated

52 utility has gone through the same experience with the
53 Board, that we've had issues of our capital budget not
54 being expended in the timeframe. Just looking at it as a
55 treatment of dollars that are attributed at the end of the day
56 to the expenditures may be doing a disservice to the
57 utilities in that regard because you have to look at what are
58 the reasons in any particular year why the capital budget
59 number was not achieved, and they can be affected as such
60 things as you don't get the right bids back to where you
61 estimated the cost of the project is so you cancel. You may
62 be affected by circumstances that you had no, you know,
63 some greater need arose and you diverted not only just the
64 dollars but the people, the time and the attention necessary
65 to get a job done. I can recall if it wasn't this year, the year
66 before, that in the middle of the year we had to make major
67 expenditures to improve the capability of our system in the
68 isolated community of Charlottetown to service a new fish
69 plant, and therefore the effort went this way instead of that
70 way, so you have to look at all the examples of what
71 affected your capital budget that you under spent, or over
72 spent, to get an idea of what's going on. Now from the
73 Board's perspective they look at ... you ask for \$100,000,
74 you only spent \$96,000 and you've done that consistently
75 for years so maybe we should deduct \$4,000 of anything
76 that you do, and I can ... because they're not looking at the
77 subsets of the expenditures and that may be a way to try to
78 get both utilities to ... but it is not a very precise thing in
79 the nature of our business to be absolutely on track with
80 the capital budget. Now it is a fact that both of us, and the
81 experience of the Board has been that we underspend, no
82 overspend. But you know, human nature being as it is. If
83 we all know the Board was going to take four percent off
84 our capital expenditures budget every year, you've got to
85 watch that you don't pad it by four percent, so we're trying
86 to get a balance. The important thing is that these projects
87 are essential to maintain the service and the reliability of
88 the service, and the Board would not inadvertently want to
89 provide an automatic percentage production that didn't
90 allow you to do that, or there'd be a mechanism, you'd come
91 back and say look, in reason we have a project here that's
92 in excess of what you've deducted and we've got to get on
93 with it. It's how to fine tune it and I take the point and the
94 figures will show that our track record is much like the track
95 record of Newfoundland Power. Now that the Board is
96 reviewing our capital expenditures what Grant Thornton is
97 reporting what is the fact, the only thing we've done is look
98 at it a littler closer and look at the projects that we know
99 were carried over and for good reason, because we couldn't
100 complete them in the year. For instance, we planned
101 something and because of the ice storm in Quebec, is one
102 example, we just couldn't get steel, and other things that we
103 had to, you know, cancel a bid, or say the job is going over.
104 I was personally involved in the power house in Nain
105 which we are currently building. We had planned to build

1 it in a certain year. We had difficulties with the Town and
2 where we're going to locate the thing and that got delayed,
3 you know, so it pushed into another year. And there are a
4 variety of circumstances. I'm not sure, I'm not faulting the
5 Board because the end result here is you're probably going
6 to ask well, at least take a percentage off of whatever
7 they're saying, and what we ... more positively, let me put
8 it this way that we have new software tools that we're using
9 to track ... because the Board has brought this to our
10 attention on a number of occasions, so how to try to cope,
11 we have ... with software and project schedules, we have a
12 lot more emphasis within, now, in our TRO engineering and
13 production engineering on the planning of projects and
14 scheduling, and periodically throughout the year now we
15 have a complete review of the critical factors affecting a
16 project, especially the more significant ones, to ensure that
17 we have the current schedule maintained and the resources
18 to complete, and that's the best I can say. The Board,
19 before this matter was brought to the Board for approval,
20 our capital budget, that type of attention wasn't paid. Now
21 the Board has made certain, and through Grant Thornton
22 which reports to the Board, that this is an issue for the
23 Board and I know the Board has dealt with this with respect
24 to Newfoundland Power, and maybe we can't expect any
25 sort of dissimilar treatment unless we could figure out a
26 way, another way to handle this difference.

27 MS. BUTLER, Q.C.: I don't think I would be disagreeing
28 with you if what we had on the screen showed that even in
29 one or two years of the period, Hydro had overestimated,
30 but in every single year Hydro's capital budget has been
31 underestimated. If you can bear with me for a moment,
32 what I'm suggesting to you is that if the historical average
33 of 15 percent overbudgeting applies to your 2002 capital
34 budget, which happens to be a test year, there will be a
35 reduction in the revenue requirement for the test year, and
36 perhaps to show you that calculation, I'll just show you
37 NP-258.

38 MR. WELLS: Look, I accept if you take that figure of 15
39 percent, if you applied that to our 2002 capital budget you
40 may inadvertently be doing a great deal of damage. We
41 take the point in issue, and we take the fact that this does
42 affect revenue requirement. What you can do, and
43 certainly you will do, is that in terms of where in which
44 divisions you see some of these variations, I think that we
45 can explain in our evidence through the right people who
46 will be on the stand. The more significant figures that
47 affected these variations and the explanation of why these
48 things occurred and then that would give the Board at least
49 a better appreciation of what is happening here because 15
50 percent which is not our average. It's more in the four to
51 five percent range ... 15 percent reduction in our capital
52 budget will only mean, I think, that we would go back to the
53 Board seeking an increase in our capital budget during the

54 course of the year, and we haven't really gained anything
55 and we haven't dealt with reality, you know.

56 MS. BUTLER, Q.C.: The reality according to this question
57 and answer, NP-258, which is taken in direct reference to
58 page 15 of the Grant Thornton report, is that there would be
59 a reduction in revenue requirements for the test year of
60 \$328,000, which is \$328,000 less in rates to consumers.

61 MR. WELLS: Yes, but what about we actually spent the
62 \$48 million as we intend to do, or even came within four
63 percent of it.

64 MS. BUTLER, Q.C.: I accept the question, the rhetorical
65 question, but all I'm saying is that if Mr. Brushett on behalf
66 of Grant Thornton's estimate of the over budget applies to
67 the 2002 test year, this is mathematically the result.

68 MR. WELLS: That would be the result, yes.

69 MS. BUTLER, Q.C.: Mr. Wells, also on the issue of budget,
70 capital budget expenses, yesterday in answer to a different
71 question, you mentioned to me the benefits from expenses
72 associated with technology, do you recall that? The P-2000
73 project, JD Edwards software?

74 MR. WELLS: Yes.

75 MS. BUTLER, Q.C.: Okay, in your 1998 report which is
76 attached to Consumer Advocate's question 101, you
77 referred to this project and because I'm not certain we can
78 get that up electronically, my colleague is going to pass
79 that out for you. Do you recognize the cover sheet, Mr.
80 Wells?

81 MR. WELLS: Yes.

82 MS. BUTLER, Q.C.: Okay, and looking at the next page
83 where you refer, or where Hydro refers to the Project 2000
84 systems implementation, it indicates here that it proceeded
85 on schedule throughout the year with the installation of
86 new hardware and implementation of new integrated
87 software modules, and then just reading down for me, can
88 you just read into the record what you say about, or what
89 Hydro says about P-2000 being one of the most
90 comprehensive projects?

91 MR. WELLS: Yes, on the second page, it doesn't have a
92 number or a date. I'm looking at the cover page of the 1998
93 annual report, and a second page which looks like it could
94 come from an annual report. I'll have to take your word that
95 it's 1998.

96 MS. BUTLER, Q.C.: What we'll do is while ...

97 MR. WELLS: It looks reasonably familiar so let me read it.

98 MS. BUTLER, Q.C.: While you're reading it, my colleague
99 will just pull out the original so you can be satisfied that it's
100 page four.

1 MR. WELLS: No, I'm sure you wouldn't do that to me, not
2 knowingly. Project 2000 (P-2000) systems implementation
3 proceeded on schedule throughout the year with the
4 installation of new hardware and the implementation of new
5 integrated software modules. The installation of human
6 resources, payroll, finance, purchasing and inventory
7 modules have been completed. Plant maintenance and
8 utility customer information systems will be implemented
9 during the first half of 1999. P-2000 is one of the more
10 comprehensive projects undertaken at Hydro and it will
11 significantly alter the way in which employees approach
12 and perform their work in future. We will also begin to see
13 the significant impact that enabling technology will have
14 on our organizational structures and change in business
15 process over the next two years. Keep going or ...

16 MS. BUTLER, Q.C.: No, that's fine. The date of the 1998
17 annual report would be what, approximately February of the
18 year after?

19 MR. WELLS: It actually has to be delivered to the Minister
20 in the month of April.

21 MS. BUTLER, Q.C.: My colleague is just going to show
22 you the actual original so you can satisfy yourself that this
23 is actually page four of the 1998 report.

24 MR. WELLS: I'm sorry about that. I'm sure it is.

25 MS. BUTLER, Q.C.: That's okay. The question I have for
26 you, Mr. Wells, flowing from that is given that this is now
27 two or three years later.

28 MR. WELLS: Uh hum.

29 MS. BUTLER, Q.C.: Can you refer me to the significant
30 impacts that the program has that you were speaking about
31 here in the 1998 ... the significant impact that enabling
32 technology would have on the structures and business
33 processes over that two year period?

34 MR. WELLS: Well, the, when we changed out and got into
35 the AS-400 and the basic hardware that's required, and to
36 get an integrated suite of applications, now that's the
37 jargon of the trade and not my kind of language, but we
38 chose the JD Edwards system and went into those areas to
39 which are referred here, and this was ... at that stage we, the
40 intent was to get the system in and we were ... again, this
41 was April of 1999, and what was approaching was the turn
42 to 2000 and that was part and parcel with the Y2K effort
43 undertaken by Hydro to ensure that we were going to be
44 able to deliver through that new year. What I was referring
45 to here, as the CEO, was the fact that this whole approach
46 with JD Edwards systems did change our organization's
47 structure quite a bit and we now have business units. It's
48 a system that really allows you to track costs and it puts all
49 the costs attributable to a process. You're looking at the
50 process more than the function and the whole of the

51 benefit of this new system has yet to be achieved by
52 Hydro. When we finally got this in and got through the
53 year 1999 into 2000 and we're now in 2001, much of the
54 effort in terms of processes, what I'd like to see we haven't
55 achieved yet, because with this rate hearing and the effort
56 put into that, early in this year we decided that we would
57 have another thorough review of our business processes
58 but we would do it in the year 2002, but the advantages of
59 the system that we can take advantage of, we have, and we
60 suspect that this is going to allow for even further
61 improvements, you know, in terms of the total program, so
62 when I say here that I expected it to significantly alter the
63 way in which employees approach and perform their work
64 in future was referring to the fact, as we knew then, that we
65 were going to have a different structure in terms, and a
66 different approach to the way we allocated and tracked
67 costs, and we would have labour managers and, you know,
68 managers of our physical assets separated in a different
69 way than before, and a different approach to how we go
70 about things. That's all that was intended to refer to, yes.

71 MS. BUTLER, Q.C.: Mr. Wells, are you satisfied that the
72 program that you're speaking of in this annual report
73 reduced costs for Hydro?

74 MR. WELLS: Yes, I think it did, and I think that it has
75 capability to assist even more, not only in the tracking of
76 expenses and what the expenses should be properly
77 attributed to, but also in the capability as we get more and
78 more familiar with this whole program that we will be able to
79 achieve ... I'm hoping, let me put it this way, from my
80 perspective we are hoping to achieve even more results
81 and even if that's just reflected in the reduction of costs
82 that would have otherwise occurred, then it's a very
83 positive thing.

84 MS. BUTLER, Q.C.: And can you tell me, Mr. Wells,
85 please, who within Hydro would be able to perhaps give me
86 the details of where these costs were saved or reduced?

87 MR. WELLS: In actual ... you're looking for some sort of,
88 like because of P-2000 we have saved X?

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

90 MR. WELLS: I'm not sure if anyone can do that. If anyone
91 can, I would ... the Vice-President of Finance, Mr. Osmond,
92 will be testifying but in that change of the whole system,
93 whether we could say today that that resulted in X dollars
94 of savings in particular, I'm not sure, but you will ask Mr.
95 Osmond, and from my perspective, that is not the end of
96 the day on Project 2000 in terms of where we started and
97 what we have to do, and where we hope to go with it.

98 MS. BUTLER, Q.C.: I wonder if that exhibit can be marked?

99 MR. KENNEDY: Well it's part of CA-101, so I think we're
100 just marking them as excerpts from existing responses to

1 the RFIs.

2 MS. BUTLER, Q.C.: Mr. Wells, the Consumer Advocate
3 spoke in his opening statements about the Hydro truck
4 passing the Power truck on the highway. Do you recall
5 that reference?

6 MR. WELLS: Yes, I do.

7 MS. BUTLER, Q.C.: Okay, and he made reference to the
8 team coordination effort between the two utility companies.
9 Since Mr. Browne has raised this, I wonder if you could
10 give us your view on the integration of the two utilities.

