(9:03 a.m.)
CHAIRMAN:
Q. So good morning. So we're back to Mr. Johnson, but first you have -
MS. GLYNN:
Q. Just a couple of preliminary –
CHAIRMAN:
Q. An undertaking?
MS. GLYNN:
Q. Yes. First of all I want to enter the—a new report from the Grant Thornton, the commissioners for the Board. This is dated March 28th, 2016. It's a new report based on the revised filing, and we'll enter that as Consent Number 3.
EXHIBIT ENTERED UPON HEARING AND MARKED AS CONSENT EXHIBIT NUMBER 3
MS. GLYNN:
Q. And then Ms. Greene did want to speak to an undertaking.
CHAIRMAN:
Q. Madame.
GREENE, Q.C.:
Q. Good morning. I've had discussions with counsel for Newfoundland Power and advised

that we were asking for an additional undertaking, and it was agreed that it would be placed on the record now this morning.
CHAIRMAN:
Q. Excuse me.
GREENE, Q.C.:
Q. And the undertaking is to provide the information with respect to the impact on Newfoundland Power's financial position of a gradual reduction in the equity component, and it has been agreed that that information would be provided at one percent intervals, so a reduction first to 44 percent and then 43, right down to 40 percent, and at various ROEs. (Undertaking) And the ROEs would be as provided in Exhibit JP 1, nine and a half percent, 9 percent, 8.8, 8.5 and 8.3. And it was agreed that that request for the undertaking would be placed on the record this morning and I understand that's agreeable to Newfoundland Power.
KELLY, Q.C.:
Q. It is, Mr. Chairman. We will do that. There's a bit of math involved in that, so it'll take a little bit of time, but we'll

do it as quickly as possible.
CHAIRMAN:
Q. Okay. So I guess, Mr. Johnson, we're back to you.
JOHNSON, Q.C.:
Q. Thank you. That would also, I take it, be understood to reflect the first mortgage, the first mortgage bond test or earnings test?
GREENE, Q.C.:
Q. Yes.
MR. SMITH:
A. Yes.
JOHNSON, Q.C.:
Q. Is that right?
GREENE, Q.C.:
Q. Yes, yes.
MR. GARY SMITH AND MS. JACQUELINE PERRY, CROSS-EXAMINATION BY THOMAS JOHNSON, Q.C. CONT'D
JOHNSON, Q.C.:
Q. Okay, thank you very much. Okay, good morning, Commissioners; good morning, Mr. Smith, Ms. Perry. I just want to start off this morning, a bit of a departure from where I had intended to go when I left off

yesterday. I've raised with Newfoundland Power's counsel, Mr. Kelly, this morning about a clip that appears on VOCM News this morning that was released that I've listened to and had typed the small clip from Newfoundland Power's director of Customer and Corporate Relations. It's presently on the site in which it stated publically that risks of reliability post Muskrat Falls particularly here on the Avalon Peninsula was an issue that mattered to Newfoundland Power's credit rating agencies. You're aware that I've brought this up with counsel?
MR. SMITH:
A. Yes, I am, Mr. Johnson.
JOHNSON, Q.C.:
Q. Okay, and I just want you to—I had the clip, and admittedly it appears to be a clip from a longer discussion, but that's all that was on the site, and just for everybody's benefit the clip as presented on the site says: "The uncertainty that exists with that, the uncertainty that exists with the integration and the engineering and the

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pulling together of this entire new system that will connect us to the rest of North America as well as risks associated with reliability post Muskrat, particularly here on the Avalon Peninsula, these are all things that matter to credit rating agencies, and at the end of the day have a potential to impact us negatively." And have you had an opportunity to actually listen to the clip on the radio that I referred to on the website, Mr. Smith or Ms. Perry?

MR. SMITH:
A. I haven't heard it on the radio, but I certainly have what you've just read here in front of me.

JOHNSON, Q.C.:
Q. Okay. And I wonder if you would have your people just check what's on the VOCM, and just to be able to come back and confirm to us that that's accurate transcription of what was said? (request) Is that fine?

KELLY, Q.C.:
Q. We take it that Mr. Johnson has transcribed it accurately. We'll check, but we'll take

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that as a –

JOHNSON, Q.C.:
Q. Okay. Well thank you very much. Now Mr. –

CHAIRMAN:
Q. They couldn't possibly make a mistake, VOCM.

MS. PERRY:
A. No.

MR. SMITH:
A. No.

KELLY, Q.C.:
Q. No, nor Mr. Johnson in transcribing it.

JOHNSON, Q.C.:
Q. Well I don't think I did, but just to confirm. Mr. Smith and Ms. Perry, we've read the March or the February 5th, 2016 credit opinion from Moody's on Newfoundland Power, and Moody's doesn't mention a word about post Muskrat Falls reliability in that report. Can you confirm that for the record?

MS. PERRY:
A. Yes, I can confirm they didn't specifically point to post Muskrat Falls reliability in the report.

JOHNSON, Q.C.:

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Q. Right, and similarly the DBRS opinion of August 21st, 2015 which is entered into evidence in this proceeding, I think you'll confirm that DBRS similarly doesn't say a word about post Muskrat Falls reliability, do they?

MS. PERRY:
A. No, I can confirm that it's not in the report. What I would say, Mr. Chair, is that to say that the credit rating agencies aren't concerned about reliability of the new system would be flawed. I go back to Dark NL. They were—Moody's was one of the first parties to actually call me and to actually ask how we're actually addressing the costs that are associated with the reliability issues that we were having. So while it's not in the report, they're concerned with reliability, because reliability can actually bring additional costs to the system.

JOHNSON, Q.C.:
Q. Okay, but no mention in any of the formal reports that they've provided to the Board and that you're relying upon in this

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application?

MS. PERRY:
A. They did not specifically mention it in the report, no.

JOHNSON, Q.C.:
Q. That's right, okay. And for that matter, have they expressed in writing to you anywhere else about a concern regarding integration and engineering holding together the entire system of post Muskrat Falls reliability?

MS. PERRY:
A. No, I don't believe there's anything in writing. I mean we –

JOHNSON, Q.C.:
Q. Right, then from either of them.

MS. PERRY:
A. We provide updates to Moody's and DBRS.

JOHNSON, Q.C.:
Q. Okay.

MS. PERRY:
A. But nothing formally from them in writing, no.

JOHNSON, Q.C.:
Q. Okay.

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MR. SMITH:
A. Can I just add for a minute –
JOHNSON, Q.C.:
Q. Yes.
MR. SMITH:
A. You know one of the things I think Moody's are indicating is that the price is going to go up. And I think by the price going up that's one of the reasons they're concerned. And in terms of the connection to reliability and the price going up, I mean the things that will be discussed before the Board later this year in the post Muskrat Falls reliability hearing will look at some of those issues, and as Ms. Perry has indicated, the—when we have situations such as Dark NL and the power goes down, there are significant costs into our business. And when we look forward to Muskrat Falls and the interconnection and what the potential reliability issues are, I mean they are significant issues, and they can bring significant costs with them. Just as an example, for instance, you know we know when Holyrood is decommissioned, we'll be

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taking 500 megawatts of generation off the island system. And when you do that, the island system will then at that time have about 1500 megawatts of generation on island. That's what we would have today. And that 1500 megawatts assumes every single machine can work at its full capacity which typically doesn't occur. So 1500 megawatts would be the maximum that's on island, and then as Hydro has indicated in their Muskrat Falls information, there's a possibility of the DC line going down for as much as two weeks, and when that occurs we have to rely on the backup from Nova Scotia. And we know that the backup from Nova Scotia is good for 300 megawatts. So you take the 1500 megawatts that will be on island which is very best case, you add 300 megawatts from Nova Scotia, you get 1800 megawatts of capacity for our customers. The on-island load today is 1750, and that load continues to increase. So there's a strong indication there that when that situation happens, and we lose the DC line to Labrador, we just won't have enough generation to service our

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customers. That's an indication from my point of view that we need to buy generation for the island. That will increase prices even further. So that's an example of how prices could go up in the future and the type of thing that the bond rating agencies would be concerned about.
JOHNSON, Q.C.:
Q. Okay, but nothing that they have put in writing to Newfoundland Power or have expressed in formal credit opinions that are exhibits in this proceeding?
MR. SMITH:
A. Other than that they've indicated by the price going up they've expressed concern about that.
JOHNSON, Q.C.:
Q. Okay. Now Ms. Perry, as chief financial officer of Newfoundland Power, do you report to someone at Fortis Inc.?
MS. PERRY:
A. No, I do not.
JOHNSON, Q.C.:
Q. And how about you, Mr. Smith?
MR. SMITH:

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A. Could you repeat the question, please?
JOHNSON, Q.C.:
Q. Do you report to someone at Fortis?
MR. SMITH:
A. No, I do not.
JOHNSON, Q.C.:
Q. Okay. Are reports submitted to Fortis on a regular basis?
MR. SMITH:
A. Which type of report? We send financial information to Fortis.
JOHNSON, Q.C.:
Q. Okay, so you're consulted when Fortis Inc. puts together its annual report and other information for its investors?
MS. PERRY:
A. So yes, we have to provide our financial statements and our public reporting disclosure documents like the Management Discussion and Analysis document to Fortis, and then they will choose from our disclosures what they—what's material to them and what they will include in their disclosures.
JOHNSON, Q.C.:

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Q. Okay. Can you turn, Ms. Perry, to page 92 of Dr. Laurence Booth's evidence that's file with the Board? Towards the bottom, Samantha, please. Okay, do you have that? Now Dr. Booth refers to the Fortis 2014 Annual Report, page 36 of that report, and he refers to the capital structure and says, "The corporation's," being Fortis Inc.'s, "principal businesses of regulated electric and gas distribution require ongoing access to capital to enable the utilities to fund maintenance and expansion of infrastructure. Fortis raises debt at the subsidiary level to ensure regulatory transparency, tax efficiency and financial"—"financing flexibility. Fortis generally finances a significant portion of acquisitions at the corporate level with proceeds from common share, preference share and long-term debt offerings. To help ensure access to capital the corporation targets a consolidated long-term capital structure containing approximately 45 percent equity including preference shares and 55 percent debt as well as investment grade ratings. Each of

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the corporation's regulated utilities maintain its own capital structure in line with the deemed capital structure reflected in each of the utility's customer rates." Now then we go down. We see the consolidated capital structure below that for Fortis, presented in the following table. And we see shareholders, common shareholders equity as at December 31st, 2014 at 34.4 percent, preference shares at 9.1 percent, and then total debt and capital lease and finance obligations, net of cash at 56 and a half percent. So Ms. Perry, you would be aware that Fortis Inc. has a target capital structure of about 30 percent common shares and 10 percent preferred shares or around there, would that be your understanding?

MS. PERRY:

A. That's where they are based on their financial disclosures, yes.

JOHNSON, Q.C.:

Q. Okay. Now when we look at Fortis Inc. it's a holding company rather than operating company, right?

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MS. PERRY:

A. That is correct, yes.

JOHNSON, Q.C.:

Q. Okay. And as it says, each of the regulated utilities has its own capital structure and does its own financing, correct?

MS. PERRY:

A. Yes, that is correct.

JOHNSON, Q.C.:

Q. Okay. And Newfoundland Power I understand is ring-fenced from Fortis Inc., is that your understanding?

MS. PERRY:

A. Yes, we have been ring-fenced from Fortis. We're a separate entity, yes.

JOHNSON, Q.C.:

Q. Okay. Can you explain for the record what ring-fencing means in this context?

MS. PERRY:

A. So I would describe ring-fencing as setting the utility up as a stand-alone entity whereby it would secure its own credit ratings based on its own financial profile and strength, and issue its own debt into the capital markets. And it's such that

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Fortis is—you know, the actions of Fortis or the—any credit actions in particular from Fortis would not influence that from Newfoundland Power. We're also set up from a governance perspective with our board of directors, our own management team and we're an autonomous operation.

JOHNSON, Q.C.:

Q. Okay. Now Ms. Perry, I understand that debt issued by a hold co like Fortis, even if it's senior secured debt, is subordinated to the debt of the op co, subordinated to debt of Newfoundland Power. Would that be your understanding?

MS. PERRY:

A. I'm not sure I understand the question.

JOHNSON, Q.C.:

Q. Okay. Well let's put it this way, my—I'm told that the—this debt issued by a holding company like Fortis is subordinated to the debt of the operating utility which meant that—which would mean that in the event of a winding down or liquidation of the business, all of the operating company obligations would have to be settled first. And the—

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leaving the hold co to collect any residual that would be used to settle any outstanding hold co obligations. And Dr. Booth can talk to this far more eloquently than I can, but I wanted to have to chance to put this to you.

MS. PERRY:

A. Well I'll explain it I guess in how I understand it. In the event of I guess some credit action or bankruptcy or receivership with Fortis that would result in obviously a proceeding with Fortis but they do not have the ability to reach down and touch the assets of Newfoundland Power. Yes, we may get caught up into the proceeding that we may result in new owners, but they cannot come down and touch the assets and use those assets for their obligations Those assets are there for the provision of service for the customers of Newfoundland and Fortis doesn't have the ability to reach in and touch those assets.

JOHNSON, Q.C.:

Q. I understand that this arrangement is called structural subordination and results in the

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senior holding company debt being rated one to two notches below the senior operating company debt. Would that be—do you have an understanding of that?

MS. PERRY:

A. No, I probably shouldn't comment on that. I'm not -

JOHNSON, Q.C.:

Q. You don't –

MS. PERRY:

A. I haven't had a look at how they rate against each other.

JOHNSON, Q.C.:

Q. Okay, fair enough. Okay. Do you have any judgment as to whether the debt of a holding company like Fortis Inc. would be regarded as riskier than the debt of an operating company?

MS. PERRY:

A. No, I don't make that assessment either.

JOHNSON, Q.C.:

Q. Okay. Can't tell us, okay. Now could you turn to page 95 of Dr. Booth's evidence? And at—starting at line 5 he refers again to the 2014 Annual Fortis Report which states

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in the MDNA that, "As of December 31st, 2014 the corporation's credit ratings were as follows: Standard and Poors A minus stable, long-term corporate and unsecured debt credit rating; and DBRS A low, stable unsecured debt credit rating," and it goes on to note how, "The above-noted credit ratings reflect the corporation's low business risk profile and diversity of its operations, the stand-alone nature and financial separation of each of the regulated subsidiaries of Fortis and management's commitment to maintaining low levels of debt at the holding company level. In October 2014 the following completion of equity financing associated with the acquisition of UNS Energy, S & P confirmed the corporation's credit rating and revise its outlook to stable." Now the—and you'll see in the—he presents from further down at line 8, he prevents—presents the 2015 third quarter presentation of Fortis in his reports, and it refers to "ample liquidity and strong credit ratings." Do you see that?