11 MR. WELLS: On the integration?

12 MS. BUTLER, Q.C.: Working arrangement between the two
13 utilities.

14 MR. WELLS: Some working ... well there are, there are ...
15 what I think the Consumer Advocate was referring to was
16 a series of reports and specifically defined meetings, which
17 have been filed in response to the questions from the
18 Consumer Advocate, and the person who would speak to
19 that would be Mr. Reeves, our Vice-President of TRO, who
20 is the executive on our side involved in these, you know ...
21 he was the Vice-President, the only Vice-President involved
22 on our side directly in those ongoing meetings, and I think
23 Mr. Evans represented Newfoundland Power, and there
24 was a whole bunch of subcommittees and they looked at
25 various ways where you could hopefully save some
26 money, and I think on the detail of that I would defer to Mr.
27 Reeves' evidence. Generally speaking though, there are a
28 number of ways including water management and how we
29 operate the system to the advantage of consumers where
30 Newfoundland Hydro and Newfoundland Power cooperate
31 and one of the things that I could comment generally on is
32 that Newfoundland Power is a distribution utility. Hydro's
33 distribution is a very small part in isolated systems,
34 different than ... our main function is in transmission, high
35 voltage transmission, and production, and many of our
36 systems then are not compatible, a small point, but if we
37 were looking for a common lay down area, and could we
38 use one of Newfoundland Power's yards and store some of
39 our poles there, we find that when we get in their yard their
40 poles, say for argument's sake, are 30 feet long and ours are
41 all 60, or we're in ... so there were areas where we could not
42 be of benefit, or we couldn't find a common benefit because
43 the, essentially the different nature of our business, there's
44 something that we are common on and there were areas,
45 there's not too many areas where the trucks actually do
46 pass, but we ... on the Baie Verte Peninsula is one area
47 where we're fairly significant in distribution, and
48 Newfoundland Power is less in that particular area, but all
49 around us, and things like that. You didn't want me to go
50 into ... I really can't get into the detail of each one of these
51 things, but it's all been filed and the reports were filed. The

52 results were not all that great. I will say that. We didn't, I'm
53 sure Newfoundland Power will confirm, we didn't come up
54 with huge amounts of opportunity here between us.

55 MS. BUTLER, Q.C.: Can I ask you, Mr. Wells, as President,
56 whether you see any inherent efficiencies with one
57 distribution utility in the province.

58 MR. WELLS: Inherent efficiencies?

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

60 MR. WELLS: Well one of the issues you have in the
61 Province of Newfoundland, because it's such a small
62 system we're talking about, relatively speaking, that any
63 one utility could handle it all, or any one utility could
64 handle a segment of it. We're just a small system and we're
65 not likely to have competition ... we continue with
66 regulation. The isolated diesel systems which create most
67 of the subsidy that's going to be the subject matter of this
68 application, you know, I don't know if it's a question of how
69 they're handled, whether there are any efficiencies to be
70 gained there in that element of distribution. That's a large
71 part of our distribution, in Hydro, we're handling it in
72 Labrador. It's unlikely that Newfoundland Power wants to
73 expand into Labrador, into isolated systems, so we might as
74 well, it's probably more efficient that Hydro continue with
75 that and in the areas, in the rural areas where we operate,
76 there's no doubt that in our set up now, as history has sort
77 of ordained it, that Newfoundland Power ... I mean that's its
78 whole focus, is distribution. It's a distribution utility and
79 there may be areas where we're associated with it that they
80 could do the job, certainly do the job of distribution.
81 Whether that would actually save us any great amount of
82 money, I'm not so sure because we still have to handle the
83 isolated systems and we still have to maintain the systems
84 in Labrador. That's not going to go away as far as I know
85 and the cost savings may be very minimal if one picks a
86 particular spot and says well let's see if that will work. You
87 know, unless you can substantiate that there's a significant
88 saving here, it might not be worth doing. It's not ... I'm not
89 saying it's not an area to explore. I think there's an
90 obligation to try to explore any avenue that would reduce
91 costs overall in the operation and maintenance of the
92 system.

93 MS. BUTLER, Q.C.: Thank you, Mr. Wells. Mr. Chairman,
94 those are my questions for Mr. Wells. I alerted my learned
95 friend, Mr. Hutchings, who is to follow me in cross-
96 examination that I would likely be finishing before the lunch
97 hour. I just want to make a note of one undertaking, and
98 I'm just curious in terms of procedures, if somebody is
99 recording the undertakings and who I might look to. Is that
100 Ms. Blundon? Okay, thank you very much, and thank you
101 Mr. Wells.

102 MR. NOSEWORTHY, CHAIRPERSON: Thank you very

1 much, Ms. Butler. We do have 25 minutes left before the
2 lunch break. Mr. Hutchings, are you prepared to begin
3 your cross with Mr. Wells at this time?

4 MR. HUTCHINGS: Yes, Mr. Chairman, we'll deal with a few
5 short snappers and then break for lunch if that's okay. Mr.
6 Wells, I just want to pick up on a couple of points that Ms.
7 Butler was asking you about earlier on and we'll deal with
8 a couple of those before lunch, as I say. In connection
9 with her questions to you about the capital budget and the
10 report from Grant Thornton which showed an actual
11 overestimation of the amounts that would be actually spent
12 in a particular year, I know you have experience outside of
13 regulated industry. Would you say that this is in fact
14 typical of most large organizations that they don't spend all
15 their capital budgeted money in a given year?

16 MR. WELLS: It would probably be more typical than
17 overspending that you be under.

18 MR. HUTCHINGS: Yes.

19 MR. WELLS: Because one of the things if you're into an
20 operating, when you're in an operating entity, no matter
21 what it is, the people that are in charge of all your
22 equipment and facilities, see the need and they all come,
23 you know, in the first instance, the blush of a budget is,
24 leaves it ... in any organization, I suggest that you start
25 with a very, fairly healthy figure and then every effort is
26 made within the organization up to and through to the CEO
27 to cut that down, to try to keep it to your free cash flow and
28 other financial parameters that you would want to keep it
29 at, mindful of the fact that essentials have to be done. So
30 the, the ... and this is a subjective opinion now. I mean the
31 tendency with, in organizations which involve human
32 beings would be that you may try to tackle more than you
33 can reasonably do in the run of a year. On the other hand,
34 take that as a blanket statement, you have to look at the
35 circumstances, and I tried to answer the question by the
36 fact that you really need ... before you make a decision
37 based on the record, you really have to be familiar and
38 comfortable with what that record is disclosing, and I know
39 in my time since we've been having the capital budget filed,
40 to our consternation throughout the year, we have had
41 various difficulties and problems which resulted in the
42 under expenditure and I think that our people can explain
43 the problems we encountered which resulted in deferrals
44 and carryovers that we would otherwise have gotten the
45 job done, and that would eliminate the high percentage that
46 is being quoted in Ms. Butler's questions and what's
47 reported in Grant Thornton. You'd have to look at the
48 detail, you know. I know we experienced ramifications on
49 our transmission line program, which resulted in moving of
50 large amounts of capital dollars from one year to the other,
51 and the thing speaks for itself. We had, we were trying
52 major transmission line upgrades just when the ice storm

53 hit in Quebec and they sopped up, in Quebec and Ontario,
54 for a period of time, everything, you know the very things
55 we were looking for they were into, and that's only
56 exemplary of the point. There are other issues.

57 MR. HUTCHINGS: Okay, what I'm going to suggest to you
58 is that there are really two issues that arise out of this set of
59 facts, this perception that Grant Thornton ... the comment
60 that Grant Thornton has made about the under spending of
61 the capital budget. One relates purely to your request to
62 have your capital budget approved, and obviously that's
63 something that all your remarks are very pertinent to in the
64 sense that you don't want an arbitrary reduction in the
65 capital budget that you've asked to be approved simply
66 because in prior years you haven't spent it all. Is that a fair
67 statement of your position?

68 MR. WELLS: Yeah, I have difficulty with the concept but
69 ...

70 MR. HUTCHINGS: Okay, but the other issue that's here,
71 and this is the one that Ms. Butler referred to somewhat, is
72 the question of the test year, and because 2002 is a test
73 year, I think you would agree with me that the Board needs
74 to come to its best possible forecast of what's going to be
75 in the rate base in 2002.

76 MR. WELLS: I agree.

77 MR. HUTCHINGS: Okay, and is it fair to say that the
78 budget, the capital budget for 2002 in all likelihood is not
79 going to be fully spent?

80 MR. WELLS: If there's anyway of doing it we're going to
81 ...

82 MR. HUTCHINGS: You've never done it yet, correct?

83 MR. WELLS: That's ... maybe the appropriate response for
84 both the Board and ourselves is that we take, you know, a
85 fairly critical review of the capital budget as proposed
86 because it is in a test year and we would try to be as helpful
87 as we can with respect to our expectations and what these
88 expenditures are. Some are clearly capable of being done,
89 like you're ordering a large amount of equipment, and it's a
90 delivery date within the year, then that's pretty clear.
91 Whether we can schedule the work, if we're working on a
92 particular line or something, that's another issue.

93 MR. HUTCHINGS: Yeah, I can understand that Hydro will
94 not want to be cramped by the fact of not having the
95 money approved in its capital budget to actually go out
96 and do the work, but that is, it seems to me, a separate
97 issue from the point of our best forecast of how much
98 money is actually going to be spent in 2002 and that, it
99 seems to me, is the revenue requirement point.

100 MR. WELLS: Yes, well it's certainly an issue in the
101 proceeding, yes.

1 MR. HUTCHINGS: And there wouldn't be a problem with
2 the Board approving a certain amount for the purpose of
3 your capital budget, as a capital budget, and inserting a
4 different amount, and assuming a different amount for the
5 test year in terms of what's going in the rate base in that
6 year, correct?

7 MR. WELLS: Have I stopped beating my wife? Yes or no.
8 *(laughter)* You're saying there'd be nothing wrong with
9 that. There may or may not be. I can't answer yes or no to
10 that question. I take your point and it's probably once
11 reviewed because it's part of this process, the capital
12 budget, that you know, the points will be argued out based
13 more closely on the facts. What you're saying is approve
14 the budget for the purposes of the budget, but for the
15 purposes of rate setting the budget is this. What would
16 you have said if we overestimated, or underestimated our
17 capital budget over the past five years? Would you be
18 willing to go the other way?

19 MR. HUTCHINGS: We have to deal with the facts as they
20 have been established to this point, right.

21 MR. WELLS: I agree, but you got me off facts and into
22 concepts.

23 MR. HUTCHINGS: Well hopefully someday we may have
24 to deal with that point, but for today and this hearing, I
25 think we have to deal with the best forecast of what's really
26 likely to be in the rate base in 2002, correct?

27 MR. WELLS: Yes.

28 MR. HUTCHINGS: Yes, okay. One reason I had a concern
29 about that was because of an earlier answer that you gave
30 to Ms. Butler in dealing with the issue of the projected
31 salary costs and looking at the question of the vacancy
32 allowance which was put at \$1 million and my friend
33 suggested to you that it should in fact be \$1.8 million. You
34 said, as I noted in the course of all of that, that it makes no
35 difference because you will spend, presumably because
36 you will spend whatever you actually spend and the
37 vacancy allowance comes off. Do you recall saying that?

38 MR. WELLS: Words to that effect, that the ... what I was
39 trying to say is that you're not mislead by the figures. We
40 put in a salary figure and a vacancy allowance which is a
41 projection, and therefore we're not taking advantage of the
42 higher salary figure because we're deducting, in this case,
43 \$1 million from it. I was approaching it from that point of
44 view.

45 MR. HUTCHINGS: So would you agree with me that the
46 amount of the salary allowance does, in fact, make a
47 difference, the vacancy allowance, does, in fact, make a
48 difference for the purpose of this hearing?

49 MR. WELLS: Yes, the dollars in total do, yes.

50 MR. HUTCHINGS: Because if you take off \$1.8 million as
51 opposed to \$1 million ...

52 MR. WELLS: You have a better result from your
53 perspective.

54 MR. HUTCHINGS: You have a lower revenue requirement.

55 MR. WELLS: Yes.

56 MR. HUTCHINGS: Yeah.

57 MR. WELLS: That's right, I think the calculation of the \$1.8
58 million, I'm not, I can't just pull up in my mind how that,
59 why ...

60 MR. HUTCHINGS: Four percent of ...

61 MR. WELLS: Oh yes, the thing is that you extrapolate four
62 percent as the average, *(inaudible)* four percent should
63 apply to this year. When we make the allowance it's at
64 least based on what we expect to be the situation. I mean
65 it's not just, it's not arbitrary and capricious in the sense
66 that we look at who is going to retire, you know, who can
67 we ... the number of retirees, the number of vacancies that
68 exist, how long is it going to take to replace those jobs, and
69 every year you're not going to have it right, but each year
70 is different than the other and to take an average in that
71 case, which was the four percent over some period of time
72 and say that's what will apply in this year, then that's what
73 I was objecting to. We don't think that the vacancy
74 allowance will exceed \$1 million, and that's the point I think
75 that if you take the percentage, you would exceed the \$1
76 million and let's use the percentage.

77 MR. HUTCHINGS: Well you're asking us to use the \$1
78 million number.

79 MR. WELLS: Yes.

80 MR. HUTCHINGS: Are you telling me that that number is
81 built up from the bottom? That's a number that is
82 calculated on the basis of actual forecasts?

83 MR. WELLS: Not totally but it's more than throwing a dart
84 at the wall, because human resources and the various
85 operating divisions, we start off the year, we know what
86 our vacancies are. We have, we can't predict the retirement
87 of a person but we can say that on our records X people
88 are now coming into a year where they can retire with full
89 pension and they may avail of that opportunity.

90 MR. HUTCHINGS: So is there someone coming after you
91 who will be able to explain to us why we should not expect
92 the average vacancies in 2002?

93 MR. WELLS: Well you should, I don't need an expert to
94 say that. I can say that. You should never expect the
95 average the next year when an average is a composite of a
96 number of years' results. The average would be absolutely

1 fortuitous, wouldn't it?

2 MR. HUTCHINGS: We use a lot of average ...

3 MR. WELLS: You can't use the average. It has to be
4 something else than the average.

5 MR. HUTCHINGS: Well, it's not going to be the forecast.
6 Whatever you forecast, it's not going to be that number.
7 The question is, you know, we use a lot of averages for
8 forecasting for this purpose, right? I mean we've just been
9 through, and we actually agree with you in terms of
10 averaging your hydraulic production and your inflows over
11 50, 70, however many years you can get. That's an average
12 and that's what you use for that forecast. What I'm asking
13 you is why that should not apply in this particular case
14 where we're dealing with a forecast of vacancies?

15 MR. WELLS: Well, I think I've, to the best of my ability,
16 answered the thing in terms of why, you know, there's \$1
17 million in. There may be a witness who could give a better
18 idea of that. Now I'm not sure if there is or not.

19 MR. HUTCHINGS: I'll let you look into that one for us and
20 you can let us know if there's someone who ...

21 MR. WELLS: That will give you some more detail as to,
22 you know, is this a shot in the dark or is it really ... it is a
23 forecast. To that extent it's not going to be necessarily 100
24 percent accurate, but it's not just we'll throw in a million
25 dollars this year and we'll throw in \$400,000 in another year
26 and there's no rhyme nor reason to it. There is some basis.

27 MR. HUTCHINGS: No, no, it's purely an effort to get the
28 best forecast we can.

29 MR. WELLS: That's right.

30 MR. HUTCHINGS: And we'll, once we understand where
31 the million came from we may be able to ...

32 MR. WELLS: We may be able to provide you with more
33 comfort with that million, not necessarily the way you want
34 to go with it but ...

35 MR. HUTCHINGS: Yeah, I quite understand. There's one
36 other point that came up yesterday actually in your
37 discussion with Ms. Butler that I wanted to pick up on and
38 it's a somewhat legal point and despite your background I
39 won't ask you for any legal opinion because that's not what
40 you're there for right now. In speaking with Ms. Butler
41 about the question of the subsidization of the rural deficit
42 you both agreed, and it shows up, and I don't think you
43 need turn to it, at page 31 of the transcript of yesterday,
44 you said that ... the question was do you agree that the
45 subsidization of the deficit which is incurred in some areas
46 by other customers is a matter of social policy directed to
47 you by government, and Mr. Wells' answer was, oh,
48 definitely, yeah, it's the government that made that

49 decision. Do you recognize the difference between the
50 government making a decision and the legislature giving a
51 direction in a piece of legislation?

52 MR. WELLS: Yeah, there would be a distinction.

53 MR. HUTCHINGS: Yes.

54 MR. WELLS: I mean between the government, something
55 in legislation and the government decision that's not
56 expressed (inaudible).

57 MR. HUTCHINGS: Yeah, and this particular one isn't ...

58 MR. WELLS: Which line are we on there?

59 MR. HUTCHINGS: We're on line 37, yeah, line 37 ... yeah,
60 35 to 39, I guess.

61 MR. WELLS: Well I think what I ... my response to the
62 question is that ...

63 MR. HUTCHINGS: Yeah, it's page 31 of the transcript as
64 opposed to page 31 of the PDF.

65 MR. WELLS: Yeah, I've got it here.

66 MR. HUTCHINGS: Okay, good.

67 MR. WELLS: She was tying, Ms. Butler was tying a
68 reference I had made in my pre-filed testimony, I guess, to
69 social policy.

70 MR. HUTCHINGS: Yes, yeah, no, I wasn't so much
71 concerned with the context of the question but the
72 distinction to be made because in fact this decision was a
73 legislative decision as opposed to simply a government
74 decision, correct?

75 MR. WELLS: Okay, yes, it's in the legislation, yes, so we're
76 all directed.

77 MR. HUTCHINGS: Yeah, exactly.

78 MR. WELLS: Yeah, it's the law of the land so we play our
79 cards as they're dealt, everybody.

80 MR. HUTCHINGS: And government is bound by the
81 legislation just as we are.

82 MR. WELLS: Yes, that's right.

83 MR. HUTCHINGS: Yeah, okay, and the Board is bound by
84 the legislation, okay, alright. Okay, we can pursue that
85 point a little further later on. I'm just trying to see if we
86 have another short snapper that we can fill in here before
87 the break. This is a point that came up in your testimony at
88 page 9. In the paragraph that starts at page 11, you're
89 dealing with the question of the preferential rates that Ms.
90 Butler also discussed with you and you say in your pre-
91 filed evidence in the last sentence of that paragraph, that
92 Hydro makes this proposal in light of the impact of the rate
93 increases requested, and I take your point to have been

1 there that because the rate increases were so high, you
2 didn't want to go further and eliminate the preferential rates
3 immediately or even start to eliminate them immediately at
4 the time of this hearing, is that fair?

5 MR. WELLS: It was in the context, yes, of the rate
6 increases that will occur in any event without any particular
7 direct action on preferential rates other than that we have
8 proposed.

9 MR. HUTCHINGS: If we could bring up the answer to IC-
10 121? This question was the proposed percentage increase
11 to fish plants, churches and community halls, and these are
12 the people who benefit, some of the people who benefit
13 from preferential rates. Okay, and the overall estimated
14 increase is 3.7 percent, correct?

15 MR. WELLS: Yes.

16 MR. HUTCHINGS: Okay, if fish plants are getting a break,
17 if you will, because they have to deal with a 3.7 percent
18 increase, does that not quite seem fair when you're asking
19 industrial customers to deal with a ten percent increase?

20 MR. WELLS: Well the fish plants were in the class with the
21 schools and the libraries, and that sort of \$500,000 item, and
22 if you had to separate out ... well you either go for all or
23 you go for none, and whether we were right or wrong, we
24 chose to go for none. If I might share with you, in rural
25 Newfoundland, things are having a rough time and I,
26 because of the job I hold, I mean I am the one who has the
27 benefit, I get the letters and the phone calls from people
28 who represent, not the fish plants now, but the churches ...
29 I mean I have discussion, they have ... on rates and the
30 costs and you get around rural Newfoundland a bit and
31 they're having a difficult time with any increase. I suppose
32 that shouldn't influence, you know, the way you deal with
33 things, but it was just the class. We looked at the \$2.5
34 million or \$2.6 million and saw that \$2 million of it was
35 attributable to government. There was another \$500,000 or
36 \$600,000 that involved these fish plants and schools,
37 churches, community halls, and libraries and said we're
38 giving them a break really for another two years, but that's
39 not our final decision, you know. You should, you will be
40 commenting on that, and the Board, and the efficacy and
41 we just made a proposal. If people think that that's really
42 not right, then it will be corrected.

43 MR. HUTCHINGS: I think you recognize that this is a rate
44 that could appear to be discriminatory in certain situations.

45 MR. WELLS: So the preferential rates, just on the nature of
46 them, probably are discriminatory in that they are shown to
47 be different than the general rate, and you have to look
48 back to where did they come from and how did they get
49 into the system and we are on record with the Board that,
50 and agree, and the Board is certainly on the record, that

51 we've got to get rid of the preferential rates and promote
52 rate equity and the question is how you go about it
53 because there are interested ... you will hear before this
54 proceeding is over, they got a lot to say about their rate
55 treatment.

56 MR. HUTCHINGS: Oh, I don't doubt that at all, and I mean
57 no one wants to pay more but it raises the question when
58 a particular group is allowed to continue at a certain rate, in
59 order to avoid an increase of more than 3.7 percent,
60 whereas other groups are already asked to pay 10 percent.

61 MR. WELLS: I don't, you know, the issue of a seasonal
62 fish plant in a remote community in the shore of Labrador
63 today, and it's ability to absorb increases in an operating
64 period which is now even cut down further with the
65 problems they're having in the fishery, I compare that to
66 Abitibi Consolidated Inc., and could they absorb an
67 increase a little more than a seasonal fish plant in a remote
68 community in Newfoundland ...

69 MR. HUTCHINGS: But I mean are you saying that that's
70 Hydro's approach or ...

71 MR. WELLS: No, it's not Hydro's approach, but you know,
72 you put the question of the fairness of it all and I've been
73 honest in saying to you that we took it as a lump, not fish
74 plant specific, because we can't distinguish between those
75 fish plants that may be doing very well this year and some
76 that are now, so who knows, but we just said there's \$2.5
77 million here that really, it will help reduce the subsidy.
78 We're moving on the two, with the two governments.
79 We're proposing for your consideration and that of the
80 Board and the others, and we're not strenuous in argument
81 either way.

82 MR. HUTCHINGS: No, and I mean this is clearly not one
83 of those issues that I referred to yesterday which is
84 important because of the number of dollars involved but it
85 is important because of the principles involved and you
86 have to ...

87 MR. WELLS: Well I thought we had all agreed on the
88 principle, no preferential rates, and that they be eliminated
89 over time. We were quite clear on that.

90 MR. HUTCHINGS: Fair and nondiscriminatory.

91 MR. WELLS: Yes.

92 MR. HUTCHINGS: Yeah, okay. I think that would be a
93 good time to take the lunch break, Mr. Chair.

94 MR. NOSEWORTHY, CHAIRPERSON: Thank you very
95 much, Mr. Hutchings. We will break for lunch now and we
96 will reconvene at 2:00 this afternoon. Thank you.

97 (break)

98 MR. NOSEWORTHY, CHAIRMAN: Good afternoon, we

1 are in a position to continue. I appreciate, Mr. Hutchings,
2 your short snappers this morning. It certainly entitled to
3 embark upon more routine questioning at this point in time.
4 I would ask if you do have any notions of when you might
5 be completed with the witness, individual counsel, it might
6 be useful and helpful to make that indication known, simply
7 from the point of view of the next cross in line so at least
8 mentally in any event they might be able to get a little bit
9 prepared, if it's this afternoon or tomorrow morning, or what
10 have you. Certainly, I recognize that you need some
11 flexibility and if your not in a position to do that, that's
12 certainly fine, but where that can be achieved it might be
13 useful for all concerned.

14 MR. HUTCHINGS: Certainly Mr. Chair, and I have already
15 indicated to Mr. Browne that I would expect that my cross
16 will use up this afternoon at least and we'll see where we
17 are as we get closer to 4 o'clock.

18 MR. NOSEWORTHY, CHAIRMAN: Right, thank you very
19 much.

20 MR. HUTCHINGS: Mr. Wells, I want to deal first of all this
21 afternoon with questions that revolve around the phase
22 out of the rural subsidy and I want you to look initially at
23 the relevant section of the Electrical Power Control Act
24 which is Section 3(a)(iv) which should be coming up on
25 your screen. Okay. You have it there now. It's the third
26 paragraph from the bottom. The opening words which we
27 needn't bother to put on the screen of course of Section 3
28 is it is declared to be the policy of the Province that the
29 rates to be charged either generally or under specific
30 contract for the supply of power within the Province, and
31 then we get to sub. 4 which provides that they should be
32 that after December 31, 1999 industrial customers should
33 not be required to subsidize the cost of power provided to
34 rural customers in the Province and those subsidies being
35 paid by industrial customers on the date this Act comes
36 into force shall be gradually reduced during the period prior
37 to December 31, 1999. Can we agree that this Act came into
38 force on January 1, 1996?

39 MR. WELLS: Yes.

40 MR. HUTCHINGS: There is an Order in Council to that
41 effect, but I don't think we need to go to that extreme. I
42 guess the first question, Mr. Wells, is were the subsidies
43 being paid by industrial customers as of January 1, 1996
44 gradually reduced during the period to December 31, 1999?

45 MR. WELLS: No, they were not.

46 MR. HUTCHINGS: They were totally eliminated in one fell
47 swoop, if you will, on December 31, 1999.

48 MR. WELLS: That's correct.

49 MR. HUTCHINGS: Okay. If you may refer at this point to

50 IC-8, page 2 of 2, the question here involved the total
51 amounts contributed by industrial customers to the rural
52 subsidy during the years 1995 to '99 in the amount that
53 would have been contributed if these subsidies had been
54 gradually reduced as in our view the Act provided and will
55 you agree with me on the basis of my arithmetic that a little
56 more than nine million dollars represents the difference
57 between the subsidy that was actually paid and the
58 subsidy that would have been paid under this scenario
59 based on the reductions?

60 MR. WELLS: If you accept the methodology for the
61 reduction, yes

62 MR. HUTCHINGS: Yes.

63 MR. WELLS: Yes, that would give you that kind of a
64 mathematical difference.

65 MR. HUTCHINGS: Yes, okay. Given that there was a
66 period prescribed which started at the beginning of 1996
67 and went to the end of 1999, would you feel that these 20%
68 reductions would have been appropriate, an appropriate
69 way of dealing with that, a reduction starting in 1996 and
70 going to 1999 in the fashion illustrated.