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MS. PERRY:

A. Yes, I see that.

JOHNSON, Q.C.:

Q. Okay. And now if we go back to page 94 of Dr. Booth's report, he has a section there where we have the utility credit ratings underneath Fortis, let's say the operating credit ratings, okay? And we see there, and this is from lines 4 to 5 essentially on that page.

MS. PERRY:

A. Yes, I see it.

JOHNSON, Q.C.:

A. We see there that Newfoundland Power with an A rating from DBRS and would be a higher rating than Fortis would enjoy. Is that right?

MS. PERRY:

A. So Fortis' rating from DBRS is A low, stable. Yes.

JOHNSON, Q.C.:

Q. A low, okay. And Fortis, it says that it's a strong rating. And then Dr. Booth has an A2 rating for Newfoundland Power from Moody's, and would that be considered, and

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presumably he's talking there about the rating on their—on Newfoundland Power's secured debt, is that right?

MS. PERRY:
A. Yes, this is the double notch from our BAA1 rating.

JOHNSON, Q.C.:
Q. Right.

MS. PERRY:
A. Provided by Moody's.

JOHNSON, Q.C.:
Q. Right.

MS. PERRY:
A. Because of the security with the debt.

JOHNSON, Q.C.:
Q. Right, and would it be your understanding that A2 rating would be considered higher than the Standard and Poors A minus rating?

MS. PERRY:
A. They're both an A rating. I haven't done a comparison of the grids between S & P and Moody's, but –

JOHNSON, Q.C.:
Q. Okay. Now if we just go back over to page 95, I take it you would not take any

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exception to Fortis saying in its materials and its MDNA discussion that it enjoys strong credit ratings? Right?

MS. PERRY:
A. No, I don't take exception to what Fortis discloses, no.

JOHNSON, Q.C.:
Q. Right. So obviously you would accept that a DBRS low rating for Fortis would be a strong rating and S & P A minus rating would be a strong rating, right?

MS. PERRY:
A. I would confirm that they are an A rating from Standard and Poors and DBRS, yes.

JOHNSON, Q.C.:
Q. And they're strong?

MS. PERRY:
A. They're an A credit rating, yes. They're an investment grade A credit rating.

JOHNSON, Q.C.:
Q. Okay. And they're strong?

MS. PERRY:
A. I don't disagree. I mean –

JOHNSON, Q.C.:
Q. Okay.

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MS. PERRY:
A. An A credit rating we say is a strong rating.

JOHNSON, Q.C.:
Q. Okay. Now can we just look back onto page 94 for a moment? And is there any subsidiary of Fortis there that would have a higher rating than what DBRS gives to Newfoundland Power?

MS. PERRY:
A. So when I look down under the DBRS column it looks as if FortisBC Gas is at an A which is similar to Newfoundland Power's A.

JOHNSON, Q.C.:
Q. Okay. FortisBC Electric and FortisAlberta would both below Newfoundland Power, correct?

MS. PERRY:
A. Yes, they're A low.

JOHNSON, Q.C.:
Q. Okay. Now could we turn to page 93 of Dr. Booth's evidence where he has set out there the—under the topic "Regulatory Overview," I guess he took that from a quarter—a third quarter report from 2015 from Fortis by the

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looks of things, where he has the allowed ROEs and common equity ratios for UNS Energy, Central Hudson, FortisBC, FortisAlberta, Newfoundland Power. And you—have you had a chance to—or take a chance if you would to look at the equity in the capital column and the 2015--allowed 2015 ROE column, Ms. Perry.

MS. PERRY:
A. Yes.

JOHNSON, Q.C.:
Q. Okay. Now again as we clearly see, Alberta has an 8.3 percent return on 40 percent common equity, right? We'll take that?

MS. PERRY:
A. Yes.

JOHNSON, Q.C.:
Q. Okay, okay.

MS. PERRY:
A. That's their current structure.

JOHNSON, Q.C.:
Q. Right. Now as I understand, Newfoundland Power's rate base in 2016 is forecast to be just over a billion dollars, is that correct?

MS. PERRY:
A. Yes, that's about right.
JOHNSON, Q.C.:
Q. And it's about—and just for the record I think that's at schedule 3, so your revised application, okay? And do you regard Newfoundland Power, Ms. Perry, as a small utility?
MS. PERRY:
A. Yes, I do. When we—when you compare the size of Newfoundland Power even to someone like a FortisAlberta, they are bigger than Newfoundland Power.
JOHNSON, Q.C.:
Q. Okay. Could you—could I ask you to turn to CANP 169, attachment A? And this document is the Alberta Utilities Commission March 23rd, 2015 decision on the--on 2013 generic cost of capital. I think we've made some reference to this decision already. And this is on the record, and could you turn please to page 94 of 113? I think it's page 94 of 113. There we go. Okay, if you could just look at table 7, okay? In this table which is titled "Parameters by Utility" and

it says in brackets "excludes the smallest utilities," we see listing of 1, 2, 3, 4, 5, 6, 7, 8, 9, 10, something like 11 utilities in Alberta: ATCO Distribution, Fortis, ENMAX, EPCOR, AltaLink, ATCO Transmission; ENMAX, and the list goes on. And you see the invested capital for each of these utilities, Ms. Perry?
MS. PERRY:
A. Yes, I see it.
JOHNSON, Q.C.:
Q. Right. And they range from a low of 195 million in the case of AltaGas to ATCO Transmission at 3.6 million, and you see a-- or 3.6 billion, I'm sorry. And you see a range there, and just looking at the range that we see there, Ms. Perry, would Newfoundland Power—it looks to be—would look to fit in the middle of that pack, would they not?
MS. PERRY:
A. So Mr. Johnson, you're asking in comparison to the utilities just in Alberta of all-- with this –
JOHNSON, Q.C.:

Q. Yes, we're trying to get a sense –
MS. PERRY:
A. With this group?
JOHNSON, Q.C.:
Q. We're trying to get a sense of the size of utility parameter, and I see both utilities here that are smaller than Newfoundland Power, and I see utilities here that are larger than Newfoundland Power. So Newfoundland Power by size wouldn't look out of place on this chart, would it?
MS. PERRY:
A. If you're comparing to this, Newfoundland Power is about a billion. When we—when I compare I look at Newfoundland Power relative to other investor-owned utilities of which FortisAlberta is one.
JOHNSON, Q.C.:
Q. Yes.
MS. PERRY:
A. And as you can see, the investor capital there for FortisAlberta is more north of two billion.
JOHNSON, Q.C.:
Q. Yes, but how about ATCO? Is that investor

owned?
MS. PERRY:
A. Yes.
(9:30 a.m.)
JOHNSON, Q.C.:
Q. ATCO Pipelines is 868 million. In any event, Ms. Perry, if we could just turn to page 104 of 113. Now we're looking at Section 8.6 of the Alberta Board's report which is titled "Summary of Equity Ratio Findings," and they say, "Given all of the above findings, the equity ratios awarded to each of the affected utilities are summarized in the following table." And then table 10, they give the equity ratio findings and you see they show in the left-hand column the "last approved" and then what's been approved in 2013 to 2015. And we see a range in the electric and gas transmission of 36 to 37 and then the electric and gas distribution between 38, a 40, a 40, a 38, a 40, and a 42 for AltaGas which would be the very small utility that I showed you a few moments ago, right?
MS. PERRY:

A. Yes, that is correct.

JOHNSON, Q.C.:

Q. Okay, yes. Now are you—I take it that you would have been aware of this Alberta Utilities Commission decision because it affected an affiliate's cost to capital in Alberta and just in 2015, would that be fair?

MS. PERRY:

A. Yes, I was aware that the capital structure was reduced. Yes.

JOHNSON, Q.C.:

Q. Right, and aware of this decision? You would have read it?

MS. PERRY:

A. Pardon? What was the question?

JOHNSON, Q.C.:

Q. You would have read the decision I take it?

MS. PERRY:

A. I didn't read the full decision, no.

JOHNSON, Q.C.:

Q. Okay. So are you aware that the Alberta Utilities Commission allows an additional two percent on the common equity ratio for those utilities that pay no income tax, such

as ENMAX which I understand is owned by the City of Calgary and as well EPCOR? Were you aware of that?

MS. PERRY:

A. No, I'm—I haven't done a deep review of the structure in Alberta.

JOHNSON, Q.C.:

Q. Okay. Regardless I guess of the size of the utility you don't see any utility there that has anything close to a 45 percent common equity ratio, do you?

MS. PERRY:

A. Certainly not on this chart that you're showing me.

JOHNSON, Q.C.:

Q. Right.

MS. PERRY:

A. But also it includes a bunch of companies that are different from Newfoundland Power, and the ones that we've compared to again are the investor-owned electric utilities in Canada.

JOHNSON, Q.C.:

Q. Yes. Including Nova Scotia Power which is a vertically integrated company which I

understand has in excess of 800 megawatts of generation, is that right?

MS. PERRY:

A. Yes, that is correct.

JOHNSON, Q.C.:

Q. Right. Now do you think that the Alberta Utilities Commission takes into account the size of the utility in determining its capital structure?

MS. PERRY:

A. Again, Mr. Chair, I haven't gone through the decision of the AUC, so I'm not sure of all their considerations in their capital structure deliberation.

JOHNSON, Q.C.:

Q. Okay. Finally, Ms. Perry, if you could turn to page 97 of 113, and table 8 and table 9 is what I'm referring to here now, and I understand it the Alberta Utilities Commission went through an exercise, and table 8 they show the credit metrics compared to equity ratios and a Commission analysis. So in table 8 they show EBIT coverage and cash-flow-to-debt percentage, and these are the types of metrics I

understand that DBRS uses, is that correct?

MS. PERRY:

A. Yeah, I know which ones DBRS used for us which is EBIT interest coverage.

JOHNSON, Q.C.:

Q. Right.

MS. PERRY:

A. And cash-flow-to-debt ratio.

JOHNSON, Q.C.:

Q. Right, yes. And then in table 9, they set out in their decision minimum equity ratios to achieve target credit metrics, and are you aware that the Alberta Utilities Commission in setting capital structure in part targets an A bond rating? Are you aware of that?

MS. PERRY:

A. No, again I haven't been through that full decision in detail.

JOHNSON, Q.C.:

Q. Okay. Anyway, on table 9 they provide the minimum equity ratios to achieve target credit metrics, and if you compare the target credit metrics from their decision in 2011, to update it to now, and you see that for the EBIT coverage or 2 EBIT coverage, they've reduced the equity ratio from 37 percent common equity to 33. Do you see that?

MS. PERRY:
A. yes, I see that on table 9.

JOHNSON, Q.C.:
Q. Okay. And the same—and they made also similar—a reduction from 35 to 33 for—what's that? FFO debt coverage—is that—or the FFO coverage, what would that be?

MS. PERRY:
A. That's cash-flow-to-debt coverage, yes.

JOHNSON, Q.C.:
Q. Right, right. And similarly, they reduced the bottom number from 30 to 38 which was in the decision of 2011 to 34 to 43 in the updated. Now I just want to refer you, Ms. Perry, to what then the Board then says at paragraphs 458 to 460 458. And I'll just read this. "The above analysis indicates that the minimum equity ratio to achieve the targeted EBIT ratio of 2 has decreased by four percentage points"—"point and the minimum equity ratio to achieve the targeted

FFO coverage of 3 has decreased by two percentage points. In contrast, the minimum equity ratio to achieve the lower end of the range for the," cash-flow-to-debt or "the FFO to debt ratio has increased by four percentage points." And then they go on to say, "In Decision 2011-474 the Commission awarded an equity ratio of 39 per cent to distribution companies prior to company-specific adjustments. In that decision, the Commission considered this value to be a representative equity ratio for an average risk utility. Table 8 demonstrates that as a result of updating the parameters of the Commission's credit metric analysis in this proceeding, a decrease of the 39 per cent representative equity ratio is warranted. In addition, having considered the findings in Section 4 with respect to global and Canadian capital market conditions, there is less reason at this time to award equity ratios significantly higher than the minimums indicated by the credit metric analysis." And then, go on to paragraph 460 to observe that "In light of the above

considerations, the Commission finds that a one percentage point reduction of the 39 percent representative equity ratio approved in Decision 2011-474 is warranted. In the Commission's view the resulting 38 per cent equity ratio is sufficient to attain the targeted A-range credit rating for an average risk utility." You see that? Were you familiar with these passages before now?

MS. PERRY:
A. No, I had not read the full decision of the AUC, and I also don't understand or I'm familiar I guess with the context by which they're making their borders with respect to capital structure, because obviously as I said in my opening, when assessing a credit rating you don't just think or consider the credit metrics of the company.

JOHNSON, Q.C.:
Q. Yes.

MS. PERRY:
A. You also have to consider the context of the regulatory regime; you have to consider the ability of the utility to earn its return; the timeliness of the cost recovery; the

predictability of Board orders; what they're actually earning. So there's a bucket of stuff that the credit rating agencies would have to assess to maintain a credit rating, and the AUC reduced the capital structure citing that the metrics alone were still within the range to—for an A credit rating, but other considerations will be applied in the actual credit assessment of these Alberta utilities.

JOHNSON, Q.C.:
Q. Okay, but would you at least agree, Ms. Perry, that with the AUC that a 38 percent capital structure ratio for smaller utilities than Newfoundland Power with an allowed ROE of 8.3 percent is enough to attain the bond rating in the A range?

MS. PERRY:
A. No, I can't –

JOHNSON, Q.C.:
Q. As they say.

MS. PERRY:
A. I can't confirm and I can't agree with that because I don't know the context of their business risk environment.

JOHNSON, Q.C.:
Q. Okay. So this is not a decision I take it that you have been—you haven't read in detail and you've not been briefed on it?
MS. PERRY:
A. I understood the reduction that FortisAlberta had, but no, I have not been through the decision of the AUC.
JOHNSON, Q.C.:
Q. Okay. Ms. Perry, the—both the-- DBRS report that's been filed in this matter refers to the fact that Newfoundland Power has a 40-million-dollar series AE bond series due in 2016? Is that right?
MS. PERRY:
A. Yes, we have a bond due in 2016.
JOHNSON, Q.C.:
Q. Okay. And I understand that that series is presently at 10.9 percent?
MS. PERRY:
A. Just give me a second, Mr. Johnson. Yes, that is correct.
JOHNSON, Q.C.:
Q. That's right. And so what will be happening in 2016 with that bond series?