71 MR. WELLS: It would be one way to deal with it if there
72 was no definition in the legislation as to the rate of the
73 gradual decreasing of the subsidy. I'm not sure what your
74 using there was 20% a year. I mean that would not be a
75 logical or it could have been some other approach.

76 MR. HUTCHINGS: Yes, that's somewhat like the approach
77 your looking at now in phasing out preferential rates over
78 a five year period.

79 MR. WELLS: The same 20% factor, yes.

80 MR. HUTCHINGS: Uh-hum. So that's an acceptable
81 reasonable approach, if one decides one has to gradually
82 reduce or phase something out.

83 MR. WELLS: It could be, yes.

84 MR. HUTCHINGS: Yes. Well it could be. Do you think it
85 is?

86 MR. WELLS: Well it's not a fact but essentially I'm
87 agreeing with that if you took that approach and 20% over
88 five years you would get the result.

89 MR. HUTCHINGS: No, my question is would that a
90 reasonable approach to take if one assumed that you had
91 to gradually reduce the amount of subsidy.

92 MR. WELLS: It would be and if one could, it would be.
93 Nobody would have thought it to be untoward if that
94 approach were taken.

95 MR. HUTCHINGS: Okay. That's fine. Now perhaps you
96 can explain for us why the subsidy was not gradually

1 reduced.

2 MR. WELLS: Well first of all, as you confirmed through me
3 the EPCA amendment to which you referred did not come
4 into force until January 1st, so there was no possibility of
5 starting the decline that would cover the 1996 year in terms
6 of the 20%, if you wanted to do that we, the Act became in
7 effect the first day of the year. That's one consideration
8 and if you'll bear with me to go back to the events of the
9 time, in January of that year there was within government
10 there were certain changes that took place, the resignation
11 of the Premier, and there was another Premier appointed
12 and then there was an election and in effect a new
13 administration and the whole thing, you know, we were
14 getting down through into the spring of 1996 and before
15 there was a discussion with the shareholder with respect to
16 that particular legislation and its application ... and the
17 other factor was that if we were to make a move it would
18 require going to the Public Utilities Board because one
19 would presume that if you were going to implement that the
20 Board would have to approve it, and certainly the Board is
21 the only authority that could reallocate those costs, if they
22 were to be reallocated ... this cost of the system which
23 everybody agreed that they were. The issue evolved to
24 this in the course of the discussion with Government they
25 ... let's say it was the new administration, they were
26 reviewing a number of things because we weren't the first
27 object of their attention, after Mr. Tobin came into
28 Premiership and after the election, so when Hydro was
29 involved in briefing Government with respect to issues that
30 were outstanding or you know, on the table, that would
31 have been one and the Government wanted to rethink the
32 position on that issue, and we were advised to that effect.
33 Therefore, the matter stayed in that way for some time and
34 there were other events happening which affected Hydro,
35 now not specifically this clear legislative direction. I'm not
36 going to dispute that with you, but in trying to explain why
37 nothing happened, or we didn't take any particular action.
38 There were a variety of things that were happening which
39 would affect the power situation within the Province, if I
40 can put it that way. By the time we got to the end of 1996,
41 the issue was all about the new smelter requirements, the
42 new smelter for Voisey's Bay, and at the end of '96 we were
43 in a position of having to issue a request for proposals to
44 try and crystalize the situation with respect to a source of
45 new power generation and do it within a six month
46 timeframe. It had never been tried before that way. I mean
47 our people were put to a real test and they came up with it,
48 but our whole preoccupation and in terms of January 1,
49 1997 down to June, or July was this request for proposals
50 that was issued ... getting them in, vetting them and
51 everything in coming to a position to be able to respond to
52 the Government, or anyone else, as to what the results were
53 and that certainly was the preoccupation with Hydro in

54 terms of rates and ... the other thing I should say, this was
55 a requirement for 200 megawatts and 1,400 gigawatt hours.
56 In our system, you know total counting everybody, 1,800
57 and 8,000 gigawatt hours that particular requirement that
58 particular requirement would have had a fairly major impact.
59 And the best I can say to you trying to go back and explain
60 this is that was one big factor that was occupying, not only
61 ourselves in doing the work in trying to come up with the
62 answer here but also in the mind of Government so that we
63 didn't get any specific direction to move in this regard ...
64 that they were still, had the issue under consideration as to
65 where, you know, the Government, being Government, was
66 in the position to change that legislation if they so wished
67 and the way it was put to us that was being contemplated.
68 So then you, as I think back, by the fall of 1997, we were
69 fairly well into the issue of negotiations with Hydro Quebec
70 in this first go around on the development of the Lower
71 Churchill, which reached a really high point towards the
72 end of the year. Not necessarily to the knowledge of the
73 public, but certainly to Hydro. We were involved in it and
74 Government, you had the big announcement of March 9,
75 1998. That has an affect on things in a sense that if the
76 project as described was going to go ahead, if that were to
77 happen, it would also affect the power requirements of the
78 island because it was contemplated at the time of a line to
79 the island if Churchill were going to be developed, and the
80 whole situation with respect to, you know, how we were
81 going to be going forward in Newfoundland and Labrador
82 with the big impact of a smelter in Argentina, you know, a
83 huge requirement relative to the system. The possibility of
84 an interconnection to Labrador and the best I can say to
85 you is that slowed down everybody's thinking and
86 nobody, and well the fact of the matter is that this issue
87 was not addressed. It was finally addressed as matters got
88 clarified and as is on file in our pre-filed testimony, in 1999,
89 because we had made representations to Government at
90 various times that this was an outstanding issue, and we
91 finally got confirmation of a direction with respect to that
92 from, in October of 1999 and you have that letter, a copy of
93 that letter in your possession, which clearly states what the
94 Government wanted us to do at that time and we then
95 subsequently filed with the Board in, and had the interim
96 order in the result of that someone argued got us to this
97 hearing. I think we would have been in this application
98 anyway, but it certainly led through to where we are today.
99 That is essentially the best I can shed on this circumstance.

100 MR. HUTCHINGS: Okay. I'd like to go back to an early
101 part of your answer where you said because of changes
102 that were happening within Government it was the spring
103 of 1996 before you could a discussion with the shareholder.
104 Why would need to have a discussion with the
105 shareholder?

106 MR. WELLS: Well I think that in the practical matter if we

1 were going to apply to the Public Utilities Board and to
2 reallocate the cost and then set out the, in some
3 appropriate way to follow what you would say were the
4 clear legislative direction with gradual reduction, I mean it
5 just seems the most appropriate thing to do. We, we did
6 put together a packet of things for the consideration of
7 Government after the change of matters related to Hydro
8 and that was one of the matters, and it was definitely
9 brought to Government's attention that this was a
10 legislated requirement under the previous administration
11 and did they wish to confirm it and we moved ... I don't
12 know if it was put in those terms, but it was certainly said
13 that this was one of things, and the repercussions of that
14 if this burden was no longer to be on our industrial
15 customers under the new legislation it all came in effect
16 there in '96, we would have to apply to the Public Utilities
17 Board to reallocate the cost and you would advise ... I
18 mean, the operating department of Government that we deal
19 with is Mines and Energy, so it would be normal for Hydro,
20 or say me, or the Board, to make the responsible minister
21 aware of things that we were doing. I mean we just
22 wouldn't go to the Public Utilities Board and not give the
23 shareholder the courtesy of a briefing in what the issues
24 are.

25 MR. HUTCHINGS: No, I fully appreciate that that is in
26 practical terms what would happen but you will agree with
27 me that the legislated direction is essentially to Hydro and
28 it's Hydro's responsibility to effect it.

29 MR. WELLS: Crystal clear. Yeah, the other thing though
30 that the shareholder also had the, has the capability to
31 reconsider and there was in effect a change within this
32 composition of the shareholder at a fairly important level
33 and as it turned out the shareholder did not want us to
34 apply immediately, in effect. They said we will get back to
35 you, in effect, you know.

36 MR. HUTCHINGS: You and I agreed this morning, Mr.
37 Wells, that the legislation is binding upon the Government,
38 the shareholder, as well as yourselves, and ourselves and
39 the Board, so that the legislation not having changed, was
40 it still not your clear legislative duty to apply to the Board
41 and effect this gradual reduction?

42 MR. WELLS: The duty was in the legislation had we been
43 talking to any other party other than the party that had the
44 power to change the legislation, I would agree.

45 MR. HUTCHINGS: Who has the power to change the
46 legislation, Mr. Wells, is it the Government or the
47 Legislature?

48 MR. WELLS: The Legislature, but the Government can
49 pretty well organize that.

50 MR. HUTCHINGS: Well that may be a political reality, but

51 we're here dealing with a particular legal proceeding under
52 a particular piece of legislation and the legislation did not
53 in fact change. Isn't that correct?

54 MR. WELLS: That is true, and the other thing is you can
55 keep asking me what happened and I will tell you what
56 happened and I can't change that either now.

57 MR. HUTCHINGS: So from your answer we can take it that
58 other events basically took control of what was happening
59 with Hydro to the point that you didn't get around to doing
60 what was necessary to do to implement this legislation.

61 MR. WELLS: The other events, no, not that they ... they
62 didn't prevent us. We still had the capability to do it but
63 we were certainly acting on the kind of reaction that we had
64 from government, that they wanted to think about this. In
65 other words, if we had gone ahead and filed, somebody in
66 Government would have certainly said, you know, can't
67 you hear, we told you to hold off here till we get back to
68 you on it. You know that would have been the type of
69 layman's terms we were in. The other thing, I'm sure is that
70 your clients were aware of the legislation and had
71 opportunity to discuss things with the powers that be.

72 MR. HUTCHINGS: And, were you aware of any
73 discussions between any representatives of the industrial
74 customers and Hydro?

75 MR. WELLS: No, I certainly wasn't, no. No, I wasn't privy
76 to any discussion. No.

77 MR. HUTCHINGS: And you weren't aware that there were
78 any discussions?

79 MR. WELLS: Ah, there was a stage later on I was aware
80 that meetings had been taking place, but I, other than there
81 were meetings and I was aware that there were meetings, I
82 don't know anything more than that about it.

83 MR. HUTCHINGS: Okay. Alright. So is it fair to say that
84 as a result of that discussion, Mr. Wells, that it in fact does
85 make a difference whether the Crown is the shareholder in
86 your situation.

87 MR. WELLS: Yes, in certain instances you have to be ...
88 we're not a broadly held Corporation, and unique in a sense
89 that the Government is the shareholder, represents the
90 taxpayers, I suppose who own the ...

91 MR. HUTCHINGS: I mean if you want to take an analogy
92 I don't think the people at Newfoundland Power would
93 have much to say if Fortis told them that they should not
94 comply with the provisions of the Public Utilities Act. Do
95 you agree with that?

96 MR. WELLS: They would have less protection, say, than
97 we would have, and I don't know if we would have that
98 protection if push comes to shove.

1 MR. HUTCHINGS: Well the Board may decide that, Mr.
2 Wells. I think we'll move on then. You were aware, I
3 presume, although it was before your time, of a report by
4 the Board in connection with cost methodology in 1993.

5 MR. WELLS: Yes, well I'm certainly no expert on that but
6 the fact that there had been the study and there was going
7 to be, and the implications for any future dealings with
8 rates and what not.

9 MR. HUTCHINGS: Yes, okay. Now I really hesitate to be
10 the first person talk about a cost of service study in this
11 proceeding, but I just need you to look at two pages, which
12 I think I've marked in the volume that you have there, and
13 their in response to IC-1. There are two pages. The first is
14 the back of the third page of the answer to IC-1 which is ...
15 let me make sure I have the right page. Yes, it's page 2 of 60
16 of the 1992 forecast final cost of service and the heading is
17 "Comparison of Revenue and Allocated Revenue
18 Requirement". Do you have that?

19 MR. WELLS: Yes, on mine the thing marked says page 3 of
20 60. Is there any ...?

21 MR. HUTCHINGS: Okay. Yeah. Yeah, I don't think it
22 really makes any difference. The same number that I am ...

23 MR. WELLS: It's the 1992 forecast - final heading.

24 MR. HUTCHINGS: Uh-hum. That's right.

25 MR. WELLS: Yes.

26 MR. HUTCHINGS: Okay, I want to refer you to the final
27 which was in fact the existing methodology prior to the
28 cost methodology hearing. Is that correct?

29 MR. WELLS: I have no idea if ... I'm not contesting it. I
30 have no idea, and if this sheet is the ... prior to the 1992
31 order.

32 MR. HUTCHINGS: Okay, well lets, lets go about it this
33 way. It is part of this application to implement, with
34 modifications, the methodology that was proposed in 1993.
35 Is that correct?

36 MR. WELLS: Yes, definitely.

37 MR. HUTCHINGS: So whatever was in place in 1992 is
38 before the hearing so that's the old one.

39 MR. WELLS: Okay. Uh-hum.

40 MR. HUTCHINGS: Okay, so the revenue requirement, and
41 we'll look at revenue after deficit allocation which is under
42 column 6. For industrial customers you'll see a number
43 there of 45,547,309.

44 MR. WELLS: Yes.

45 MR. HUTCHINGS: Okay. I want you now to flip to the
46 second marked reference and that, I think, is at page 2 or 3,

47 MR. WELLS: 3 of 61.

48 MR. HUTCHINGS: 3 of 61, and the heading there is "1991
49 Cost of Service Methodology Hearing".

50 MR. WELLS: Yes.

51 MR. HUTCHINGS: Okay and this is the comparable
52 number under, in the same place under heading, under
53 column 6 industrial, 43,965,711. So the difference between
54 those two numbers is 1.581 million dollars. I ask you to
55 accept my arithmetic on that, and I would suggest to you
56 that that was the forecast at the time of the 1993 hearing for
57 the difference that this would make to the industrial
58 customers. It was gonna save them a little over one and a
59 half million dollars if the new methodology was
60 implemented. Is that correct?

61 MR. WELLS: Yes.

62 MR. HUTCHINGS: Alright. Are you familiar with, what
63 has been called the interim and the generic methodologies?
64

65 MR. WELLS: I'm going to have to plead ignorance.

66 MR. HUTCHINGS: Okay. I don't think I put out the volume
67 for you, but could you look at IC-18, and actually I think
68 the answer to this is on the system, IC-18 revision two, and
69 page 2 of 2. Okay. The bottom half of that page shows
70 definitions of three different methodologies.

71 MR. WELLS: In whose testimony is this filed?

72 MR. HUTCHINGS: This is the answer to the question put
73 by the industrial customers IC-18, okay filed by Hydro.

74 MR. WELLS: Sorry, okay, uh-hum, but this relates to Mr.
75 Brickhill's evidence.

76 MR. HUTCHINGS: I suppose you could say it's Mr.
77 Brickhill's evidence, yeah. So the interim methodology as
78 referred to there is defined as being the methodology
79 approved by the Board in its report in, dated April 1992. So
80 that was the methodology which was basically in place
81 prior to the generic methodology being approved in the ...

82 MR. WELLS: Yes, okay. Yes, it was just to differentiate
83 the three things that were happening, yes.

84 MR. HUTCHINGS: Yes, exactly. Okay. So the generic one
85 is the 1993, the February 1993 report and then we have the
86 proposed one which is the current one that you're looking
87 for approval of now.

88 MR. WELLS: The generic being a basis for the next
89 hearing and the next hearing would confirm, yes

90 MR. HUTCHINGS: Yes, okay. So I want to try to avoid
91 taking you through a whole bunch of additional references
92 in the, in these cost of service studies but I'm going to

1 suggest some numbers to you and in the answers, and I'm
2 referring to the cost of service studies, and these are all
3 produced in the answers to either IC-1 or IC-18. I'm not
4 going to ask you to open these up, I'm going to ask you to
5 take on faith the numbers that I'm giving you. In respect of
6 1999 the interim cost of service study, at page 3 of 88, will
7 show the revenue requirement for industrial customers at
8 45.287 million. The generic cost of service, at page 3 of 92,
9 shows a revenue requirement for industrial customers at
10 41,947,000, and odd. And there's a difference there of about
11 3.3 million, and my suggestion on that basis is that if in
12 1999 the generic methodology had been in place there
13 would have been a saving to industrial customers of 3.3
14 million dollars.

15 MR. WELLS: You may be right.

16 MR. HUTCHINGS: If those are the numbers..

17 MR. WELLS: But you're using the 1999 interim cost of
18 study against the 1992 cost of service study.

19 MR. HUTCHINGS: No, 1999 generic.

20 MR. WELLS: The 1999 generic ...

21 ...MR. HUTCHINGS: Verus the 1999 interim.

22 MR. WELLS: Yeah, which is what Hydro should be using
23 is the generic after we got past '93.

24 MR. HUTCHINGS: Yes.

25 MR. WELLS: Yeah, so we applied ...

26 MR. HUTCHINGS: But that's not what you used.

27 MR. WELLS: You're saying that's not what we used.

28 MR. HUTCHINGS: You are still, as I understand it,
29 applying the interim methodology. Is that not correct?

30 MR. WELLS: I've never had any discussion with anybody
31 in Hydro that we're using the interim as opposed to the
32 generic specifically.

33 MR. HUTCHINGS: Okay. So

34 MS. GREENE, Q.C.: I hesitate to interrupt in cross
35 examination. I don't know if it would be more helpful for
36 counsel for industrial customers if he addressed these
37 questions to Mr. Osmond or Mr. Brickhill. Mr. Wells is not
38 familiar with the details of cost of service study, and I will
39 confess I helped draft the definitions here, so Mr. Wells
40 didn't see those but they were reviewed with our rates
41 people.

42 MR. HUTCHINGS: Oh, Mr. Chairman, perhaps what I will
43 do is to ask Mr. Wells to make certain assumptions in that
44 regard, because otherwise I'll only have to recall him after
45 we speak to Mr. Osmond or Mr. Brickhill.

46 MR. NOSEWORTHY, CHAIRMAN: Would you have any
47 objection to that?

48 MS. GREENE, Q.C.: No depending on the nature of the
49 question. We're prepared to acknowledge that there is a
50 change with respect to the allocation of cost to industrial
51 customers and to Newfoundland Power arising from which
52 cost of service methodology is used. I just don't know if it
53 would be helpful to try to get Mr. Wells to be the witness
54 for the specific difference, in dollar amounts of the cost
55 allocations to each of these customers, but I am prepared to
56 acknowledge as counsel for Hydro that there is a difference
57 in the allocation of cost to all of our customers based on
58 which methodology is used, and the detail of that, my
59 suggestion is, Mr. Osmond would be the most helpful with
60 Mr. Brickhill in providing the detail of those changes with
61 the different methodologies. I don't know if that's helpful.

62 MR. HUTCHINGS: I don't have any difficulty with carrying
63 on on that basis Mr. Chair.

64 MR. NOSEWORTHY, CHAIRMAN: Okay. Thank you
65 very much.

66 MR. HUTCHINGS: In any event, Mr. Wells, from what we
67 have been able to determine from the cost of service
68 studies, the failure to implement the generic methodology
69 cost industrial customers 3.3 million in 1999, 3.7 million in
70 2000, and ...

71 MR. WELLS: It's just those years that ...

72 MR. HUTCHINGS: No, no those are illustrative years,
73 because those are the ones we have the cost of service that
74 we can make the comparisons. Is there any reason that you
75 can point to that Hydro did not make a separate application
76 to implement this generic cost of service methodology
77 instead of waiting until the next rate hearing came up.

78 MR. WELLS: Just generally, my understanding would be,
79 would have been that we would not deal with the cost of
80 service methodology until the next rate hearing, and you
81 know, with respect to this whole area, I apologize I can't,
82 but I just did not anticipate, nor did anybody, or my
83 associates expect that I would be getting into cost of
84 service methodology. You know, so I really didn't prepare
85 for this.

86 MR. HUTCHINGS: No, and I'm not trying to take you into
87 the methodology as such, but rather the effects of it. Did
88 you understand, or did you have any understanding that
89 the failure to implement this methodology was costing the
90 industrial customers a lot of money?

91 MR. WELLS: That was never discussed with me.

92 MR. HUTCHINGS: Okay. Alright. The other issue that
93 comes up, and again we'll discuss the numbers in more
94 detail with Mr. Osmond, is comparison between the generic

1 methodology and the proposed methodology as it relates
2 to the test year 2000, and were you aware that so far as we
3 can calculate the implementation of the proposed as
4 opposed to the generic methodology will cost industrial
5 customers an additional 1.7 million dollars each year, or that
6 year, in the test year?

7 MR. WELLS: No, not in that sense, no.

8 MR. HUTCHINGS: Have you become aware of the effect
9 on industrial customers of certain reallocation of assets
10 from specifically assigned to common for the purpose of
11 the cost of service studies?

12 MR. WELLS: Related to this hearing, yes.

13 MR. HUTCHINGS: And that involves both the Great
14 Northern Peninsula and some other areas.

15 MR. WELLS: The one I'm most familiar with would be the
16 Great Northern Peninsula. There are others.

17 MR. HUTCHINGS: Yes, okay. And I think the answer
18 appears in IC-134, it probably wouldn't hurt to put that on
19 the screen. And on page 2 of 2 we can see, and perhaps
20 the numbers to the right-hand side after deficit and revenue
21 credit allocations have been made are the more telling
22 numbers that from the four proposed changes in plant
23 assignment that we see there, there is a total of \$1,621,000
24 added to the cost for the industrial customers and \$4,000
25 taken away as a result of these assignments.

26 MR. WELLS: Yes.

27 MR. HUTCHINGS: Yes. Okay. Now I suppose, Mr. Wells,
28 one tends to look at it as an additive sort of process in the
29 sense that from the point of view of the industrial
30 customers, we have the failure on the part of Hydro to
31 phase out the industrial, or the rural subsidy as regards to
32 industrial customers. We have the failure on the part of
33 Hydro to implement the cost of service methodology which
34 would have meant savings to the industrial customers. We
35 have now a new proposed methodology which apparently
36 assigns again more cost to the industrial customers, and we
37 have a bunch of changes in plant assignment that is again
38 putting more cost on the industrial customers. Is this part
39 of some plan or policy on the part of Hydro or is this pure
40 happenstance?

41 MR. WELLS: Well you may not believe this but the issue
42 of the industrial customers and what they would have to
43 pay in charges is on our mind and, you know, from the
44 general view of it we have been concerned about the
45 impact on our industrial customers, and for that matter,
46 Newfoundland Power and consumers, but I'm well aware of
47 the clients that you represent and the role they play in the
48 Newfoundland economy and some of the issues and
49 difficulties that they have to contend with, so there is no

50 plot to get the industrial customers. The issue of the
51 things that you now speak, rather than get into the cost of
52 service study because I never did try to venture into there
53 and figure out what they were going on with, but the issue
54 of the, like the interconnection of the Great Northern
55 Peninsula and the impact that may have and my
56 understanding of that, and again, other Hydro witnesses
57 will speak to the particulars, was that the Board had
58 expressed the view that that, when the interconnection
59 took place, that the matter should be treated as common
60 until the next hearing for the Board to consider it, so I take
61 it that the Board had taken just an interim view of it, and
62 therefore the application of those GMP assets to common
63 is in line with the Board's recommendation that that's what
64 we should do but subject to the caveat that the Board
65 would review that at this hearing, so you know, it's not that
66 we were targeting anything in terms of the industrial
67 customers specifically. There are a number of issues. That
68 is one. The frequency converters is another that has been
69 the subject of a fair amount of discussion between Hydro
70 and industrial customers or representatives, and I have
71 been involved in that directly and discussions, you know,
72 back over the last three or four years about the frequency
73 converters. We tried to work a way around it or through it.
74 In the end, and I'm aware of the history that you've
75 presented in the pre-filed testimony on behalf of the
76 industrial customers and the history of it. Hydro is just
77 taking the view that really it's ... at the current point in time
78 that we are now, that the frequency converters really serve
79 the two mills involved, two different companies, and there's
80 an opposing view from that expressed by the companies.
81 I think the issue is most appropriately put to the Board
82 because all we're talking about is which class of customers
83 should bear that expense. Is it specific or is it common, and
84 the Board will weigh the merits of the case and come to a
85 conclusion.

86 MR. HUTCHINGS: Do you know what the cost would be
87 today if we had generators at Bay d'Espoir generating 50
88 cycle power and they had to be changed?

89 MR. WELLS: I'm well aware of that. I don't think that
90 anybody is going to dispute the fact that when the Bay
91 d'Espoir development came into being, and without the two
92 paper mills at the time, things would have been very
93 difficult. You know, you were looking at the future for the
94 province, one of the best things ever happened to the
95 province was Bay d'Espoir development. It's the only really
96 good hydro resource that we have where there's a fairly
97 significant amount of energy, and had there not been these
98 adjustments made to incorporate the two paper mills and
99 Deer Lake Power, for instance, and the developments on
100 the Exploits, things would have not gone the way that they
101 have. You know, we wouldn't argue that. I think the issue
102 becomes over a period of 30 years or 40 years, how long is

1 that supposed to take place, these original arrangements,
2 and I have heard differing views from people who were
3 involved, you know, going back in time and the issue is
4 probably best determined by the Board.

5 MR. HUTCHINGS: Uh hum.

6 MR. WELLS: So the two, you know, your \$1.6 million that
7 you have on that particular page and the Doyle's to Bottom
8 Brook is added in there. I mean these are matters that are
9 open to debate. The Board expressed a view. We have
10 reacted to the Board's view, put the figures there, and the
11 Board has said we want to review this at the next hearing,
12 and so there we are. We're here to review.

13 MR. HUTCHINGS: Well I mean in terms of the allocations
14 obviously we'll deal with the specifics of those with the
15 other witnesses as they come up, but I did want to give
16 you the opportunity to comment upon the whole range of
17 hits that it is perceived by the industrial customers that
18 they have been taking since 1992. Well let's move on and
19 we can turn to some general questions about the situation
20 of Hydro as a Crown-owned utility and the relationship
21 between you and your shareholder, if you will. I noted in
22 your opening statement that on a couple of occasions you
23 referred to the provision of electricity in the province as
24 being an essential service. Is it fair to say that it has
25 always been regarded as such?