MS. PERRY:
A. So we will repay this particular bond. I believe it's in May of 2016.
JOHNSON, Q.C.:
Q. Okay.
MS. PERRY:
A. And then we will—we have planned to do a long-term bond issuance the latter part of this year, and a part of that will be to refinance the funds that are needed to repay this particular bond.
JOHNSON, Q.C.:
Q. Okay, so you go to the market the latter part of 2016?
MS. PERRY:
A. That is the expectation currently, yes.
JOHNSON, Q.C.:
Q. Okay. And why would you go in the latter part of 2016 if it's maturing May of 2016?
MS. PERRY:
A. So when it comes to when we're going to refinance or issue long-term bonds, so we will want to have, I'm going to say a significant enough bond issuance. It costs money to go to the markets and the process

you have to go through. So by the latter part of this year we'll have enough to issue approximately 75 million into the market. If we had to issue today, we'd have to do a much lower amount, and—or alternatively, if we had to fund 75 million today, we would be carrying cash for a significant part of the year. So we just time it with cash-flow needs, but all throughout the year we will be watching the market, and if there's a good window of opportunity that we feel we should issue into market, then we may choose to go earlier. And we've done that in the past.
JOHNSON, Q.C.:
Q. Okay. And what—so you're expecting to be able to have the new bonds issued at much, much lower rates than the 10.9 percent, right?
MS. PERRY:
A. Yes, that is correct.
JOHNSON, Q.C.:
Q. And what would be your present estimate as to the rate on that bond issue when it's made later in 2016?

MS. PERRY:
A. Sorry, can you repeat the question, Mr. Johnson?
JOHNSON, Q.C.:
Q. What would be your present estimate as to the rate that new issuance will carry later in 2016?
MS. PERRY:
A. It's approximately five percent.
(9:45 a.m.)
JOHNSON, Q.C.:
Q. Approximately five, so less than half. Can you explain, Ms. Perry—there's reference in the Moody's report at Exhibit 4 at page 3 –
MR. HAYES:
Q. Mr. Johnson, the specific reference for the –
JOHNSON, Q.C.:
Q. Oh, I'm sorry, page 3 of the Moody's report. Samantha, it's at Exhibit 4, Volume 2 of—yes, if you go to page 3 of that document. It's the next page. Okay, keep in coming down, please. Yes, it's under "Liquidity Analysis." There you go. Thank you. Do you see that, Ms. Perry?

MS. PERRY:
A. Yes, I see it.
JOHNSON, Q.C.:
Q. Okay, thank you. There's a reference here in the second paragraph under "Liquidity Analysis." "NPI's liquidity arrangements are considered adequate in the context of its relatively stable cash flow and funding requirements. In 2016 NPI plans to spend about 107 million on capital expenditures and pay dividends in amounts commensurate with maintaining the 45 percent deemed equity layer. Additionally, as of the 30th of September, 2015, NPI had 37 million in short-term debt which relates primarily to a bond maturity in May 2016." And then they—it continues on, but I just had a question about how that 37 million in short-term debt related to the bond maturity in May of 2016.
MS. PERRY:
A. So Mr. Chair, we have a short-term credit facility, a hundred million committed credit facility that we would borrow to support just the operations of Newfoundland Power. And so when that approaches that 75 million

or plus to support the operations, then we'll term out that short-term debt with long-term debt. So this 37 million is just the balance that was on that short-term debt at that time.
JOHNSON, Q.C.:
Q. I see. And so that 37 million would be now what in short-term debt?
MS. PERRY:
A. I believe we have around 40 million outstanding today.
JOHNSON, Q.C.:
Q. And then, so the amount that is going to be repaid arising out of the maturity of that long bond series is how much?
MS. PERRY:
A. What was the question, Mr. Johnson?
JOHNSON, Q.C.:
Q. How much is going to be maturing in that long series that we were talking about that's maturing in May?
MS. PERRY:
A. So about 30 million.
JOHNSON, Q.C.:
Q. Okay.

MS. PERRY:
A. Yes.
JOHNSON, Q.C.:
Q. So that's where you get this about the 75 million bond issue?
MS. PERRY:
A. Right, yeah.
JOHNSON, Q.C.:
Q. Okay. Now what's the annual debt payment on that AE series now that's in at 10.9 percent?
MS. PERRY:
A. The annual?
JOHNSON, Q.C.:
Q. Yes.
MS. PERRY:
A. It's one percent of principal is the original. We pay about--I think it's around four to five million a year in annual principal payments.
JOHNSON, Q.C.:
Q. In relation to that bond?
MS. PERRY:
A. No, in—with all of our bonds.
JOHNSON, Q.C.:

Q. Okay, I'm just—I'm interested in the payment in relation to that bond.
MS. PERRY:
A. I don't have that specific number here.
JOHNSON, Q.C.:
Q. Perhaps you could undertake to just to provide what that number is? (request)
KELLY, Q.C.:
Q. Certainly, Mr. Chairman.
JOHNSON, Q.C.:
Q. Thank you.
MS. PERRY:
A. Sure.
MS. GLYNN:
Q. Noted on the record.
JOHNSON, Q.C.:
Q. Okay. Now at Exhibit 5--Exhibit 5 of the same volume. This is Exhibit 5, First Revision, Comparative Financial Forecast 2016 to 2017. It shows the existing and proposed 2016 and existing and proposed 2017, and it shows your rate of return and credit metrics from lines 29 to 34.
MS. PERRY:
A. Can you move the screen down, Samantha?

Thank you.

JOHNSON, Q.C.:

Q. Okay.

MS. PERRY:

A. Yes.

JOHNSON, Q.C.:

Q. And just to clarify for me, does this—do these figures reflect the refinancing in 2016 of that long-term debt that's presently at 10.9 percent?

MS. PERRY:

A. Yes.

JOHNSON, Q.C.:

Q. They do?

MS. PERRY:

A. It does, yes.

JOHNSON, Q.C.:

Q. Okay. And so the—so there is an estimate built into that in terms of what that cost is going to be?

MS. PERRY:

A. Absolutely, yes.

JOHNSON, Q.C.:

Q. Okay. And could you—would you be able to provide for us what that—the actual estimate

that got built into that, to those assumptions were?

MS. PERRY:

A. Just one second, Mr. Johnson. Are you asking what the specific interest rate assumption -

JOHNSON, Q.C.:

Q. Right.

MS. PERRY:

A. Yeah, it was five percent.

JOHNSON, Q.C.:

Q. It's five, okay. That's fair enough, okay. Now I just want to go back to Newfoundland Power's rebuttal evidence. Page 7 if you would, please. At page 7, starting at line 13, you were about to describe a table R4 as providing a comparison of credit metrics for Newfoundland Power and FortisAlberta for the period of 2012 to 2014 as assessed by Moody's. And then, you've gone on to provide a copy of Moody's opinion for FortisAlberta, and then you—so we see those in front of us there from your evidence. And then you go on to the next page to state that, starting at line 1, "Over the period

of 2012 to 2014, FortisAlberta generated slightly stronger credit metrics on average than Newfoundland Power. However, both during"—"However, during the period FortisAlberta had both the lower allowed return on equity and a lower equity ratio than Newfoundland Power." And you go on to say, "The returns on equity authorized by the AUC for FortisAlberta have enabled FortisAlberta with its 40 percent equity ratio to achieve credit metrics that are comparable to those of Newfoundland Power with its 45 percent equity ratio." Now I'd just like to refer you for a moment to not Moody's credit metrics, but DBRS's for a moment, and that's a cross aid. It's the FortisBC filing, and that would be a cross aid that was sent over on the 28th of March. It would be cross aid—it's item number 1 referenced on that letter.

MS. GLYNN:

Q. That would be Information #6.

JOHNSON, Q.C.:

Q. Thank you. Now just for the benefit of the Commissioners because they're seeing this

for the first time probably, the cover letter is from FortisBC. I think there's a cover letter on that one. I don't know who it's signed by, someone on behalf of FortisBC is sending in – oh, Diane Roy, there you go. She's sending in Volume 1 of Evidence dated October 2, 2015, regarding FortisBC Energy Inc., having to do with common equity component and return on equity for 2016, and I understand that, in fact, your expert, Mr. Coyne, is representing FortisBC Energy in that matter, is that right?

MS. PERRY:

A. Yes, that is correct.

JOHNSON, Q.C.:

Q. Now if you could just turn to page 26 of this filing, or actually 25, Samantha, if you would first. At the bottom of the page at line 17 and 18, the company has indicating that Table 4, which is on the next page below compares the approved capital structure and other credit metrics of a sample of Canadian utilities with those of FEI, and if you flip over the page, so here you have it, and Table 4 is a comparative analysis of utilities credit metrics, allowed REO, and equity thickness, source DBRS research. Now the first thing I'd like to bring your attention to is do you see the metric for EBIT interest coverage for Newfoundland Power. It's down towards the middle of the page, and this is for the years 2012, 2013, and 2014, right?

MS. PERRY:
A. Yes, that is correct.

JOHNSON, Q.C.:
Q. You've had a chance to see this document and review it, Ms. Perry?

MS. PERRY:
A. Yes, I have.

JOHNSON, Q.C.:
Q. Right, okay, so Newfoundland Power is showing EBIT interest coverage of 2.74 times in 2012. Just compare that to FortisAlberta a couple lines up.

MS. PERRY:
A. On this table, Mr. Johnson?

JOHNSON, Q.C.:
Q. Yes.

MS. PERRY:
A. Yes, it says 2.34 for FortisAlberta.

JOHNSON, Q.C.:
Q. Yes, and in 2013, it's 2.95 interest coverage for Newfoundland Power. Just compare that to FortisAlberta for 2013?

MS. PERRY:
A. And it's 2.19.

JOHNSON, Q.C.:
Q. 2.19, and in 2014, Newfoundland Power is 3.10 times compared to -

MS. PERRY:
A. 2.19 for FortisAlberta.

JOHNSON, Q.C.:
Q. FortisAlberta, yes. In fact, if I look at the whole number of these companies because the top part of the chart just deals with natural gas distribution and transportation companies, and then the bottom part with the graph deals with electric distribution and transmission companies, right?

MS. PERRY:
A. Yes, that is correct.

JOHNSON, Q.C.:
Q. And I see in 2012 that Newfoundland Power's

interest coverage at 2.74 is higher than every single company there, with the exception of Hydro One, which is rated an A High by DBRS, is that right?

MS. PERRY:
A. For 2012, Mr. Johnson?

JOHNSON, Q.C.:
Q. That's right.

MS. PERRY:
A. Yes, that's what it appears there.

JOHNSON, Q.C.:
Q. Yes, and 2012, that's the year you file your GRA, so that wasn't new rates, that the existing rates prior to your filing of your GRA in the fall of 2012, correct?

MS. PERRY:
A. That is correct, yes.

JOHNSON, Q.C.:
Q. Yeah, that's when your return on equity was in the low 8s. If you'll just flip over -

MS. PERRY:
A. In 2012, our return was 8.8, which is consistent with what it is today.

(10:00 a.m.)

JOHNSON, Q.C.:

Q. Well, I think you're allowed return at that point was 8.1. Would that be right? Just look over at the column here.

MS. PERRY:
A. No, that must be an error on that sheet.

JOHNSON, Q.C.:
Q. It was a bit higher than 8.1, was it?

MS. PERRY:
A. It was 8.8 in 2012.

JOHNSON, Q.C.:
Q. That was your actual return.

MS. PERRY:
A. It was 8.38 in 2011.

JOHNSON, Q.C.:
Q. Okay, we can sort that out. Now just look at 2013, your 2.95. Can you confirm for me that you would be – you're tied with Hydro One at 2.95 EBIT interest coverage in 2013, and higher than every other utility there presented, correct?

MS. PERRY:
A. Yes, I will agree we are consistent with Hydro One in this table.

JOHNSON, Q.C.:
Q. That's right, and, in fact, at 2.95 in 2013,

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the average for electric distribution and transmission is only 2.66, and that would include Newfoundland Power's 2.95, is that right?

MS. PERRY:
A. Yes, looking at these specific utilities, yes, that's what the map is saying here. I haven't checked the map, but that's what it's saying.

JOHNSON, Q.C.:
Q. And in 2014, Newfoundland Power's EBIT interest coverage at 3.10, that again is the highest out of any of these listed utilities. Can you confirm that?

MS. PERRY:
A. Yes, I can confirm on this table, we are the highest in 2014.

JOHNSON, Q.C.:
Q. Now if you'll just go over to the right of that table for a little bit, it talks about the allowed ROE and equity thickness. Now 2012, we have a question mark about your ROE, and that's fine, but in 2013 and 2014, Newfoundland Power is listed down as 8.8 in each year, that's correct, right?

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MS. PERRY:
A. Yes, in the allowed returns.

JOHNSON, Q.C.:
Q. Okay, and you see that the average electric distribution and transmission company listed there has an average return in 2013 of 8.8, so your rate at that average, right?

MS. PERRY:
A. Based on what's in this table, yes.

JOHNSON, Q.C.:
Q. Right, and in 2014, the average ROE for these average electric distribution and transmission companies is 8.9, so you're just a touch below that allowed at 8.8, correct?

MS. PERRY:
A. Again based on this table, yes.

JOHNSON, Q.C.:
Q. And so this would bear out the observation because just look for a moment before we pass on, just look at your equity thickness, and you see Newfoundland Power is 45, 45, 45. Just look at the average electric distribution and transmission equity thickness in those columns, they're 40.5,

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40.2, and 40.2, right?

MS. PERRY:
A. Yes.

JOHNSON, Q.C.:
Q. So this would bear out the observation, I would suggest to you, that Newfoundland Power has had average allowed ROEs on above average equity thickness, which is a point that Dr. Cleary makes in his evidence. Would you agree with that?

MS. PERRY:
A. I agree that Newfoundland Power's common equity component is higher than others at 45 percent, but again I'll go back to what I said earlier that the 45 percent, which has been approved by this Board for over 20 years, is unique to Newfoundland Power maybe, but it's the result of our unique risk that we have. We are a small utility. When we do the comparisons – when I do the comparisons, we're a relatively small utility and we are in, as Mr. Smith said yesterday, we're in a low growth environment and that hasn't changed, and 45 percent certainly supports those unique risks that

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we face as a utility.

JOHNSON, Q.C.:
Q. But, I guess, going back to my question, this would seem to bear the truth of the observation that Newfoundland Power has had average allowed ROEs on above average equity thickness, which is the point that Dr. Cleary is making. Can you disagree with that based upon what we see?

MS. PERRY:
A. I disagree, in that it's – mathematically, I agree it's above the average of what's in Canada. I just think they have to put it in context that the 45 percent is what we've had for, as I said, over 20 years. It supports Newfoundland Power and it supports our credit rating that we have today. Obviously, with respect to those utilities, which I haven't done a study on, the 40 percent or somewhere about that supports their business risk that they face, but for Newfoundland Power, 45 percent supports ours.