26 MR. WELLS: Yes.

27 MR. HUTCHINGS: Yes, okay, can you explain for me why
28 it is that the shareholder of Hydro should expect to make a
29 profit on the provision of this essential service?

30 MR. WELLS: Well the question really becomes that the
31 shareholder, being the government, took the initiative to
32 found Hydro and it's predecessor, the power distribution
33 (inaudible), to bring about the electrification in
34 Newfoundland and throughout, including rural
35 Newfoundland. It was a creation of government policy of
36 the time. There were no private interests that were either
37 capable or prepared to take on that challenge so the
38 government backstopped it and while the government may
39 not have put in a direct contribution of equity to fund the
40 thing initially, what it did do was put its signature to the
41 bottom line and say start the operation, engage in, you
42 know, attracting debt, and move the system forward. You
43 know, I'm paraphrasing here, but I mean essentially we
44 started from square one, accumulated debt which was
45 guaranteed by the government, took the monies and built
46 the system. Nobody else was prepared to do that, so now
47 over time in the operation of Hydro, there was accumulated
48 retained earnings within the company which is essentially
49 the equity of the shareholder, and the question then
50 becomes how do you assess the opportunity cost, or what
51 are the issues that you put into the balance. The

52 government having done this and provided a service that
53 could have been provided, there's no reason why it has to
54 be government, it could be private enterprise, or investor-
55 owned or regulated, or whatever. The question is should
56 the government representing the taxpayers not look at the
57 opportunity costs of its investment, and then you get into
58 the pure question of financial arguments. What are the
59 better signals to send to people who consume, whether
60 they're industrial customers or retail or other distributing,
61 utilities distributing the power, then that there is a cost
62 factor here and that we should treat such an entity as a
63 normal commercial venture, you know.

64 MR. HUTCHINGS: Okay, you're getting, I guess, a long
65 way ahead of where my initial question started.

66 MR. WELLS: I'm sorry, I got ahead of you, did I, with ...
67 bring me back.

68 MR. HUTCHINGS: Yes, come back to the notion of the
69 provision of electricity as an essential service, and
70 undoubtedly it was an initiative of government and money
71 was invested by government directly or indirectly initially
72 I guess through the Power Commission, but what is the
73 distinction between government providing that essential
74 service and providing another essential service like schools
75 or hospitals?

76 MR. WELLS: Well, you don't see too many investor-
77 owned corporations providing services in schools, or for
78 that matter ... there are some but I mean ...

79 MR. HUTCHINGS: Private hospitals.

80 MR. WELLS: Realistically in our society, we would be in
81 pretty poor shape if we depended upon private schools
82 and private hospitals. That is not the options that we have
83 taken generally in Canada.

84 MR. HUTCHINGS: Did we have an option for private
85 development of electricity in the sixties?

86 MR. WELLS: Yes, but you would have to wait a long time
87 for the things that were going to come with respect to the
88 electrification of Newfoundland because the private utilities
89 or the predecessors of Newfoundland Power did not have
90 the capability, or if they had the capability, didn't exercise
91 the opportunity to try to duplicate what Hydro did in terms
92 of generation, so it was government that was instrumental
93 in developing the Bay d'Espoir project which is the
94 foundation of our system in terms of generation, so you
95 know, I don't mean to fence with you, but the fact is that
96 now we've reached this stage of maturity, and for some
97 years, that if you look across the country, Newfoundland
98 and Labrador Hydro, you look to BC Hydro, Manitoba
99 Hydro, Saskatchewan, Ontario as it was and is now, and
100 maybe forever shall be, Hydro Quebec, New Brunswick,
101 every one of these utilities that were started by the Crown,

1 the concept of getting a return on equity and making a
2 profit, even though the electricity to their citizens is also an
3 essential service and gave rise to that. If you go back to
4 the days of the start of Ontario Hydro, back in the 1890's,
5 the whole concept, everywhere else has been that these
6 entities, although they're Crown-owned, should make a
7 profit. To a greater or lesser degree, they have and
8 contributed to the provincial economy and now you can
9 get people who in the financial community like our Mr. Hall,
10 or Ms. McShane will testify about all the utilities, whether
11 they're investor-owned, or state-owned, or Crown-owned,
12 and the fact that they should operate on a certain
13 debt/equity ratio, and that they should properly attribute a
14 cost, an opportunity cost to the capital deployed and that
15 there should be a reasonable return on that capital,
16 consistent with the business risk to which the utility is
17 exposed, so we are only applying here the normal financial
18 principles to Newfoundland and Labrador Hydro, and
19 really, you know, in front of the Board here in the ... look at
20 the Electrical Power Control Act, and if you want the
21 legislative guidance of the province which must guide the
22 Board and all of us, and a couple of times already at this
23 hearing you've pointed out the requirements of legislation,
24 that we're to, generally speaking, if you look at the
25 Electrical Power Control Act, to recover the cost of service
26 provided and the margin of profit sufficient to achieve and
27 maintain a sound financial position and credit rating in the
28 financial markets of the world ... now that's expressed in the
29 legislation of Newfoundland and Labrador, governing
30 Newfoundland and Labrador Hydro to the extent that you
31 would like to engage in a question of public policy, should
32 the public entity make a profit or not make a profit, I think
33 that the legislation has already declared what the public
34 policy of Newfoundland is, it's clearly expressed, and you
35 would be one that would be the first to respect that clear
36 legislative definition.

37 MR. HUTCHINGS: And Newfoundland and Labrador
38 Hydro has a sound credit rating in the financial markets of
39 the world?

40 MR. WELLS: At the moment we have a sound credit rating
41 in the financial markets of the world in part because our
42 debt is guaranteed by the Provincial Government.

43 MR. HUTCHINGS: Yes, and we pay for that.

44 MR. WELLS: Yes, and believe me, from the perspective of
45 your clients, it's not a bad deal, heh. One percent that
46 gives us at least a hundred basis points on our bargaining.

47 MR. HUTCHINGS: I understand and I don't think anyone,
48 I don't think Newfoundland Power, and I'm not sure about
49 the position of anyone else, but I don't think anyone is
50 actually questioning the level of the guarantee fee in this
51 hearing. Some may quibble with its calculation but in terms

52 of the one percent, I haven't heard anyone raise a problem
53 about that, but in terms of getting back to the legislation as
54 you suggest we do, the legislative direction is to achieve
55 and maintain a sound credit rating in the financial markets
56 of the world, and we have that in the current situation.

57 MR. WELLS: Well, yes, the reports that we get from the
58 rating agencies are ... we haven't had a really negative
59 report.

60 MR. HUTCHINGS: Uh hum, no, and it's been ever thus,
61 certainly go back to the time that this Board rather
62 indirectly began regulating Hydro, and it approved interest
63 coverages and as low as 1.03 and we maintained a certain
64 sound financial credit rating in the markets of the world,
65 correct?

66 MR. WELLS: Yes, and that would relate to the guarantee
67 and the level of Hydro's debt, and the perceived ability of
68 the utility to make a return on its operations.

69 MR. HUTCHINGS: Uh hum, yeah, but the point you raised
70 about opportunity cost is one that I had noted as well, and
71 that makes the debate interesting, I would suggest to you,
72 because what is the opportunity cost for government to
73 invest in Hydro? What opportunities is government
74 passing up by not putting its money in Hydro? If it doesn't
75 put its money in Hydro, unless it decides apparently to
76 invest in the Newfoundland Liquor Corporation, it doesn't
77 have any other profit-producing companies to invest in.

78 MR. WELLS: But that would be up to government,
79 wouldn't it? I mean it is, what I suggest ...

80 MR. HUTCHINGS: The opportunity cost is what they're
81 giving up, you see, and if you invest in a school or a
82 hospital or a road, you're not going to get a return.

83 MR. WELLS: And it's giving it up on behalf of who? The
84 taxpayers of the government and the issue is, there's two
85 segments to this that you might want to consider, because
86 the debate we're having today, while interesting, is really,
87 it's already predetermined by the legislation that we should
88 have a profit.

89 MR. HUTCHINGS: I don't think you should assume that
90 but carry on.

91 MR. WELLS: Okay, the taxpayers should not in theory be
92 subsidizing ratepayers because while the two are much the
93 same, they are not always the same, and take the instance
94 of the two taxpayers making the same annual income with
95 the same deductions and the same tax rate, but one has oil
96 fired space heating and one has electric, so they're not the
97 same. You don't have the returns the same. So in theory
98 we should have a situation where if, even though it's a
99 government-owned utility, the people that are funding that
100 utility, the taxpayers, should have an appropriate return on

1 their equity. Now this is not me speaking personally. This
2 is the generally accepted theory that is applied throughout
3 North America, and let's just define it to that extent, in
4 trying to deal with investor-owned, state-owned, or
5 government-owned utilities, and all I can say to you is that
6 there is a pervasive (sic) amount, persuasive amount of
7 evidence of people who say that it is inappropriate and
8 wrong for regulatory authorities not to recognize that fact
9 and provide for that, that the return on the capital deployed
10 should be recognized appropriately, and I have here, and I
11 didn't mean to file it, but it's just an article. Hydro One
12 should pay market rates for its capital, and there's an
13 author, Andrew Connasty (*phonetic*), an economist with
14 the New Hampshire Public Utilities Commission who has
15 done such and such and various degrees and such and
16 such, and he talks about fair regulatory treatment with
17 respect to Hydro One and in the eventual sale of the utility
18 over the time you'd expect the taxpayers to see a fair return.
19 By accepting a lower return on common equity than is
20 available on investments in other similar assets, taxpayers
21 are providing a subsidy to themselves through lower
22 electricity rates. In essence they are robbing Peter as
23 taxpayer, to pay Peter as ratepayer, and of course, as
24 ratepayers, they're not all equal. I'm just saying that ... and
25 I didn't know you were going to ask me this, I just happen
26 to carry this kind of stuff around ... (*laughter*)

27 MR. HUTCHINGS: I am only surprised because you don't
28 have 20 copies of it, but I'm sure we'll have those by the
29 end of the day. I would, Mr. Chairman, like to get a copy of
30 Mr. Wells' ...

31 MR. WELLS: I don't want to alarm Ms. Greene more than
32 ... she's not sure what I carry around in the run of a day. It
33 was just some ...

34 MS. GREENE, Q.C.: I'm going to check your briefcase.

35 MR. HUTCHINGS: No, I presume, Mr. Chairman, that we
36 can get copies of that for our use.

37 MS. GREENE, Q.C.: Yes, that's no problem. I had not been
38 aware that Mr. Wells was going to refer to that at all in his
39 testimony.

40 MR. NOSEWORTHY, CHAIRPERSON: Given that he has
41 I think ...

42 MS. GREENE, Q.C.: We'll provided copies, yes, certainly.

43 MR. NOSEWORTHY, CHAIRPERSON: Thank you.

44 MR. WELLS: And so help me, I can assure the Board and
45 counsel that when I walked in here this afternoon, I had no
46 intention of referring to it either.

47 MR. HUTCHINGS: But your answer leads into, I guess,
48 where you would perhaps thought I was going initially with
49 this line of questioning and that, of course, is the

50 comparison between where Hydro One gets its equity and
51 where Newfoundland Hydro gets its equity, and I think
52 from the answer that's been provided to IC-211, it's clear
53 that the equity, so called, that's in Hydro at the present
54 time, did not come from government, is that correct?

55 MR. WELLS: The means to secure that equity came
56 directly, specifically and by one reason only, and that is the
57 government moved to create the corporation.

58 MR. HUTCHINGS: What are you referring to by the means
59 to create the equity?

60 MR. WELLS: Well otherwise there was no entity as Hydro
61 ... for simplification, you didn't have a company and they
62 created the company and gave it the ability to go borrow
63 the money that started the process of building the system
64 that created the assets, that created the revenue, that
65 created the equity, and then ... because it wasn't a
66 collection of people sitting around a circle and suddenly
67 equity appeared. It was the backing of government and the
68 capability of government to back the effort of the
69 individuals in this new entity called Hydro that resulted in
70 over time the creation of these retained earnings and
71 equity. Now the issue before the Board is consistent with
72 the legislation, what should be an appropriate return on
73 equity to ratepayers, or to the taxpayers ... I'm sorry, to
74 taxpayers, because you can't have the returns, and that
75 article refers to that. It's very difficult to be even handed in
76 the distribution of the benefit to ratepayers because all
77 ratepayers are not the same, and therefore, the money
78 returned, you know ... otherwise you're going to distort the
79 financial entity, you know, the finances of the entity that's
80 providing the service, and there is a certain cost of capital
81 and it should be recognized, and there's a certain capital
82 structure that's required and it should be recognized.

83 MR. HUTCHINGS: Okay, can I ask you, Mr. Wells, to turn,
84 and I think you'll have to turn to the hard copy of IC-211.
85 I don't believe the attachments to that were on the system.
86 Do you have that reply?