JOHNSON, Q.C.:
Q. Can you turn to R-2 of Newfoundland Power's rebuttal evidence? That's on page 5. The

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company has set out here in Table R-2 the earnings test for 2017, and this pertains to the earning test for the first mortgage bonds proposed versus 7.5 percent ROE at 40 percent equity. Just to confirm for a moment, there's no mention here of 2016. So can we conclude from that, that in 2016 at 40 percent equity at 7.5 percent ROE, that the earnings test for the first mortgage bonds are met, or can we not?

MS. PERRY:

A. Mr. Chair, the reason we chose 2017 is because the earnings test is actually based on the year prior to the bond issuance, so if we had to display 2016, we would have had to use 2015s actual earnings. So for purposes of this rate case, that wasn't necessarily a relevant piece of information, so we chose to show what would happen if we changed it in the test year. So we chose 2017, which means we had to use 2016 forecast earnings because you have to use the year prior to calculate the earnings test under the trust deed.

JOHNSON, Q.C.:

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Q. Could you not do the same exercise in respect of 2016, so we could have visibility on that, or does that just not make sense, and if it doesn't make sense, tell me to live with it?

MS. PERRY:

A. All I'm saying, we would have to use the 2015s earnings, which would not be based on an ROE of 7.5. It would actually be based on what we actual earn in 2015, which is 8.98. So we wouldn't be actually comparing the impact of a 7.5 percent return, because we're using actual results for 2015.

JOHNSON, Q.C.:

Q. Let's put it this way, you're talking about going to the long market again in the end of 2016, towards the end of 2016, okay.

MS. PERRY:

A. Yeah.

JOHNSON, Q.C.:

Q. If you had this common equity structure at that point, 40 percent at 7.5 percent ROE, would you be able to pass the earnings test to issue those bonds in 2016?

MS. PERRY:

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A. So when we go to market at the end of 2016, we will actually apply the earnings from the year prior, which is 2015, not the 2016 forecast. We will actually use the 2015 actual results and then compare that to the total interest on our long bonds.

JOHNSON, Q.C.:

Q. Let me come at it in a slightly different way, and I apologize if I'm not getting it or obtuse, it wouldn't be the first time. Would there be any impediment in relation to your issuance of first mortgage bonds in the fall of 2016 of having 7.5 percent ROE on 40 percent common equity?

MS. PERRY:

A. While we may still pass the earnings test because it will not be based on the 7.5 and 40, it will be based on '15, so we actually may pass the earnings test. If we were at 7.5 percent ROE and 40 percent capital structure, it is possible that the impact of our bond issuance would be with respect to whether that would result in any credit action of Newfoundland Power, and if there were credit action applied to our credit

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ratings, then our issuance could actually cost more than what it otherwise would be. So while we may pass the earnings test, there may be consequences outside of just the earnings test.

JOHNSON, Q.C.:

Q. Okay. I just want to understand the point. The other thing about this Table R-2, as presented, does this make any assumptions as to whether there's any preference shares in your capital structure or is it just straightforward equity?

MS. PERRY:

A. It's 40 percent common equity.

JOHNSON, Q.C.:

Q. Okay, now talk about that first mortgage bond for a moment. Could you turn up CA-NP-016, Attachment "A". This is a picture of the famous Deed of Trust and Mortgage. I think this dates back to the 60s.

MS. PERRY:

A. It does.

JOHNSON, Q.C.:

Q. And if we could turn to the earnings test, which I think is at Section 6.2. Mr.

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Chairman, I see it says, "Newfoundland Light and Power".
CHAIRMAN:
Q. I liked the 60s, what I can remember.
JOHNSON, Q.C.:
Q. So this is Article 6, bonds in addition to initial bonds, and it says in 6.2 earnings test, "No additional bond shall be certified and delivered hereunder unless the net earnings of the company for the earnings period selected by the Directors shall have been at least two times the maximum annual interest charges on all bonds to be outstanding after the proposed issue of additional bonds". So that's the operative wording for the earnings test, is that right?
MS. PERRY:
A. Yes, that is correct.
JOHNSON, Q.C.:
Q. Okay, now we note that there is an option given to the Directors in relation to the earnings period that will be selected by them. Is that your understanding?
MS. PERRY:

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A. No. I've only ever applied - the earnings period is the year prior to the issuance.
JOHNSON, Q.C.:
Q. Okay, now could we go to the earnings period which is defined at page 6 of this instrument? See at the definition of earnings period, it says, "Earnings period means at the option of the company; (a) the last completed fiscal year of the company, or (b) a period of any 12 consecutive calendar months terminating within the 24 calendar months next preceding the certification and delivery of such additional bonds, except that; (1) if such period of 12 consecutive calendar months selected by the company in part anti-dates the formal date, any portion of the earnings period applicable to any of the predecessor companies need not immediately proceed". In any event, you'd want to be a Philadelphia lawyer probably to -
MS. PERRY:
A. Absolutely.
JOHNSON, Q.C.:
Q. Now I just want to understand. Were you aware

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that there is an option as to the selection of the earnings period?
(10:15 a.m.)
MS. PERRY:
A. What I will say is that when we go to apply the earnings period, it always ends up to be the previous calendar year. I see there's some options, but I would have to read it in the context again just to get familiar with it again. We use lawyers for when we go to do our certifications, and any time from the ten years that I've been at Newfoundland Power, the earnings period has always been the previous 12 calendar – the calendar year.
JOHNSON, Q.C.:
Q. And I understand that, but what I'm wondering is whether you were aware that there was a different earning test – an earning period that could be selected?
MS. PERRY:
A. I've had a discussion about what the earnings period is, yes.
JOHNSON, Q.C.:
Q. And what's that discussion?

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MS. PERRY:
A. Only just with the lawyers, and actually with a finance person at Newfoundland Power about what is the appropriate earnings period to use, and between us and the lawyers, we have used the previous calendar year. As I said, I would have to go back and check with legal counsel just about the formalities of this particular option.
JOHNSON, Q.C.:
Q. So would you be able to indicate to us whether in 2017 – because we saw the rebuttal evidence that said that you would fall below in Table R-2 the earnings test for first mortgage bonds at 7.5 percent ROE and 40 percent equity in 2017. Could you provide for us an answer as to what your earnings test would amount to under that scenario if you used the other option that the security instrument gives you?
MS.PERRY:
A. I can certainly look at that. I think I should provide clarity. The earnings test is simply the annual earnings of the utility over the total annual interest of your long

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bonds. So regardless of what exact period we use, if we're assuming we are going to earn 7.5 percent on the equity we have in the company, there would be very little differences between the earnings value that you're going to use because this is on a hypothetical forecast of earning 7.5 percent on 40 percent equity. So that's what this was squared to do. So we've chosen earnings of 7.5 percent equity on 40 percent over total interest, and the total interest wouldn't change regardless what period you used. So our assumptions are not changing with respect to earnings, and they are certainly not going to change with respect to debt, so I don't envision that this is going to have any material impact on the earnings test calculation that we have here.

JOHNSON, Q.C.:

Q. Well, the table that you've shown in Table R-2 assumes a particular earning period, right?

MS. PERRY:

A. But it's assuming a 7.5 percent return.

JOHNSON, Q.C.:

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Q. Right, and what I'm asking you to do is to provide this table using the other earning period that Newfoundland Power has at its option?

KELLY, Q.C.:

Q. I don't know what that would be, Mr. Chairman. My friend would have to define it because while I haven't attempted in the few minutes I've been sitting here, just looking at it on the screen, it says, "A period of any 12 months", and then there's a long (1), so my friend would have to define what other period he wants the witness to go back and do some calculation against, and then we would have to determine; (a) is that even possible, and then what the calculation is on that particular point. For the reasons the witness has explained, it seems like a useless exercise.

JOHNSON, Q.C.:

Q. Mr. Chairman, I don't know why this is complicated. The witness – this is the trust instrument that Newfoundland Power has. These are the rules under which the issuance of first mortgage bonds are

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governed, okay. The document says they have an option as to the earnings period. That option is at the selection of the Directors of Newfoundland Power. They have put this forward predicated on the use of an earnings period that they've used for the last ten years. All I'm seeking is what would be the result if the other earnings period that this document permits was run. I think that's an entirely -

CHAIRMAN:

Q. Is wrong?

JOHNSON, Q.C.:

Q. Is run.

CHAIRMAN:

Q. Oh, run.

JOHNSON, Q.C.:

Q. Yes, it's an entirely fair question because Newfoundland Power has presented to this Board that the equity ratio that Dr. Booth has put forward necessarily puts them offside their earnings test in 2017, and I pointed out to them that that's only if they use the earnings period that they've employed, however, the document speaks to

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another earnings period. I mean – I fail to see why that would not be relevant.

MS. PERRY:

A. If I could just add just a point of clarity, the purpose of calculating that earnings test was to show the impact of an earnings period having a 7.5 percent return. So even if we chose another earnings period, we're just going to assume a 7.5 percent return, so it's not going to change the earnings. We're going to assume a 7.5 percent return. We're not basing it on what we've actually earned, we're just basing it on what we're forecasting to earn at 7.5 percent.

JOHNSON, Q.C.:

Q. Well, I –

CHAIRMAN:

Q. Excuse me. So you're saying under either scenario, it's still a forecast period, is that what you're saying?

MS. PERRY:

A. This was to show the impact of if the utility were to earn 7.5 percent return, which would impact its earnings, right. Compare that to the total interest, this is

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what the earnings test would yield. So regardless of what period, if the utility actually had a 40 percent capital structure and a 7.5 percent return, this is the calculation if we had to do a debt issue in 2017.

CHAIRMAN:

Q. And the only variation would be in the forecast for the two different years, is that what you're saying?

MS. PERRY:

A. Right. So if, in fact, rate base were to change significantly within those periods, which it wouldn't, right, then the earnings of the 7.5 percent wouldn't be materially different with respect to this earnings test, not at all.

CHAIRMAN:

Q. I think I might understand that, I don't know.

MS. GLYNN:

Q. If I might interrupt here for a second.

CHAIRMAN:

Q. Oh, please interrupt.

MS. GLYNN:

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Q. And suggest that this may be an intersection between the legal counsel and the finance, and ne'er the two may meet, but maybe if we could set that aside and have some further discussion at the break between the two counsel and ourselves and see if there was some middle ground where we can meet on this, having a better look at the entire section.

JOHNSON, Q.C.:

Q. That's fine for the moment.

CHAIRMAN:

Q. I mean, the year you're using is not real numbers, they're forecast numbers, is that what you're saying?

MS. PERRY:

A. So the earnings test is based on an annual earnings number, right, which we've based it on a return on the equity that was in the company for 2016 fundamentally, and then that just compares to the total interest.

CHAIRMAN:

Q. So when you say 2016, you're using the calendar year?

MS. PERRY:

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A. Calendar year 2016.

CHAIRMAN:

Q. Okay.

MS. PERRY:

A. So even if we were to alter another 12 month period, the amount of equity in the business is not going to materially change between these 12 month periods, and we're just assuming we are earning 7.5 percent on that equity.

JOHNSON, Q.C.:

Q. But I don't -

CHAIRMAN:

Q. You can use the Julian calendar or Gregorian calendar, there's 12 days difference, does it make any difference? I don't know, I mean.

JOHNSON, Q.C.:

Q. I don't know if it's that simple because the document talks about the ability to not only use the preceding 12 month period. It also talks about the ability to use a period of any 12 consecutive calendar months, any terminating within the 24 calendar months next preceding the issuance. So the debtor would be able to

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pick a 12 month window, not necessarily the calendar year, and say look at this as our earnings period for the purpose of determining whether we meet the earnings test. Now that's not, with all due respect, and I'm not a chartered accountant, but that does not seem to me to be exactly the same thing, and as a lawyer, I would suspect that it's not the same thing because why would a document say that (a) and (b) is the same thing. It can't be.

VICE-CHAIR WHALEN:

Q. But that's if you're actually going to be going to the market?

MS. PERRY:

A. Yes.

VICE-CHAIR WHALEN:

Q. Not in a hypothetical scenario.

JOHNSON, Q.C.:

Q. Well, it's all hypothetical.

VICE-CHAIR WHALEN:

Q. Yeah, but in a hypothetical scenario, it doesn't matter which 12 month period you pick because your 7.5 percent and 40 percent is -

CHAIRMAN:

Q. Yeah, they're the fixed numbers, aren't they?
VICE-CHAIR WHALEN:
Q. Is that what I understand?
CHAIRMAN:
Q. The 7.5 is fixed, is that right?
MS. PERRY:
A. Yes.
CHAIRMAN:
Q. And the 40 percent is fixed for the purposes of the exercise, is that what you're saying? So the only variable is the start and end of your 12 month year -
JOHNSON, Q.C.:
Q. Twelve month period.
CHAIRMAN:
Q. Twelve month period.
JOHNSON, Q.C.:
Q. Yes.
CHAIRMAN:
Q. I mean, what difference does it make whether you start on January 1st or January 11th? You're still going to run it out from January 11th until January 10th the next year or December – January 1st to December 31st.

It's just – it's still a 12 month period and that's – it's the variable, I guess. I mean, how much variation would there be. Anyway -
JOHNSON, Q.C.:
Q. Mr. Chairman, I'm certainly content to go with counsel's suggestion then to come back to it as need be.
CHAIRMAN:
Q. Well, good luck with it.
JOHNSON, Q.C.:
Q. If you could turn to Table 4-11 of the company's evidence. Ms. Perry, the company indicates in Table 4-11.
MS. PERRY:
A. Excuse me, what page is that?
JOHNSON, Q.C.:
Q. It's at page 4-14. The table indicates, Ms. Perry, that Newfoundland Power's forecast return on equity in 2016, without any new rates, is 8.03 percent for 2016, and 7.3 percent for 2017, and I just want to turn next to Table 4-12, which is on the very next page.
MS. PERRY:

A. Yes.
JOHNSON, Q.C.:
Q. Where they compare – the company compares the credit metrics from 2013 to 2017, and just to confirm a couple of points for us that in relation to the 8.03 percent return on equity for 2016, that, in fact, Newfoundland Power's credit metrics actually improve in relation to cash flow interest coverage and cash flow debt coverage over 2015, and there's only a slight decrease in your pre-tax interest coverage, right?
MS. PERRY:
A. Yes, I can confirm that.
JOHNSON, Q.C.:
Q. And in 2017, at a 7.3 percent return on common equity, your cash flow interest coverage of 3.7 times is what it was in 2013, which was a GRA year, right?
MS. PERRY:
A. Yes, that is correct.
JOHNSON, Q.C.:
Q. And your 2017 cash flow debt coverage of 16.2 percent is certainly within an acceptable range according to current metric

expectations of Moody's, isn't that right?
MS. PERRY:
A. The 16.2 is within the range indicated by Moody's, yes.
JOHNSON, Q.C.:
Q. That's right, and finally the 2.1 pre-tax interest coverage for 2017, Moody's doesn't use that metrics, right?
MS. PERRY:
A. No, that's correct.
(10:30 a.m.)
JOHNSON, Q.C.:
Q. Okay. Now if we can turn to DBRS in Volume 2, Exhibit 4. I just want to go to page 2, where they talk about the rating considerations and the first one they mention in terms of the strength are the stable and supportive regulatory environment, and just for the record, DBRS states, "Newfoundland Power operates in a stable and supportive regulatory environment that is based on cost of service, COS regulation. The PUB also allows for the pass through of purchase power costs, and an RSA is in place to absorb fluctuations in

purchase power costs relating primarily to the cost of fuel oil used by NLH to generate electricity. Furthermore, the company also has a WNA", which is a weather normalization account, "to stabilize earnings during extreme weather conditions". Now, Ms. Perry, there is no reference there in this discussion of the stable and supportive regulatory environment, or any reference to Newfoundland Power's high equity component in your capital structure. Would that be fair?

MS. PERRY:

A. In this particular paragraph, there is no mention, and if you look at the second, they talk about our solid financial profile which obviously the 45 percent would be a factor, and I would note that if you go to page 4 under "Summary Outlook" in terms of what they view as an outlook for Newfoundland Power over in the second column under the 2015 summary outlook, the last point there, it says, "DBRS expects the company to continue to maintain its approved capital structure through dividend management and

debt financing". So there's an expectation there that they expect our capital structure to remain the same.

JOHNSON, Q.C.:

Q. Well, you've probably told DBRS that you expect your capital structure to remain the same, is that right?

MS. PERRY:

A. Mr. Chair, as I said earlier, I never make predictions about cost of capital and capital structures. I do advise them on factual developments within the company.

JOHNSON, Q.C.:

Q. But would you not have told them that it's your expectation that your capital structure will remain unchanged?

MS. PERRY:

A. The conversations I would have with DBRS is that we have had the capital structure for over 20 years, and that we are filing to maintain the capital structure, and, yes, we expect that we're going to maintain it based on the risk that we face today.

JOHNSON, Q.C.:

Q. Okay, that's fine, that's all I was getting

at. Now in DBRS Report again at page 1, see the second paragraph, part way down through they say, "The company currently has an allowed return on equity, ROE, of 8.8 percent and regulated capital structure of 45 percent common equity, which is comparable to its peers across Canada". Ms. Perry, Dr. Cleary's Report says that in 2015, the average common equity ratio amongst Canadian electric distributors was 39.24 percent, excluding Newfoundland Power. He says that at page 30 of his report. Do you dispute his tabulation and averaging of what the average common equity structure was?

MS. PERRY:

A. You'd have to show me the exact reference.

JOHNSON, Q.C.:

Q. Page 30 of Dr. Cleary's Report. Just keep on coming down, if we could. So in 2015 at Table 10, equity ratios, he shows Canadian electric distributors having an average equity ratio of 39.24 percent and a median equity ratio of 40 percent. Accept that?

MS. PERRY:

A. That's his math, yes, that's what it's saying.

JOHNSON, Q.C.:

Q. Ms. Perry, if DBRS finds and considers that a 45 percent common equity ratio is comparable to your peers, they would have to regard a 40 percent common equity ratio at Newfoundland Power as being even more comparable, would they not?

MS. PERRY:

A. I disagree with the conclusion that you're making, Mr. Johnson. I view what DBRS has said here – Samantha, if you could go back to the front page of the DBRS Report. That's good, thank you. So down where Mr. Johnson had read this line, "The company currently has an allowed regulated return of 8.8 and a regulated capital structure of 45 percent, which is comparable to its peers across Canada", they've included both within their statement, and so I view the comparability to its peers to mean both. The 8.8, as I've said a couple of times so far in this proceeding, is the second most in the country today, so together, I think, they've made some statement that it's comparable to its peers across Canada.

JOHNSON, Q.C.:

Q. So are you suggesting that when they say that your capital structure of 45 percent common equity is comparable to its peers across Canada, they're not referring to your common equity structure, they're referring to your return?

MS. PERRY:

A. I believe they're referring to both. Now I can't speak for DBRS, but I believe in that statement there they're actually referring to both the 8.8 and the capital structure.

JOHNSON, Q.C.:

Q. But I wouldn't have thought that you would disagree with me, that if DBRS found that, you know, 45 percent is comparable to the 40 that we've seen, and Dr. Cleary talks about, that Newfoundland Power having a 40 percent common equity structure would even be more comparable, but you're not prepared to concede that, are you?

MS. PERRY:

A. No, not at all. I believe that they are

talking about comparability with reference to both the capital structure combined with the return on the capital structure.

JOHNSON, Q.C.:

Q. Are you aware whether Newfoundland Power has said in a response to an RFI, that DBRS has found your equity structure to be comparable to other Canadian utilities?

MS. PERRY:

A. You'll have to show that to me, Mr. Johnson.

JOHNSON, Q.C.:

Q. Okay, maybe I'll take a look. My memory might be faulty, but I'll have a look. In terms of the Moody's Report of February 5 at page 3, they likewise have a section on supportive regulatory and business environment, and they start off by saying, "NPI's operations benefit from a well developed regulatory framework and business environments that we consider credit supportive. We consider the PUB's regulation of NPI to be credit supportive primarily because of a track record of reasonably timed and balanced decisions that enable NPI to generate stable and predictable cash flow

and earn its allowed ROE, which has not been directly subject to political interference. NPI has access to courts for disputes with the PUB". You see Moody's has pointed there to these factors being the primary reasons, I put to you, why they consider this to be a credit supportive regulatory environment. Do you accept that?

MS. PERRY:

A. Yes, that's exactly what I said in my opening yesterday.

JOHNSON, Q.C.:

Q. Okay. Now Moody's is not equating this Board continuing your high equity ratio to credit supportiveness, are they?

MS. PERRY:

A. Moody's points to the 45 percent as a credit strength and a credit positive, so it's a factor that they've considered in the credit rating assessment.

JOHNSON, Q.C.:

Q. Okay, but they don't equate the common equity structure being static at 45 with the regulatory support?

MS. PERRY:

A. I'm not sure I understand the question. I would view that they would look at orders of this Board, which would include decisions on the capital structure for Newfoundland Power to be a part of what they view as regulatory support for Newfoundland Power.

JOHNSON, Q.C.:

Q. Ms. Perry, page 2, they talk about factors that could lead to a downgrade, and they say, "We consider a downward revision in NPI's rating to be unlikely in the near term. However, NPI's rating would likely be downgraded if we perceived a meaningful reduction in the level of regulatory support, combined with a sustained deterioration in NPI's financial metrics such as cash flow, pre-working capital to debt, falling into the low teens". Ms. Perry, it's not any reduction in regulatory support, but a meaningful reduction. That's what your understanding is what Moody's is talking about there, is that right?

MS. PERRY:

A. Yes, Moody's indicates that it would be a meaningful reduction in regulatory support,

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but I'm not quite sure, you know, their range of meaningfulness, but that's their words, yes.

JOHNSON, Q.C.:

Q. That's right, and even this would have to be coupled with a sustained deterioration in your financial metrics. That's what they're saying, right?

MS. PERRY:

A. I'm not sure it's that specific. Depending on what the decisions are with respect to Newfoundland Power's capital structure or return, or any regulatory mechanisms that we have, I think Moody's will reserve the right to downgrade based on the whole package of what they see. They're just giving some indication that, you know, if they saw a meaningful reduction and it was also combined with a sustained deterioration, that that could lead to a downgrade, but that's not to see that's in stone with respect to the only things that could result in a downgrade, but it is an indication of what could cause a downgrade.

JOHNSON, Q.C.:

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Q. Newfoundland Power is not expecting to lose any of its deferral accounts, right?

MS. PERRY:

A. No, that is correct.

JOHNSON, Q.C.:

Q. And you're not expecting decisions from the PUB to be less timely, are you?

MS. PERRY;

A. Not the decision to be less timely, but certainly as Mr. Smith indicated earlier, which is the credit constraint that Moody's has pointed to, the significant costs that are coming with respect to our customers may, in fact, result in changes in the timing of collection of our own costs, so to say that -

JOHNSON, Q.C.:

Q. What I'm referring to, Ms. Perry, is how Moody's said that primarily they considered this to be a credit supportive regime is because of a track record of reasonably timely and balanced decisions. What I'm getting at is you're not expecting for decisions from the Board to become less timely in the future, are you?

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MS. PERRY:

A. No, I'm not expecting that, no.

JOHNSON, Q.C.:

Q. And you're not expecting decisions to be unbalanced, are you?

MS. PERRY:

A. I hope not.

JOHNSON, Q.C.:

Q. And in terms of factors that could lead to a downgrade, we note here that Moody's is not referencing Muskrat Falls as a factor that they've identified as leading to a downgrade, right?

MS. PERRY:

A. I will acknowledge that Moody's hasn't specifically put it in this paragraph, but they have clearly stated in its report that it is a constraint of our credit rating with this single biggest project, and even during this last ratings review, the biggest piece, I guess, of update that we had to provide to them was what was the latest with respect to Muskrat Falls, what are the cost estimates currently and how is it going to impact customers, and the visibility on what

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customers are going to see in rates, and we had to provide that to Moody's during this ratings assessment.

JOHNSON, Q.C.:

Q. Prior to them issuing their February report?

MS. PERRY:

A. Absolutely, yes.

JOHNSON, Q.C.:

Q. And then in their February report, they refer on page two to factors that could lead to an upgrade?

MS. PERRY:

A. Yes.

JOHNSON, Q.C.:

Q. "NPI's ratings would likely be upgraded if cash flow pre-working capital to debt is forecast to be sustained above 17. However, an upgrade of NPI's rating is unlikely without further clarity on the timing and size of the increases in electricity rates in relation to Muskrat Falls Hydro Electric Project". So without further visibility on that, they can't entertain an upgrade is how I read that. Is that your understanding?

MS. PERRRY:

A. I don't envision any upgrade until there's – and even with the certainty, Moody's will certainly, I think, have reservation about the magnitude of the cost that the utility is going to have to bear and ultimately pass on to its customers.

JOHNSON, Q.C.:

Q. Let's put it this way, I take it you're forecasting your cash flow pre-working capital to debt ratio or a percentage to be above 17 percent, are you not?

MS. PERRY:

A. In the proposed, yes, we are.

JOHNSON, Q.C.:

Q. Yes, that's right, and Moody's gave Newfoundland Power a stable outlook in this report?

MS. PERRY:

A. Yes, they have.

JOHNSON, Q.C.:

Q. According to your rebuttal evidence, if we could turn to that, and I'm referring specifically to the Moody's credit opinion on FortisAlberta. That would be Exhibit R-1.

KELLY, Q.C.:

Q. That would be at the end of the report, Samantha. Just scroll down what you got on the screen. There you go.

JOHNSON, Q.C.:

Q. Thank you. So if we see the rating drivers in that opinion, if you could come down a bit further, we see rating drivers, credit support of regulatory environment. So your understanding is that Moody's considers the AUC to be providing a credit support of regulatory environment, right?

MS. PERRY:

A. Yes, that's what it says here, Mr. Johnson.

JOHNSON, Q.C.:

Q. That's right, and if you just go into the Moody's document, into the second page of it, the second page of the document – I'm sorry, that's -

KELLY, Q.C.:

Q. We're still in the R-1.

JOHNSON, Q.C.:

Q. Okay, thank you very much. So you see at the top, "Summary rating rationale, FAB's BAA-1 senior unsecured rating reflects its

credit support of regulatory framework and stable financial performance", and they go to note, "The PBR framework increases regulatory risk in the near term and increases cash flow volatility", so that's something that's been introduced by the regulator in Alberta is PBR?

MS. PERRY:

A. Yes, that's correct.

JOHNSON, Q.C.:

Q. And you're aware of that, okay. And they note here that, if you go down, one, two, three, four—the fifth paragraph under the heading, "Credit Supportive Regulatory Environment", starting with "Offsetting", the word "Offsetting". They say offsetting these strengths that they've referred to in the above paragraphs, our regulatory lag, ongoing uncertainty related to utility asset dispositions and relatively modest allowed returns. And then they go on in the next paragraph, starting with "Ongoing", the "Ongoing utility asset disposition issue is a weakness in Alberta regulation. The

prospect of suffering a loss of prudently incurred rate base that is borne by shareholders is clearly a negative, a credit negative for utilities." And, Mr. Smith, you were an executive at FortisAlberta, I understand?

MR. SMITH:

A. Yes, and I left FortisAlberta in 2008.

JOHNSON, Q.C.:

Q. Okay, was that an issue out there when you were there, the ongoing utility asset disposition issue?

MR. SMITH:

A. You will have to give me a moment to catch up, Mr. Johnson.

JOHNSON, Q.C.:

Q. Certainly.

MR. SMITH:

A. Can you point me to the right place?

JOHNSON, Q.C.:

Q. It's starting that paragraph, "The ongoing utility asset disposition, UAD issue."

MR. SMITH:

A. I'm not familiar with it, sir.

JOHNSON, Q.C.:

Q. Okay, apparently there's—do you have any familiarity with it, Ms. Perry?

MS. PERRY:

A. Yes, I'm aware of the issue of the utility asset disposition. I understand that it's still tied up within the courts in some proceeding with respect to what it all means.

JOHNSON, Q.C.:

Q. What's the nature of the risk to the shareholders in FortisAlberta?

MS. PERRY:

A. I think it's with respect to assets that are not considered used and useful or they're stranded assets and they're no longer allowed to be recovered in rate base.

JOHNSON, Q.C.:

Q. Okay, and then of course, we've seen now recently, I guess after the issuance of this opinion, this is a June 30th opinion, this would have been after the issuance of the opinion which dropped the ROE from 8.75 to 8.3 and reduced the common equity structure in Alberta, right? Do I have the timing right?

MS. PERRY:

A. I'm not sure of the timeframe of when all of this was known and unknown to the regulator.

JOHNSONS, Q.C.:

Q. Well we saw the March decision from the AUC that we referred to earlier and just flip on the first page of this credit opinion, if you could go back, Samantha, please? Dated June 30th, 2015, so after that, and just scroll over to rating outlook, that would be the third page at the bottom, Moody's is saying "as regard rating outlook, FAB's stable rating outlook reflects our view that FAB will continue to operate as a low risk electric distribution utility and a credit supportive regulatory environment." Now, I want to turn you to Mr. Coyne's report at Figure 8.