87 MR. WELLS: This is IC-211, 1 of 2, is it?

88 MR. HUTCHINGS: Yes, and ...

89 MR. WELLS: What consideration if any?

90 MR. HUTCHINGS: Right.

91 MR. WELLS: Yes.

92 MR. HUTCHINGS: That's the one. Now there are two
93 attachments to that reply. The second one is what I believe
94 to be the final financial statements, set of financial
95 statements for Newfoundland and Labrador Power
96 Commission before it became Newfoundland Hydro, and I
97 don't believe the pages of that are actually numbered, but
98 the fourth page in shows the statement of revenue and

1 expenses and accumulated revenue deficiency.
2 MR. WELLS: You're counting from the first page of that?
3 One, two ...
4 MR. HUTCHINGS: The first page of the second attachment
5 which is the 1973 statements from the Power Commission.
6 MR. WELLS: I think I'm there.
7 MR. HUTCHINGS: Okay, so under the heading 1973, the
8 last number in the column is the accumulated revenue
9 deficiency as of the end of the year is \$2.465 million?
10 MR. WELLS: Yes.
11 MR. HUTCHINGS: Okay, now if we go to the first
12 attachment there, we have the audited financial statements
13 of Hydro for December 31, 1975, and that conveniently
14 shows us comparative figures for 1974, and it is the fourth
15 page there that shows the statement of income and retained
16 earnings. Do you have that?
17 MR. WELLS: The 908 and ...
18 MR. HUTCHINGS: Yes.
19 MR. WELLS: Yes.
20 MR. HUTCHINGS: Actually I'm interested first of all in the
21 number just above the 908 which is retained earnings at the
22 beginning of 1974, retained earnings beginning of year,
23 \$573,000 deficit.
24 MR. WELLS: Oh, I'm sorry, '74, yes, yes.
25 MR. HUTCHINGS: Yes, that's at the beginning of '74.
26 MR. WELLS: Uh hum.
27 MR. HUTCHINGS: And then at the end of '74 there was a
28 turn around. That's when retained earnings first came into
29 being in Newfoundland and Labrador Hydro.
30 MR. WELLS: I'll accept your word. I don't know what
31 happened in '72 and '73, but ...
32 MR. HUTCHINGS: Well, '74, if you look back to the note
33 there ...
34 MR. WELLS: Well let's assume that it came in in the
35 seventies and this is as good a year as any.
36 MR. HUTCHINGS: Actually in the first, in the beginning of
37 the notes to the financial statements it says in 1974 the
38 name of the Power Commission was changed to
39 Newfoundland and Labrador Power Corporation by the Act
40 of '74 and then the Hydro Act came in '75, so this is the
41 point of transition.
42 MR. WELLS: This is the good year.
43 MR. HUTCHINGS: So up until 1974, the entity that is now
44 Hydro had no retained earnings in it, correct?

45 MR. WELLS: Yes.
46 MR. HUTCHINGS: Okay, and the retained earnings that
47 have gone in it ever since that date have been the result of
48 ratepayers paying light bills, correct?
49 MR. WELLS: That would be the source of the revenue for
50 the services provided.
51 MR. HUTCHINGS: Uh hum, and that was the only source
52 of revenue that Hydro had was its ratepayers.
53 MR. WELLS: Yes, that would be like any business.
54 General Motors sells cars, so customers provide the
55 revenue.
56 MR. HUTCHINGS: Yeah, but shareholders of General
57 Motors put money into it before it started, didn't they?
58 MR. WELLS: Yes, in Hydro's particular instance, in effect
59 the government put the ... the government stood behind
60 the debt. In other words, if you and I went to the bank and
61 said we were going to start a utility, maybe you're different
62 than me, but I don't think we would have gotten very far.
63 The issue is that the government had the capability to
64 direct individuals to take action to create the entity.
65 MR. HUTCHINGS: The government provided a debt
66 guarantee?
67 MR. WELLS: Yes, and was recognized as being able to
68 cover it.
69 MR. HUTCHINGS: And for a good number of years the
70 government didn't require any fee for that guarantee, did it?
71 MR. WELLS: Personally I'm not aware of how far back
72 when the debt guarantee came in. I'm sorry, you may be ...
73 MR. HUTCHINGS: I think it was in the mid-eighties.
74 MR. WELLS: Yes, I would have thought that, yeah.
75 MR. HUTCHINGS: I'm told 1990, but you know, certainly
76 not in the sixties or the seventies. There was no demand
77 made for a guarantee fee in the early years.
78 MR. WELLS: I'm prepared to accept that, yes.
79 MR. HUTCHINGS: Uh hum, okay, but I mean those are
80 closed transactions, if you will. The government decided
81 not to ask for a guarantee fee in those days and they didn't
82 get it, correct?
83 MR. WELLS: I assume.
84 MR. HUTCHINGS: Yes, okay, but certainly you know that
85 from the time that government asked for a guarantee fee, it
86 did get one.
87 MR. WELLS: Yes.
88 MR. HUTCHINGS: Okay, and it's being paid?

- 1 MR. WELLS: Yes.
- 2 MR. HUTCHINGS: And it's, for all intents and purposes,
3 equivalent to an arm's length transaction. Everybody's
4 agreed that it's a fair price for what we're getting.
- 5 MR. WELLS: Yes, consistent with practices right across
6 the country.
- 7 MR. HUTCHINGS: Yes, okay, so there is no equity being
8 injected into Hydro by reason of the guarantee?
- 9 MR. WELLS: No.
- 10 MR. HUTCHINGS: No, because the guarantee is paid for
11 separately, so where then is the source of the government's
12 equity in Hydro?
- 13 MR. WELLS: The retained earnings.
- 14 MR. HUTCHINGS: But those were put in by the
15 ratepayers.
- 16 MR. WELLS: See it's the revenues that ... otherwise I'm
17 going to have a discussion with my wife today. I think I
18 better talk to the owner of Belbin's. Over the years I've got
19 a pretty good equity. I've been buying groceries there for
20 years. Does that give me an equity in the business?
- 21 MR. HUTCHINGS: Where did the first dollar of retained
22 earnings ... if government had had a dollar of investment in
23 Hydro, then the return that came to Hydro could have been
24 a return on that dollar.
- 25 MR. WELLS: Yes.
- 26 MR. HUTCHINGS: And maybe it was 10,000 percent in the
27 first year.
- 28 MR. WELLS: The government borrowed its first dollar of
29 equity. It's somewhat no different than if we were to
30 proceed with the, say the construction of something as
31 large as Gull Island, and for financial purposes we would
32 have to have, say, 30 percent equity, 70 percent long-term
33 debt secured by a contract, but that's the theory
34 (inaudible). We would have to borrow that first dollar of
35 equity put in. If Newfoundland and Labrador Hydro ...
- 36 MR. HUTCHINGS: Can I interrupt you for a second? You
37 say we would have to borrow, you would say government
38 would borrow and inject it as equity into the company?
- 39 MR. WELLS: No, well let me put it this way. The way it
40 would work with the entity. Let's say, whether it's Gull
41 Island or Power Development, or Acme Corporation, the
42 fact is that we would proceed with a major major industrial
43 development in a company that owned the asset that would
44 borrow its first dollar of equity and over a 30 or 40 year
45 timeframe would pay off the debt and would have retained
46 earnings which, and paid off the debt on the equity, and
47 then would have an equity in the form of retained earnings,
48 and that's absolutely no different than what the
49 government putting up the first dollar ... there are business
50 people in Newfoundland who didn't really put 50 cents into
51 their business. They went to the bank and borrowed that
52 first few dollars to get themselves going, and they end up
53 with retained earnings and equity.
- 54 MR. HUTCHINGS: Okay, do you not recognize the
55 difference between borrowing money and investing it into
56 a company for shares, and having the company itself
57 borrow money.
- 58 MR. WELLS: With the backing of the shareholders.
- 59 MR. HUTCHINGS: If the ... yes.
- 60 MR. WELLS: Okay, you make that distinction which there
61 are some shares ... fooling around now, but I'm not sure
62 where all this is leading us but ...
- 63 MR. HUTCHINGS: Well I think the point is that in order for
64 the shareholder to have a return, it must be a return on
65 some investment, must it not?
- 66 MR. WELLS: Yes, and the investment in Hydro is the
67 degree of equity that's in the corporation now and
68 recognized in our financial records.
- 69 MR. HUTCHINGS: That was not invested by government,
70 was it?
- 71 MR. WELLS: It was the cause of the activity that produced
72 that result was because of government.
- 73 MR. HUTCHINGS: Government, well the Legislature
74 created the corporation.
- 75 MR. WELLS: Because if you ...
- 76 MR. HUTCHINGS: Do you agree with me on that?
- 77 MR. WELLS: Yes.
- 78 MR. HUTCHINGS: Okay, and that's what government did,
79 but it didn't put money in in the sense of putting equity
80 into say this is no longer my money now, this is the money
81 of another entity.
- 82 MR. WELLS: It's the money of the entity that I established
83 ... I, government, established and I have earned over a
84 period of time everything to pay off my expenses and have
85 something left over and I've paid off debt on assets which
86 all leads me to have equity in the corporation, the good will,
87 the assets, the equity on, the retained earnings.
- 88 MR. HUTCHINGS: I will agree with you that it has, that
89 equity has been created in the company.
- 90 MR. WELLS: Yes, and then you're debating who should
91 own that equity.
- 92 MR. HUTCHINGS: Exactly.

1 MR. WELLS: Well the best I can do is not ... I mean the
2 conventional view, let me suggest to you that there would
3 be no dispute, that really the equity here is the equity of
4 the government on behalf of taxpayers that backed the
5 thing. The ratepayers made no investment in
6 Newfoundland and Labrador Hydro. Ratepayers just paid
7 X cents a kilowatt hour for the electricity received, so they
8 bought a service in the marketplace and paid for it. They
9 didn't expect to get any equity or extra return on their
10 investment in paying a bill. I mean I've been paying light
11 bills to Newfoundland Power for, well a long, long time, and
12 I have never expected to get any return other than I get
13 cents per kilowatt hour service provided to me.

14 MR. HUTCHINGS: Yes, but if you bought shares in
15 Newfoundland Light and Power you would expect a return.

16 MR. WELLS: It's different. But the fact that I bought the
17 power doesn't mean I get the shares and people who
18 bought power from Hydro didn't expect any shares, they
19 didn't get any shares, and there's, you know, it's just the
20 whole thing ends there.

21 MR. NOSEWORTHY, CHAIRPERSON: Excuse me, I don't
22 like to break up this debate at this point in time but it is
23 quarter after three and I would like, as I indicated this
24 morning, finish around four o'clock in any event, so if we
25 could take a break until 3:30 and be back promptly at that,
26 we'll have another half an hour, thank you.

27 *(break)*

28 MR. KENNEDY: We're missing counsel, Chair, and the
29 witness.

30 MR. NOSEWORTHY, CHAIRPERSON: We'll just wait a
31 moment for Ms. Greene. Is she ...

32 MR. YOUNG: I thought she was right behind me.

33 MS. GREENE, Q.C.: I apologize for the delay.

34 MR. NOSEWORTHY, CHAIRPERSON: No problem.

35 MS. GREENE, Q.C.: It won't happen again.

36 MR. NOSEWORTHY, CHAIRPERSON: Okay, Mr.
37 Hutchings, if you're ready to proceed please? Again, with
38 a view to 4:00, but I don't mean to harp on that, but I ...
39 thank you.

40 MR. HUTCHINGS: No, I quite understand, Mr. Chair,
41 having said everything I said about the requirements of the
42 legislation earlier today, it's the least I can do. Mr. Wells,
43 if we can turn back for a moment to IC-211, which I think is
44 still on the display there, and just up a little bit further from
45 where we were so we can get all of paragraph D. The
46 answer here shows that the full amount of retained
47 earnings on a regulated basis being considered as equity
48 for the purpose of this application represents an

49 accumulation of amounts earned by Hydro as its net
50 income or margin previously expressed for regulatory
51 purposes as interest coverage margin from sales to
52 ratepayers. Are you aware of how that margin was
53 characterized previously by predecessors of yours
54 appearing before this Board?

55 MR. WELLS: No.

56 MR. HUTCHINGS: Okay.

57 MR. WELLS: And if I am it's certainly not in my head now.

58 MR. HUTCHINGS: Alright.

59 MR. WELLS: I just said, if I have an opportunity I might
60 apologize to you but I said that I had no knowledge about
61 the differences between the, in the cost of service
62 methodologies and it's been pointed out to me in no
63 uncertain terms that I was briefed on that by a number of
64 individuals who did the due diligence and ...

65 MR. HUTCHINGS: I won't ask what brave soul pointed
66 that out to you.

67 MR. WELLS: But that was an issue that was going to be
68 left to expert witnesses and my only consolation was they
69 told me that we were doing the right thing, and I didn't
70 pursue it further.