MS. PIERCEY:

Q. May I ask which report? We have the cost and capital and we have the other -

JOHNSON, Q.C.:

Q. His main report. I'm not seeing that reference here. Perhaps, Mr. Chairman, I can sort that out if we wanted to break just

a tad early so we could be on the right page.

CHAIRMAN:

Q. Yes, sir, thank you.

(BREAK – 10:55 a.m.)

(RESUME - 11:33 a.m.)

CHAIRMAN:

Q. Well I guess I have to watch the news tonight this evening, so – Mr. Johnson.

MS. GLYNN:

Q. Mr. Chair, there is –

CHAIRMAN:

Q. Oh, sorry.

MS. GLYNN:

Q. No, my apologies, I forgot to mention it before we came out, but Newfoundland Power has some undertakings from yesterday ready to file and Mr. Kelly is going to speak to us.

CHAIRMAN:

Q. Sir.

KELLY, Q.C.:

Q. We have, Mr. Chairman, filed the responses to the three undertakings from yesterday and they have now been distributed, so that

completes the undertakings from yesterday.

JOHNSON, Q.C.:

Q. Mr. Chairman, Commissioners, we now have Figure 8, it was the right Figure 8 but it was in Mr. Coyne's appendix, his capital structure report that I wanted to bring the witness to. And this is where Mr. Coyne sets out a ranking of regulatory jurisdictions in Canada as—and the source for his data is DBRS, right? And we just went through a discussion of Alberta and we see Alberta is third from the left, so lower than the Canadian average. Do you see the Canadian average, which is the fifth bar, as you go from left to right?

MS. PERRY:

A. Yes, I see that.

JOHNSON, Q.C.:

Q. Right, and we see Newfoundland and Labrador, they look to be tied with PEI and the only two provinces that look to be above Newfoundland and PEI and the Province of Quebec and British Columbia, right, according to your own expert.

MS. PERRY:

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A. Yes.
JOHNSON, Q.C.:
Q. Now, Ms. Perry, we see a graphic representation of the fact that a major bond rating institution in the country would place Alberta significantly below average in terms of the ranking of regulatory jurisdictions for credit supportiveness and I just ask you, Ms. Perry, where is your evidence that with a reduction in Newfoundland Power's capital structure that the Public Utilities Board of Newfoundland and Labrador would not still be seen as being a credit supportive regulatory jurisdiction in Canada?
MS. PERRY:
A. So the evidence that we've put forward towards this Board is really based on the reports for both DBRS and Moody's, both have indicated that the 45 percent is a credit strength and when I talked with both of them, we'll go over our credit metrics and the regulatory construct in this area, recent decisions of this Board and inclusive of all those discussions is our capital

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structure and that's been around for over 20 years, as I've said. If a decision were made that would actually reduce the capital structure, well then it's obvious that they would have to reconsider that as a part of their overall perception of regulatory support in this area. I cannot say with certainty what Moody's or DBRS would do. The one certainty that I feel pretty strongly about is, you know, to change from 45 to 40 in a 7 ½ percent return would be pretty significant material changes to Newfoundland Power and Newfoundland Power's cash flows and I'm saying that they would certainly have to look at that in the context of their credit assessment of Newfoundland Power.
JOHNSON, Q.C.:
Q. But I guess a move to 40 percent common equity with, say, an 8 percent or 8.3 percent ROE, like Alberta, wouldn't be as significant a change, I take it, in your opinion?
MS. PERRY:
A. Can you repeat the question, Mr. Johnson?

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JOHNSON, Q.C.:
Q. You just prefaced it to the 40 percent common equity on 7 ½ percent ROE in your discussion a moment ago. I take it you would agree that if it was 40 percent and 8 percent or 8.3 percent return on common equity, that that would not be, that would not be as so significant a change?
MR. PERRY:
A. No, I'd still disagree with that comment. I see a 40 percent capital structure as significantly different than 45 percent and I think any change in the capital structure, it will be one of the rating's consideration of both the credit rating agencies.
JOHNSON, Q.C.:
Q. And we've seen from the Moody's report that Moody's in June or July of 2015 had to assess the PBR charges in Alberta, the dispute about the assets that might be stranded to the detriment of shareholders, the movement of PBR and associated regulatory lag, the drop in the common equity component for the Alberta utilities, the drop by 50 basis points in the ROE, and

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you will confirm that they still, at the end of the day, confirm that Alberta had a credit support of regulatory environment, correct?
MS. PERRY:
A. I will agree that they've indicated that the support of regulatory environment was a credit strength, but you have to consider it in the context of Alberta and I'm not fully versed in all of the specifics of the Alberta utilities, but you have to consider that they're bigger, their economy is different, their demographics are not ours and as I've shown in the rebuttal, what they actually achieve is significantly above what they're allowed to earn, which is contrary to what Newfoundland Power actually reports.
JOHNSONS, Q.C.:
Q. But they ended up, notwithstanding the fact that they had higher earnings than Newfoundland Power, they still ended up having much weaker EBIT credit metrics according to the DBRS methodology, didn't they?
MS. PERRY:

A. Can you show me where you're pointing to that?

JOHNSON, Q.C.:

Q. Well I thought we went through that this morning when we compared Newfoundland Power to the other utilities across the country, in the BC, FEI evidence, do you recall that?

MS. PERRY:

A. Yes. I would have to look at what's behind the calculation for the EBIT coverage. I know that the DBRS EBIT coverage for us actually adjusted for employee future benefits and we have a pretty significant defined benefit pension plan that factors into our EBIT calculation, they normalize for that. So I would have to do a deeper comparison to say with certainty that one actually compares to the other.

JOHNSON, Q.C.:

Q. So are you putting into question the evidence that I put to you from the regulatory filing by FEI in BC who retained Mr. Coyne to represent them in that proceeding that we went through this morning?

MS. PERRY:

A. No, I'm not disputing the evidence; I'm just saying I'm not fully understanding the differences in what's driving the EBIT coverage for each of the utilities, that's all.

JOHNSONS, Q.C.:

Q. Okay, you just don't know.

MS. PERRY:

A. Absolutely, I do not know.

JOHNSON, Q.C.:

Q. Just go back to the Fortis BC Energy cross aide material for a second, at page 20, lines 4 to 8 of Fortis BC's filing indicate that the factors in the rating grid do not constitute an exhaustive treatment of all the considerations for ratings of companies in the regulated electric and gas utility sector. Other considerations that may play an integral part of a rating process include items such as liquidity, management quality, ownership and governance; therefore, the grid indicated ratings do not always match the actual Moody's ratings of each company. Now, would you agree with that statement,

Ms. Perry?

MS. PERRY:

A. Yes, I would agree.

JOHNSON, Q.C.:

Q. Okay, and in terms of liquidity, Newfoundland Power's core liquidity comes from its 100-million dollar credit facility, is that right?

MS. PERRY:

A. Yes, I would agree with that.

JOHNSON, Q.C.:

Q. And that has no material adverse change provision, is that right?

MS. PERRY:

A. That is correct.

JOHNSON, Q.C.:

Q. So in other words, no matter what happens in terms of the material adverse change at Newfoundland Power, that does not have to be an issue in terms of accessing that 100 million dollar credit facility, correct?

MS. PERRY:

A. We had the material adverse clause removed some years ago, yes.

JOHNSON, Q.C.:

Q. Okay, and you have to make no warranty statements whatsoever under your credit facility in order to access that liquidity, correct?

MS. PERRY:

A. I would have to confirm that there's no warranty, but I believe you're correct, yes.

JOHNSON, Q.C.:

Q. Okay, and in terms of management quality at Newfoundland Power, is it your understanding that the credit rating agencies have a good view of the management quality at Newfoundland Power?

MS. PERRY:

A. I've not specifically asked them what they think of us, but we're very keen to keep them updated and give them good quality information, so I haven't heard any negatives about us thus far.

JOHNSON, Q.C.:

Q. And we're expecting stability in the management group at Newfoundland Power, are we?

MS. PERRY:

A. Sorry, what was the question?

JOHNSON, Q.C.:
Q. Can we expect stability in the leadership team at Newfoundland Power?
MS. PERRY:
A. I think that's a fair observation. There's always changes, but we don't know what's coming, but –
JOHNSON, Q.C.:
Q. Yes, and in terms of ownership, the ownership of Newfoundland Power by Fortis, that would be considered a credit positive?
MS. PERRY:
A. What the credit rating agencies will say about Fortis is that they respect that Newfoundland Power is a stand-alone utility and that Fortis is not creating any interconnections with the utility.
JOHNSON, Q.C.:
Q. Well if we turn to—we don't have to turn there, I'll just for the record note that in Moody's report they say, under the heading NPI is Independent of Fortis Inc., and I'm not disputing that, by the way, okay?
MS. PERRY:
A. Yes.

JOHNSON, Q.C.:
Q. They say "While NPI is one of a number of utility operating companies"—this is at page 3, just for the record, "a number of operating companies owned by" –
MR. HAYES:
Q. Exhibit 4, Mr. Johnson?
JOHNSON, Q.C.:
Q. It is, yes. There you go, if you go down a little bit further, Ms. Piercey, thank you. "We consider NPI, like sister companies FortisAlberta, FortisBC Inc. and FortisBC Energy Inc., to be operationally and financially independent from Fortis. A credit positive Fortis has consistently demonstrated good management and support of its subsidiaries and we view NPI's access to the executive and strategic support of Fortis to be a credit positive." So that just confirms my understanding?
MS. PERRY:
A. Yes.
JOHNSON, Q.C.:
Q. And then in terms of governance also being something that would be an integral part of

the rating process. What is the governance picture that the credit rating agencies are thinking about there?
MS. PERRY:
A. I haven't had specific governance related conversations with either Moody's or DBRS, but they are fully aware that we are a stand-alone utility with our own board of directors which provide oversight to the management and utility in general.
JOHNSON, Q.C.:
Q. So just to conclude on the point, we would agree that management, quality, ownership, governance and liquidity are strengths of Newfoundland Power from a credit supportiveness point of view?
MS. PERRY:
A. In my opinion, yes. Again, I think referenced with respect to anything in either the Moody's or DBRS report.
JOHNSON, Q.C.:
Q. And these would be considered, to your understanding as we read, an integral part in a rating process?
MS. PERRY:

A. Can you repeat the question, Mr. Johnson?
JOHNSON, Q.C.:
Q. Well the BC evidence indicated that these considerations may play an integral part in a rating process.
MS. PERRY:
A. I'm not sure I would say it's an integral part, but I would say that they do consider things like ownership, management, quality, governance as a part of their ratings consideration. It hasn't been a bit part of the process that I followed with Moody's or DBRS.
JOHNSON, Q.C.:
Q. Regarding preference shares, Ms. Perry, you have been, I think it's fair to say, critical of Dr. Booth's suggestion to replace 5 percent common equity in your capital structure with preferred shares, is that the proper characterization?
MS. PERRY:
A. That I've been critical?
JOHNSON, Q.C.:
Q. Yes.
MS. PERRY:

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A. Yeah, I would agree with that and the fact that I, from a practical perspective, we're a small issuer and I believe Dr. Booth agrees with this, that we're unable to access that preferred share market.

JOHNSON, Q.C.:

Q. Well, just on that point, your evidence in rebuttal at page 2, if we could go to that, down at the bottom of the page, Ms. Piercey, please? Page 2 of the rebuttal of Newfoundland Power, that is, right. There you go. This rebuttal says, starting at line 19, "Dr. Booth has indicated that Newfoundland Power is correct in its assessment that any preference share issue must be over 100 million dollars to be marketable." Ms. Perry, that's not what Dr. Booth says and I put to you that mischaracterizes what Dr. Booth says, are you aware of that?

MS. PERRY:

A. No, I'm not aware of that. Can you show me that complication?

JOHNSON, Q.C.:

Q. Yes, page 96 of Dr. Booth's evidence, lines

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15 to 16. What Dr. Booth said was not that they must be over 100 million, he said first Newfoundland Power is correct that the size is generally over 100 million. So do you accept that your rebuttal evidence mischaracterized what Dr. Booth said?

MS. PERRY:

A. I would acknowledge that he said it's generally over a hundred, but that's practically what it would have to be in order for us to issue –

JOHNSONS, Q.C.:

Q. But he didn't say it must be over a hundred, did he?

MS. PERRY:

A. He might not have said it, but I've had conversations with investment bankers about access to the preferred share market and certainly the hundred million, the, I'm going to say the magic number that we talk about with respect to accessing that particular market.

JOHNSON, Q.C.:

Q. And what I was getting at is how you characterize what Dr. Booth had said. Now

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in any event, Dr. Booth advises that Canadian Utilities Inc., finances the Atco Utilities by raising debt and preferred shares on their behalf and then the utilities then issue these shares or securities to the parent that mirror the parent's costs. Are you aware of that happening?

MS. PERRY:

A. Yes, I was aware of that, yes.

JOHNSON, Q.C.:

Q. You're aware of that, okay. And Dr. Booth advises and he can testify to this, but I want to put it to you that there is no technical reason why Fortis Inc. cannot do the same for Newfoundland Power, would you agree with that?

MS. PERRY:

A. Could Fortis issue preferred shares and push them down to Newfoundland Power? On a technical basis, I suspect they could; that would defy recent directions and orders from this Board and I believe it was in 2003/2004 where at that time there was linkages being made between the credit quality of Fortis

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and Newfoundland Power because S&P had decided to do a consolidated rating at that time and that was all happening when we were actually in front of this particular Board, and the Board at that time stipulated that we needed to take the necessary steps to mitigate those linkages between us and Fortis. So for Fortis to actually issue preferred shares on our behalf, creates clear linkages between the credit quality of Fortis and that of Newfoundland Power.

JOHNSON, Q.C.:

Q. Okay, so in terms of Fortis Inc.'s financing, we've already established that Fortis Inc. finances its investments with approximately 35 percent common shares and 10 percent preferred shares and you would agree that Fortis Inc. is a regular issuer of preferred shares, can you agree—do you disagree with that?

MS. PERRY:

A. I'm not sure if they're considered a regular issuer, but they have issued preferred shares, yes.

JOHNSON, Q.C.:

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Q. Are you aware of the concept of deeming a preferred share component in your capital structure?

MS. PERRY:

A. Yeah, I understand what "deeming" means, I'm just not sure how it works, practically and I've had this discussion at the office for many hours about what would it mean if we deemed five percent of our capital structure and as I said in my opening, I believe that if an investor is not earning a fair return, that investor would redirect that investment to something that would yield a reasonable return and I think that's a reasonable theory because we all invest our own money and we would expect to earn a fair return, so to leave our money somewhere where we're not earning a fair return just doesn't seem reasonable, so I understand the concept of deemed, I just don't understand the practical implications of what that means.

JOHNSON, Q.C.:

Q. Are you aware that deeming a preferred share component is what the Regis in Quebec allows in relation to Gaz Metro.

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MS. PERRY:

A. I'm unaware of their deemed structure.

JOHNSON, Q.C.:

Q. Okay, I'm told and Dr. Booth can speak to this, that in Quebec, Gaz Metro has a 38 ½ percent common equity ratio and a 7 ½ percent deemed preferred share component, but you're not aware of that?

MS. PERRY:

A. I'm not aware of that. I'm not familiar with it, no.

JOHNSON, Q.C.:

Q. Okay. I'm advised and understand from Dr. Booth that a deemed preferred share component has the advantage of imposing no financial risk on the shareholder, while also providing equity support for the bond rating and credit metrics, is that accurate?

MS. PERRY:

A. I think we're going to have to direct that to get clarity from Dr. Booth. I don't personally understand it. I actually believe that if you were to deem a capital structure, then it would be reasonable to assume that the shareholder is going to make

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a choice on what they're going to do with their investment in that case. So practically I believe there's implications for deeming a capital structure here in Newfoundland.

JOHNSONS, Q.C.:

Q. And preferred shares wouldn't be treated as debt for the purpose of credit metrics, is that correct?

MS. PERRY:

A. No, that's not correct. What happens with preferred shares, depending on the terms and conditions of the preferred shares, perpetual prefs. are normally considered equity. The preferred shares that are most recently issued in the market that have this rate reset provision, so they're repriced every five years or so, credit rating agencies actually look upon those type of preferred shares more as debt than they do equity just because they have that financing risk associated with it.

JOHNSON, Q.C.:

Q. I see, and so you've indicated you don't know what they do in Quebec, so the

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preferred shareholder, they wouldn't have a claim on the assets of the company, like debt holder, would that be right? A preferred shareholder?

MS. PERRY:

A. Preferred, like if Newfoundland Power were to issue preferred shares?

JOHNSON, Q.C.:

Q. Right.

MS. PERRY:

A. Depends on the preferred shares that we issue, yes.

JOHNSON, Q.C.:

Q. Okay, I see. And, Ms. Perry, please understand the reason I'm asking you these questions is in fairness to get you to put to you what I understand Dr. Booth will testify to give you a chance to respond to that, as opposed to not asking you a word and having Dr. Booth come before the Board, okay?

MS. PERRY:

A. Yes.

JOHNSON, Q.C.:

Q. I want to go back to Mr. Smith for a moment.

I note that undertakings had been filed. I just haven't had a chance to look completely at them, so it might be something—but I want to go into another line of questioning, Mr. Smith, and that pertains to the executive compensation aspects of the case. Mr. Smith, I sent over to you on March 24th a number of cross-examination aides and I will be referring to those in my examination.

(12:00 p.m.)

MS. GLYNN:

Q. Did you want to enter them all at this point or –

JOHNSON, Q.C.:

Q. I think it would be helpful as opposed to doing it one by one. Just one note, on the letter of March 24th, there is an Item 6 that refers to an examination aide short-term incentive policy comparison and that, there is no such document a short-term incentive policy comparison and so the item 7 is where we--we can strike reference to No. 6 and just continue on with No. 7 and if need be, I can file something for housekeeping purposes, whatever you need, but it was

pointed out to me when I sent it over to Newfoundland Power that there was no Item 6 enclosure and then I determined that that was a misnomer.

MS. GLYNN:

Q. So the items that have been distributed will be entered Information 7 through to No. 16, skipping No. 6 on the letter.

JOHNSON, Q.C.:

Q. Okay, thank you very much.

KELLY, Q.C.:

Q. Is that 7 to 16?

MS. GLYNN:

Q. Yes.

JOHNSON, Q.C.:

Q. Thank you. Now if we could just briefly turn to CANP-204 at page 1 and I'm down at lines 14 to 19, and the question starts off with what comparator groups does Newfoundland Power consider in assessing whether its wages, salaries and benefits are reasonable for a) executive; b) non-executive senior management; c) management; and d) unionized, and I'm referring now to the executive portion of the answer that

starts at line 13 where it states, "To establish annual executive-base salaries, the company uses the broad Canadian commercial industrial executive market as the relevant comparator group. The company's policy is to establish salaries by reference to the median of this market. The forecast median of this market establishes the company's salary policy for executives. The typical salary range is 80 to 115 percent of the salary policy. Actual salaries are set within this range according to the incumbent's experience or progression of performance." So as I understand it, Mr. Smith, Newfoundland Power uses the Hay Group's broad Canadian commercial and industrial executive market as the relevant comparator group, is that right?

MR. SMITH:

A. That is correct.

JOHNSON, Q.C.:

Q. And the policies we've seen is to pay executives between 80 and 115 percent of the median of this market, right?

MR. SMITH:

A. Yes, that is correct.

JOHNSON, Q.C.:

Q. Okay, now Newfoundland Power, using this broad Canadian commercial industrial executive market provided by the Hay Group, who chose this as the comparator group, Newfoundland Power or Hay?

MR. SMITH:

A. This would be the work that Hay would have done.

JOHNSON, Q.C.:

Q. So they chose the comparator group?

MR. SMITH:

A. That's my understanding.

JOHNSON, Q.C.:

Q. As I understand it, Mr. Smith, the comparator group chosen is the one that best reflects Newfoundland Power's executive compensation policy, would that be right?

MR. SMITH:

A. Yes, the comparator group would be used to reflect the compensation policy for the company.

JOHNSON, Q.C.:

Q. Right. And in essence, Mr. Smith,

Newfoundland Power's executive compensation policy states that the category of companies states or implies, at least, the category of companies that Newfoundland Power's compensation for executives should compete with, would that be fair?

MR. SMITH:
A. Could you take me to the document?

JOHNSON, Q.C.:
Q. Well we're at this document where it indicates the forecast median of this market establishes the company's salary policy for executives and the market we're talking about is the broad Canadian commercial industrial executive market.

MR. SMITH:
A. That's fair.

JOHNSON, Q.C.:
Q. And so in essence, would you agree with me that it's implied from this that these are the companies that Newfoundland Power's compensation for executives must be competitive with?

MR. SMITH:
A. That is correct.

JOHNSON, Q.C.:
Q. Okay, and your executive pay has to be competitive so that you can attract and retain qualified executives?

MR. SMITH:
A. That is correct.

JOHNSON, Q.C.:
Q. And so it's Newfoundland Power's executive compensation policy that says compensation should be comparable to the broad Canadian commercial industrial executive market, would that be right?

MR. SMITH:
A. That would be true.

JOHNSON, Q.C.:
Q. And if the compensation policy said that compensation should be comparable to the broad Canadian utilities' executive market, a different Hay assortment would be used, would that be your understanding?

MR. SMITH:
A. Yeah, the one we use is a broad Canadian, you're referring specific to utilities, so I assume there would be a different group, yes.

JOHNSON, Q.C.:
Q. Right, and if the comp. policy said that compensation should be comparable to the eastern Canadian utilities' executive market, your understanding, similar to mine, would be that Hay would give you a list of groups populated—groups of companies populating another market, would that be right?

MR. SMITH:
A. Yeah, if Hay thought that was the right comparable group, then you would get a different list, yes.

JOHNSON, Q.C.:
Q. So it would be fair to say that the comparator group that is used is dependent on how Newfoundland Power defines its compensation policy, would that be fair?

MS. SMITH:
A. Again, Hay brings us a recommendation to use the broad Canadian commercial industrial executive group.

JOHNSON, Q.C.:
Q. But just so we can understand, if Newfoundland Power decided, no, we want our

compensation to be comparable to Canadian utilities, Hay would provide you another group of companies?

MR. SMITH:
A. If you directed Hay to look at a different format or a different request, they would look at a different group of companies, yes.

JOHNSON, Q.C.:
Q. That's right and it's Newfoundland Power that sets the executive compensation policy?

MR. SMITH:
A. Well it's our board of directors that sets the executive compensation for the company.

JOHNSON, Q.C.:
Q. Right. If I could turn you to the salary policy comparison which is –

MS. GLYNN:
Q. That would be Info No. 14.

JOHNSON, Q.C.:
Q. Thank you.

MS. GLYNN:
Q. No. 9 on the correspondence.

JOHNSON, Q.C.:
Q. Yes, that's right. And we've listed here, Mr. Smith, well first of all, I guess, have

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you had a chance to review the tables that we're going to be discussing today?

MR. SMITH:

Q. Yes, I have.

JOHNSON, Q.C.:

Q. Now I sent it over plenty early so that we could have a fruitful discussion, so I hope that was of benefit to you. The examination aide regarding salary policy comparison shows, on the left-hand column, 9 different utilities, it refers to what compensation consultant, it talks about what peer group to use, whether it's a regional focus, a utility focus, whether it includes Crowns and it also provides the salary ranges in terms of a percentage of median, okay, and have you had a chance to confirm the accuracy of what we've put forward to you in this chart?

MR. SMITH:

A. I haven't had a chance to confirm the accuracy, I mean, I just looked at the information.

JOHNSON, Q.C.:

Q. Okay, and so you're not proposing that there

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be any corrections or additions that you think should be made to this representation, are you?

MR. SMITH:

A. I haven't reviewed it to be able to check it, I've just looked at the information as provided.

JOHNSON, Q.C.:

Q. Okay, and so would you accept this subject to check, that this is accurately setting it out?

KELLY, Q.C.:

Q. There's no way for the company to know the individual policies of all these other companies, it's a cross-examination aide that Mr. Johnson has put forward. It's not for us to determine whether it's accurate.

JOHNSON, Q.C.:

Q. If you flip to the next page, I've provided hyperlinks to each and every source that we're referring to, so in Newfoundland Power's case, brought them to a specific request for information, an application to FortisBC's, FortisAlberta, every single one of them has a ready-to-use hyperlink that

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you can go on and it also shows, not only the material, but the page numbers and the line numbers where this data comes from.

KELLY, Q.C.:

Q. That simply reflects whatever source data Mr. Johnson has used, he's entitled to put forward an aide in cross-examination, we don't take any issue with that, but it's not for the company to have to go and check that each of those documents is accurately reflected in the table and the circuit would have no ability to check the circumstances of any individual company, that it's accurately reflected in the source document that Mr. Johnson puts forward as the source. That's not something that is the company's responsibility.

JOHNSON, Q.C.:

Q. Well, let's put it this way, you don't have no intentions of checking with whether or not what I've put forward and have provided links to is accurate, is that Newfoundland Power's position?

KELLY, Q.C.:

Q. If the Consumer Advocate wishes to put

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forward evidence or testimony, it's the Consumer Advocate's obligation to do so. He has put forward an aide for cross-examination. We take no issue that he can put forward his aide in cross-examination, but it doesn't, per se, constitute proof, there's no report from the Consumer Advocate or anything, no witnesses coming to testify and it's certainly not our job to actually have to verify that any information in the source documents correctly sets forth the compensation package for a company that we wouldn't have any way to be able to ever determine whether it's right or wrong. It's simply not either our job or feasible.

(12:15 p.m.)

JOHNSON, Q.C.:

Q. This ties into Board orders, it ties into these companies' websites, they're publically available documents, no different than the Hay study that's being used in this case is publically available and what's the suggestion, that I'm to bring somebody down here at \$300 or \$400 an hour and go through this exercise of saying, yes, we've got this on the website and here is the documentation and Newfoundland Power here indicating, they've had this for five or six days, the very reason they had it was so that they could have time to source check what I have said and to offer any corrections that they thought were appropriate and they're here today saying they haven't looked at it, haven't checked, no way of knowing what I said is accurate; that's a bit much.

KELLY, Q.C.:

Q. It's not our job to source check, Mr. Chairman; it is simply not our responsibility. It's an aide that Mr. Johnson has put forward for cross-examination. As I said before, we fully respect his right to do so and put his questions to the witness.

JOHNSON, Q.C.:

Q. Well let's put it this way, Mr. Smith, let's look at the table for the salary policy comparison. Some of these, by the way, are Hay Group studies, Hay Group being your expert consultants. Now, would you accept that of these nine utilities, that there is

a regional focus, in terms of the peer group on four of them, including FortisAlberta, which is a sister utility, ENMAX, EPCOR, as well as New Brunswick Power?

MR. SMITH:

A. So you're referring to the column that says "regional focus"?

JOHNSON, Q.C.:

Q. Yes.

MR. SMITH:

A. So I don't really understand what that means, what this regional focus means.

JOHNSON, Q.C.:

Q. It means that when they're looking at their peer group that they are looking at a peer group in their region, Mr. Smith.

MR. SMITH:

A. So if I look at the first one, NB Power is in the same peer group as ENMAX, I'm not sure how that works.

JOHNSON, Q.C.:

Q. No, that's not what that is conveying. New Brunswick Power who uses Hay Group, okay?

MS. SMITH:

A. Yes.

JOHNSON, Q.C.:

Q. They use—they have a regional focus to the identification of their peer group, okay?

MR. SMITH:

A. Okay.

JOHNSON, Q.C.:

Q. Whereas Newfoundland Power, you'll see that's blank, empty box means no. Newfoundland Power does not use a regional focus to its peer group, is that correct?

MR. SMITH:

A. Newfoundland Power uses the broad Canadian industrial median group.

JOHNSON, Q.C.:

Q. No regional focus?

MR. SMITH:

A. It's the broad Canadian group.

JOHNSON, Q.C.:

Q. Right, and you were in FortisAlberta, were you aware that they use a regional focus in Alberta, you were an executive out there?

MR. SMITH:

A. I can't speak to what you have here for FortisAlberta, I really can't.

JOHNSON, Q.C.:

Q. Okay. Do you agree, Mr. Smith, on the basis of this chart that it appears that a number of these utilities, I count five, have a utility focus in the identification of their peer group?

MR. SMITH:

A. Again, Mr. Johnson, I guess my struggle is utility focus and how the data is put together and what it means. I mean, there's check boxes in five columns that indicate FortisAlberta's utility, ENMAX, EPCO and Nova Scotia Power and Ottawa Hydro, but what other utilities would be in their peer groups, I don't know and what other type of companies, I don't know.

JOHNSON, Q.C.:

Q. Okay, let's just look at FortisAlberta for a moment, just flick to the next page. And we see under FortisAlberta the second hyperlink, if you could click on that.