71 MR. HUTCHINGS: Well we will pursue it with the expert
72 witnesses in any event, Mr. Wells. I've distributed through
73 the break two extracts from previous reports of this Board.
74 I don't know that you can identify them from their, tell them
75 apart from one another by immediately looking at them.
76 The first one that I want to look at is pages number 32 and
77 33 and that's all you can tell about them from looking at the
78 page, but I'll tell you they're extracted from the report of this
79 Board to the honourable Leo D. Barry, Minister of Mines
80 and Energy, on rate proposal filed by Newfoundland and
81 Labrador Hydro on April 20th, 1981. And page 32 starts off
82 with a recitation of some evidence submitted by a Mr.
83 Young, and that is not Mr. Geoff Young, but actually Mr.
84 Victor Young who was occupying your position, Mr.
85 Wells, at that time, and this table on page 32 is intended to
86 show, I think, if you look four lines from the bottom as the
87 reinvested margin as a percentage of capital program, and
88 you can see the various percentages there through 1979
89 through to 1982 which vary from three to 12.2 percent, and
90 I refer you then to the comments on page 33, the following
91 page and this is a summary by the Board of Mr. Young's
92 evidence where he says five lines down, six lines down,
93 "The margin represents a contribution to the capital
94 program from consumers which reduces borrowing
95 requirements and the associated long-term interest costs as
96 well as enhancing Hydro's financial stability and how it is
97 perceived by the credit rating agencies. While the benefits
98 of reinvestment of the margin begin immediately, it will

1 have its greatest impact in the future, especially as regards
2 Labrador power strategy development." Would you regard
3 it as consistent with your current position that the
4 shareholder owns that equity where Mr. Young took the
5 position that the margin was in fact a contribution to the
6 capital program from consumers?

7 MR. WELLS: The best I could say and I've never seen this
8 before this moment, is that ... and I'm assuming the margin
9 here would refer to profit accumulated during a period and
10 that that profit was being reinvested in the capital program
11 of the utility, and therefore I come back to the exact same
12 issue I tried to make before that the people bought
13 electricity from the utility, the customer paid for their
14 electricity. There was a profit factor in it and that profit
15 factor which is termed as margin was reinvested in the
16 capital program referred to here. I don't think that that
17 changes the issue with respect to construing from that the
18 use of the terminology in that way, that the people who
19 purchased electricity at the time thought they were making
20 an investment that would give them in essence a share
21 holding in the company.

22 MR. HUTCHINGS: Okay, if you can refer to the second
23 extract which is pages 27 and 28, and that's extracted from
24 the report of this Board to the Honourable Ron Dawe on
25 proposals filed by Newfoundland and Labrador Hydro, on
26 March 1, 1983. The same Mr. Young in his testimony, the
27 summary of his testimony begins at the bottom of page 27,
28 and over on to page 28 you will see essentially the same
29 position being taken by Hydro at that time. The margins
30 achieved represent a direct contribution to Hydro's
31 ongoing capital program and this reduces its borrowing
32 requirements and associated long-term interest costs.
33 While the benefits of the investment to margin begin
34 immediately it will have its greatest impact later on, and so
35 on. These are, of course, Mr. Wells, are they not, the
36 margin that is being spoken of in IC-211 where the existing
37 equity is said to be an accumulation of amounts earned by
38 Hydro as its net income or margin.

39 MR. WELLS: Yes.

40 MR. HUTCHINGS: Yes, okay, and is it fair to say that your
41 predecessor defended the margin at that time by
42 characterizing it as an investment by ratepayers in Hydro?

43 MR. WELLS: See, I don't, I'm not sure ... I don't want to
44 dispute with you before ... what it appears to me is though
45 he's using margin as the profit and saying it's being
46 reinvested. The other way it could have gone to the
47 shareholder government, for argument's sake, but I think he
48 looks to be making the point that now that this new entity
49 is making a margin, we're reinvesting the margin which
50 would be a positive thing to say in terms of the
51 corporation.

52 MR. HUTCHINGS: The clear intent, I would suggest to
53 you, is to say that this margin will be applied to the benefit
54 of the ratepayers.

55 MR. WELLS: Yes, because it would have an effect on
56 reducing the costs. By reinvesting the margin earned you
57 would reduce the costs that ratepayers would have to
58 absorb in their bills and as opposed to not reinvesting the
59 margin.

60 MR. HUTCHINGS: Uh hum, but that effect will not occur
61 if the shareholder takes that money out, will it?

62 MR. WELLS: That's true, and I think if there was a sort of
63 good news/bad news here, it's pointing out that we are
64 taking our margin and reinvesting it and that would be a
65 benefit to ratepayers but I doubt if Mr. Young was making
66 a comment with respect to the shareholding and who
67 actually owns Hydro.

68 MR. HUTCHINGS: Well I think you just agreed with me
69 that the only way that the ratepayers would get the benefit
70 that Mr. Young was touting here was if this money stayed
71 in Hydro.

72 MR. WELLS: Yeah, reinvest it in more assets and in the
73 capital program and because they were using that
74 reinvested money that would reduce the borrowing
75 requirement, and the borrowing requirement could add
76 costs to rates which ratepayers would pay, so in effect it
77 was helping to build the system and reduce the, and keep
78 the rates down to ratepayers.

79 MR. HUTCHINGS: He was saying this is your money,
80 you've paid it in and we're going to keep it here so that
81 your rates will be lower in the future.

82 MR. WELLS: You're interpreting the words there by that
83 approach.

84 MR. HUTCHINGS: I'm asking you if you feel that's a fair
85 interpretation?

86 MR. WELLS: Yeah, I honestly, I might be shocked but I
87 think if you took this same argument to Mr. Young he
88 would be somewhat confounded by the approach, as am I.

89 MR. HUTCHINGS: Well we'll leave it at that point then. If
90 we can look for a moment at the Grant Thornton report of
91 2001, particularly Exhibit 1. Directing your attention toward
92 the bottom half of that exhibit, Mr. Wells, there is an
93 amount there which in quotations is entitled "regulated
94 equity".

95 MR. WELLS: Yes.

96 MR. HUTCHINGS: Okay, and that's essentially the
97 regulated retained earnings that we're talking about here,
98 isn't it?

1 MR. WELLS: That's correct.

2 MR. HUTCHINGS: Okay. And this illustrates, as well
3 though, that government does have some money in the
4 company, correct, if you look up a few lines higher?

5 MR. WELLS: You want me to get up in the CF(L)Co. lines
6 or ...

7 MR. HUTCHINGS: Yes, yeah.

8 MR. WELLS: Yes.

9 MR. HUTCHINGS: Yeah, so government has invested
10 money in the company in the sense that it put the shares in
11 CF(L)Co in the company?

12 MR. WELLS: Through Hydro.

13 MR. HUTCHINGS: Yes.

14 MR. WELLS: Yes.

15 MR. HUTCHINGS: It put them into Hydro?

16 MR. WELLS: Yes.

17 MR. HUTCHINGS: Yeah.

18 MR. WELLS: Hydro.

19 MR. HUTCHINGS: The government bought the shares of
20 CF(L)Co and put them into Hydro and took out shares of
21 Hydro in return. I think that appears from 211 as well.

22 MR. WELLS: I think that's how the transaction was
23 structured, yes.

24 MR. HUTCHINGS: Yes, so that's obviously government's
25 asset in there.

26 MR. WELLS: Yes.

27 MR. HUTCHINGS: The CF(L)Co shares, and government
28 is taking the return to that asset, correct?

29 MR. WELLS: Through Hydro.

30 MR. HUTCHINGS: Yes.

31 MR. WELLS: Subsidiary.

32 MR. HUTCHINGS: Yeah, uh hum, so in terms of
33 government's actual financial participation in the entity
34 known as Newfoundland and Labrador Hydro, it's getting
35 a return for what it has put in. It put in CF(L)Co shares and
36 it's getting out a dividend which relates to the CF(L)Co
37 income, correct?

38 MR. WELLS: It used Hydro as a vehicle when the
39 government in effect nationalized Brinco or CF(L)Co and it
40 used Hydro as a medium to, and then it set the whole thing
41 up on Hydro's books, and you know, what you're
42 describing there is true. It reflects the investment of
43 Churchill Falls and the debt that Hydro is retiring through

44 its subsidiary, the income from its subsidiary, yeah.

45 MR. HUTCHINGS: And there is no comparable investment
46 by the government related to the regulated equity, is there?

47 MR. WELLS: No, and I mean we've already clearly stated
48 in our evidence that it is an accumulation of retained
49 earnings is the equity that's represented in Hydro.

50 MR. HUTCHINGS: There's perhaps one short matter that
51 we'll be able to deal with before 4:00 Mr. Wells, but I need
52 to ask you to look at a particular document which I don't
53 believe is on the system, and that is the, it's part of the
54 response to CA-101. We have the annual report of Hydro
55 for the year 1994.

56 MR. KENNEDY: Counsel, while the witness is just digging
57 out that information, I'm wondering whether we should
58 enter these last two documents as exhibits. I don't believe
59 they're already part of the record.

60 MR. HUTCHINGS: I think you are correct in that that they
61 should be marked because there's a number of reports that
62 are on the record but I don't think these two are.

63 MR. KENNEDY: So just so I'm clear, the one that was at
64 page 32 and page 33, what specifically was that from?

65 MR. HUTCHINGS: That's from the report of the Board on
66 the rate proposals of hydro filed on April 20th, 1981, the
67 1981 report.

68 MR. KENNEDY: If no counsel has objection, we could call
69 that Consent No. 1.

70 **EXHIBIT CONSENT 1 ENTERED**

71 MR. WELLS: CA-101?

72 MR. HUTCHINGS: Yes.

73 MR. WELLS: And it's the ...

74 MR. HUTCHINGS: 1994 report, the annual reports are all
75 attached to CA-101.

76 MR. WELLS: Yes, and which one was it?

77 MR. HUTCHINGS: 1994.

78 MR. WELLS: Okay.

79 MR. HUTCHINGS: Okay, sorry, Mr. Kennedy.

80 MR. KENNEDY: No problem, and the second document,
81 page 27 and 28, that ...

82 MR. HUTCHINGS: That comes from the 1983 report.

83 MR. KENNEDY: And if counsel has no objection we'll call
84 that Consent No. 2.

85 MR. HUTCHINGS: Thank you.

86 **EXHIBIT CONSENT 2 ENTERED**

1 MR. HUTCHINGS: Now, Mr. Wells, I don't doubt on the
2 original the pages are numbered in this document, but
3 they're not on the photocopy that I have, but what I want
4 to get you to look at is first of all the consolidated
5 statement of income and retained earnings which is part of
6 the financial statements that are attached to the report.
7 Have you got that? Okay. Before we start the questioning
8 can I ask you to flip over about eight or ten pages and
9 you'll get to note number eleven. Okay, the two things
10 obviously relate to one another. On the consolidated
11 statement of income and retained earnings, under expenses
12 there is a note, or there is an item marked "other" for \$4.3
13 million, and the reference is to note 11.

14 MR. WELLS: Yes, as an expense.

15 MR. HUTCHINGS: Yes.

16 MR. WELLS: Yes.

17 MR. HUTCHINGS: And can you tell us what those other
18 expenses actually were?

19 MR. WELLS: My assumption is that these are expenses
20 that were related to the privatization of Hydro, or the
21 exercise that was undertaken to privatize Hydro and didn't
22 materialize.

23 MR. HUTCHINGS: Okay, and these were expenses
24 incurred by Hydro presumably?

25 MR. WELLS: Yes.

26 MR. HUTCHINGS: Okay, and did these expenses reduce
27 the regulated retained earnings of Hydro?

28 MR. WELLS: I really ... this is before my time, and I think
29 that others could better ... I honestly couldn't give you an
30 answer and be certain of it. I'm not sure how that was
31 treated. It was, this was the 1994 report.

32 MR. HUTCHINGS: That's right.

33 MR. WELLS: And I went there in the 1996, January 1. I'm
34 pretty sure that when it talks about the public distribution
35 of shares, if that was ... 1994 was that attempt to privatize
36 Hydro, and I think that's the, that cost sounds about right
37 as what I've heard were the figures and whether ... your
38 question is whether that was included in the regulated
39 portion or not. I really can't confirm that, but I think that
40 Mr. Osmond may be able to do that.

41 MR. HUTCHINGS: Okay, we'll pursue that with him but
42 would you agree with me that that would not necessarily
43 represent a reasonable and prudent expense for the supply
44 of power in the province?

45 MR. WELLS: It depends on ... well we don't know how it's
46 treated and then you have to look at what the benefits were
47 with respect to privatization and what would carry on

48 thereafter. I'm really not prepared to commit on that
49 without some thought.

50 MR. HUTCHINGS: Okay, well perhaps you and Mr.
51 Osmond will discuss it before he gets to the stand. We
52 may nonetheless get an answer.

53 MR. WELLS: Well the fact of whether it was or was not is
54 a legitimate question and, you know, the comment is an
55 opinion that, you know, I think we could come up with a
56 half informed opinion if not a fully one.

57 MR. HUTCHINGS: Okay, we'll leave you to that. I think
58 that might be an appropriate time to break, five minutes to
59 the good, Mr. Chairman.

60 MR. NOSEWORTHY, CHAIRPERSON: Thank you very
61 much, Mr. Hutchings. We'll adjourn until 9:30 tomorrow
62 morning, thank you very much.

63 *(hearing adjourned to September 26, 2001)*