MS. PIERCEY:

Q. Would you like to log in?

JOHNSON, Q.C.:

Q. I don't have that log-in information here with me.

KELLY, Q.C.:
Q. Neither do we, Mr. Chairman.
JOHNSON, Q.C.:
Q. If necessary, we can provide the portions of the hard copies as well. Let us look to Nova Scotia Power, could you click on the— this is taken from a public document, Nova Scotia Power, Annual Meeting of Shareholders, May 2014 and could you refer to page 17, please, of this report. Keep on coming down a little bit. Okay, now we see here NSPI Benchmarking, survey data, data from Mercer's Benchmark database survey was used to benchmark compensation using a broad set of energy and utility companies that were not necessarily restricted by size. See below for participant organizations, in some cases, data, Canadian general industry companies of small size were used to provide sufficient data. So we see the companies that they are listing here. ATCO, AESO, BC Hydro, Brookfield Canadian Utilities, Capital Power, Devon Canada, EPCOR, FortisAlberta, Fortis BC, Fortis Inc., Hydro One, Just Energy, Manitoba Hydro, Northland

Power, Toronto Hydro, TransAlta, Valender, that's what I was referring to, Mr. Smith in terms of their being apparently a utility focus in the peer group.
MR. SMITH:
A. Okay, so we're back to the table before.
JOHNSON, Q.C.:
Q. Yeah, would you accept that those companies appear to have a utility focus?
MR. SMITH:
A. So we're in Nova Scotia Power under utility peer group focus and there's a checkmark there?
JOHNSON, Q.C.:
Q. No, we're looking, see what we have on the screen here now.
MR. SMITH:
A. Yes, I understand. So you're asking me are these utilities?
JOHNSON, Q.C.:
Q. Right, and they appear to have a utility focus, do they not?
MR. SMITH:
A. These—I don't know Devon Canada Corporation and I don't know Capital Power Corporation,

but some of them do look like utilities to me, yes.
JOHNSON, Q.C.:
Q. Yes, indeed. Just go to, if we could the peer group comparison utilities, which is, I think that would be 15, would that be right?
KELLY, Q.C.:
Q. Which item on your list, Mr. Johnson for Ms. Piercey?
JOHNSON, Q.C.:
Q. That would be –
MS. GLYNN:
Q. So that would be No. 10, I think.
JOHNSON, Q.C.:
Q. Ten, that's right.
MS. GLYNN:
Q. And Information No. 15.
JOHNSON, Q.C.:
Q. And have you had a chance to look at this table, Mr. Smith?
MR. SMITH:
A. I've read it, yes.
JOHNSON, Q.C.:
Q. Okay, you've read it. And we see the information for Newfoundland Power over on

the right-hand column and you see the names, the compensation consultant, total companies in peer group, utilities as a percentage of total and can you confirm that Newfoundland Power in fact uses the Hay Group? Are we in agreement on that?
MR. SMITH:
A. We use the Hay Group to do our compensation, yes.
JOHNSON, Q.C.:
Q. Yes, and can you confirm that there's 275 companies used by Hay?
MR. SMITH:
A. It's what's on this table, I can't confirm that but it's what's in this table for sure.
JOHNSON, Q.C.:
Q. Okay, and can you confirm that the number of utilities that Newfoundland Power uses in its peer group is zero?
MR. SMITH:
A. Again, that's what this table says, I'd have to go through all of the companies to confirm that for you in terms of the Hay –
JOHNSON, Q.C.:
Q. No, you wouldn't – well do you believe that

you used utilities in Newfoundland Power's comparator group?

MR. SMITH:

A. What I'm saying is to confirm it for you, I'd have to go through the list to do that and I can take a minute to do that, if you like.

JOHNSON, Q.C.:

Q. Certainly.

MR. SMITH:

A. I see Bruce Power here. I guess that's a form of utility possibly. It's a generation company. I see Telus Corporation, I guess, which is a telecommunication company, not an electric utility, but it's a utility of sorts, I guess. So that would be a couple I can see in a quick review of it.

JOHNSON, Q.C.:

Q. Okay, and in terms of the utility companies, our survey would indicate, Mr. Smith, out of these utilities that the only other compensation study that would include no utilities, because we didn't consider that yours did, but you point out Telus and Bruce Power, that the only other comp study that

included no utilities is your sister company, FortisBC, on this chart at zero, okay, and, Mr. Smith, we noted that the number of companies in the peer group, and again with the links to all the sources, showed that Newfoundland Power had 275 in the broad comparison, FortisAlberta used 37 companies, including a whole list of utilities that we see there in that column, ENMAX used 23 companies as part of the peer group, 61 percent were utilities. Towers Watson and EPCOR used only 19 companies, 58 percent were utilities. Mercer in Nova Scotia Power's case used 27 companies, 37 percent were utilities, and New Brunswick Power, again the Hay Group, 23 companies, 17 percent were utilities.

(12:30 p.m.)

MS. PERRY:

A. Mr. Johnson, if I could just add one comment to this group. I do know that with our affiliates, FortisBC and FortisAlberta, that for purposes of determining executive compensation, which is approved by each respective Board, they both used the Hay

Group, and they used the comparator group that we have here. So I'm not quite sure what this column is for FortisAlberta, if it's with respect to what is included in customer rates, but I do know for purposes of setting executive comp, they are consistent with Newfoundland Power.

JOHNSON, Q.C.:

Q. Okay, and we had a footnote on the bottom that for Alberta Hay's peer group is not disclosed – peer group information is from earlier Towers Watson report.

MS. PERRY:

A. Right.

JOHNSON, Q.C.:

Q. So you're saying now that Hay is in place for FortisAlberta, and they don't use – they've gone from 37 companies that had a utility focus to the broad commercial industrial list that Newfoundland Power uses, is that what you're saying?

MS. PERRY:

A. I'm not sure what's here, but I can confirm that they use the Hay Group in the broad commercial industrial group, yes.

MR. SMITH:

A. And, I guess, another thing that's kind of obvious from the information from Hay in terms of the list, obviously, when Hay does this for us, they don't include other Fortis companies, and it is investor owned companies that are on the list.

JOHNSON, Q.C.:

Q. Mr. Smith, can you explain to me why the peer group used in Newfoundland Power's compensation study includes – well, there was only two apparently you would characterize as Canadian utilities. Why would – out of 275 companies, that you could only point to two. Why is it that Newfoundland Power doesn't use any other utility company when it's comparing itself for executive compensation purposes?

MR. SMITH:

A. Well, again this is Hay's list and their recommendation to us, but as I said before, Hay certainly doesn't use any other Fortis companies in their list, and the list is investor owned companies, so that's the reason why you wouldn't see a crown corporation in there in terms of the comparable group.

JOHNSON, Q.C.:

Q. So do you believe that not only not using crown companies, but not using any other utility companies in your list, is my understanding and we can get that confirmed with Mr. Booth, but do you believe that executives in other Canadian utilities are not part of the executive market within which you compete to attract and retain executives?

MR. SMITH:

A. Again all I can tell you is that this is the group that Hay put together to recommend to the company. It's been the group we've had for quite a number of years, and I've explained why other Fortis companies aren't in the list and why crown corporations aren't in the list, and that's what I would say.

JOHNSON, Q.C.:

Q. Is it fair to say that by excluding Canadian utilities from your peer group, you end up providing a higher median level of

compensation?

MR. SMITH:

A. I wouldn't be able to say that.

JOHNSON, Q.C.:

Q. So would you – you don't know whether that's a result of doing that, do you?

MR. SMITH:

A. Again that's the work of Hay.

JOHNSON, Q.C.:

Q. Okay. Let's go to the document – I'm sorry, the document, "Re; Peer Group Comparison, Crown Corporations".

MS. GLYNN:

Q. Information #16, and Item #11 from the correspondence.

JOHNSON, Q.C.:

Q. Again Newfoundland Power, as common with FortisBC, would indicate that no crowns are used in your group. Is that your understanding, Mr. Smith?

MR. SMITH:

A. Again the column for FortisBC?

JOHNSON, Q.C.:

Q. And for Newfoundland Power.

MR. SMITH:

A. That's what this data shows, yes.

JOHNSON, Q.C.:

Q. That's right, and do you know why Crown's are excluded?

MR. SMITH:

A. I think when Hay does their work for the company, they do look at investor owned companies, and crown corporations are not included.

JOHNSON, Q.C.:

Q. And do you know why they don't look at investor owned companies?

MR. SMITH:

A. I think that's a question you could ask Hay for sure, but other than that, if I think of the different Fortis companies that I can do on the top of my head, I don't believe any of them have people that came from crown corporations at the executive level.

JOHNSON, Q.C.:

Q. I see that FortisAlberta, at least when they were having their work done by Towers Watson, that they used quite a number of crowns in their information group. Do you see that, Mr. Smith?

MR. SMITH:

A. Again the data that's here, I really can't validate or speak to. I can acknowledge the numbers that are on the sheet of paper, and as Ms. Perry said, exactly how FortisAlberta do this with Towers or Hay, I'm not familiar.

JOHNSON, Q.C.:

Q. To your knowledge, does Mr. Aboud do the work for FortisAlberta?

MR. SMITH:

A. I believe Hay does work for FortisAlberta.

JOHNSON, Q.C.:

Q. Yes, and does work for NB Power as well?

MR. SMITH:

A. Again if that's what your table says, I can acknowledge your table. I just don't know if they do or not.

JOHNSON, Q.C.:

Q. Mr. Smith, would it be reasonable to guess that the exclusion of crown utilities from Newfoundland Power's peer group results in there being higher comparative salaries on average because you're excluding lower crown salaries? Would that be a fair assumption?

MR. SMITH:
A. I couldn't speak to that assumption, Mr. Johnson.
JOHNSON, Q.C.:
Q. In terms of the regional focus, there's no regional focus in Newfoundland Power's group of comparable companies. You acknowledge that, right?
MR. SMITH:
A. I've acknowledged that Hay used a broad Canadian industrial commercial group.
JOHNSON, Q.C.:
Q. Right, and it's my understanding that none of the current executives at Newfoundland Power were attracted from beyond the Atlantic Canada region, is that correct?
MR. SMITH:
A. No, I wouldn't agree with that. I had one member on our executive team who is from Newfoundland. He worked – let me see, I'll try to do this from memory now. He worked on the gravity base structure, he moved to Prince Edward Island to do some consulting work in the engineering field, he moved to Ontario to do some work in the construction

field with a firm, I believe, in hydro plants, and Newfoundland Power hired him somewhere around 2004 and he's currently on our executive team.
JOHNSON, Q.C.:
Q. So he came to Newfoundland Power in 2004 as a non-executive?
MR. SMITH:
A. He was brought in, I guess, at the director level of the company as an individual with high potential, and his career has unfolded the way we had hoped for, and he's currently on the executive team.
JOHNSON, Q.C.:
Q. Now directors at Newfoundland Power, is their salary policy tied to a region or is it broad Canadian?
MR. SMITH:
A. I'd have to get Ms. Perry to help me with this, but I believe they're national also.
MS. PERRY:
A. It is, and it's the non-executive group within the Canadian broad industrial group.
JOHNSON, Q.C.:
Q. And so with the exception of this example,

none of the current executives at Newfoundland Power were attracted from beyond Atlantic Canada?
MR. SMITH:
A. Well, I guess, I was myself. I came to Newfoundland Power from FortisAlberta.
JOHNSON, Q.C.:
Q. But you had been at Newfoundland Power before going to FortisAlberta?
MR. SMITH:
A. Very true. When I left Newfoundland Power, I guess, I was a superintendent of area operations, and when I was at FortisAlberta, I was on the executive team and came back to Newfoundland Power to join the executive team here.
JOHNSON, Q.C.:
Q. And Mr. Phonse Delaney was with Newfoundland Power, Vice-President. He went to FortisAlberta, and you came home. Is that how it worked?
MR. SMITH:
A. Well, I guess you could say I came home certainly, but Mr. Delaney went to FortisAlberta and I came to Newfoundland

Power, that's right.
JOHNSON, Q.C.:
Q. And you took Mr. Delaney's role here?
MR. SMITH:
A. I took Mr. Delaney's role in Newfoundland Power, that's correct.
JOHNSON, Q.C.:
Q. That's right. Could we turn to CA-NP-199, Attachment "B" at page 13. Mr. Smith, just before -
MR. SMITH:
A. I just need another second to find it. I'll do it from the screen.
JOHNSON, Q.C.:
Q. Certainly. Just before we get to the screen, wouldn't it be reasonable, Mr. Smith, for Newfoundland Power's peer group to at least include utilities located in the Atlantic region as a market for which you would attract executive talent?
MR. SMITH:
A. Again that's a question you would have to ask Hay.
JOHNSON, Q.C.:
Q. You don't know?

MR. SMITH:
A. I'm just saying Hay puts together the group for us in terms of what they feel is the comparable group, and you would have to ask Hay.
JOHNSON, Q.C.:
Q. Yes, but you set the policy, Newfoundland Power sets the policy, and Hay finds you the group, isn't that correct?
MR. SMITH:
A. Hay finds us the group, yes.
JOHNSON, Q.C.:
Q. Based upon your policy?
MR. SMITH:
A. Hay recommends to the company that the broad Canadian industrial group has the recommendation and Hay goes and finds the companies that fit that group.
JOHNSON, Q.C.:
Q. But if you had a different policy to say that we want to be competitive with Atlantic Canada executives, Hay would find you the other group, would find you that group, would they not?
MR. SMITH:

A. I think we talked about that in the beginning and -
JOHNSON, Q.C.:
Q. That's right, we did. Now in terms of this Appendix "B", this is Appendix "B" of the Hay Group's 2012 Manager Compensation Report, and the table compares median compensation for executives and non-executives between the overall Canadian commercial industrial market and the Atlantic Canadian industrial market for the year 2012, okay.
MR. SMITH
A. I just want to confirm it is the screen that's up on the computer, is it?
JOHNSON, Q.C.:
Q. Yes, that's right.
MR. SMITH:
A. Okay.
JOHNSON, Q.C.:
Q. And it actually states that the year is 2102, but that should read "2012", okay, do you accept that?
MR. SMITH:
A. I believe it would be 2012, yes.

JOHNSON, Q.C.:
Q. Right, and it says that the median salary for executives and non-executives in Canada was $180,400.00, which is 32.5 percent higher by our calculation than the same group in Atlantic Canada. Do you want to take a moment and see if I got that right?
MR. SMITH:
A. So again you're looking at the commercial industrial group, the exec, non-exec, compared to the Atlantic Canada industrial?
JOHNSON, Q.C.:
Q. Right, it's $180,400.00 versus $136,000.00?
MR. SMITH:
A. That's what the numbers are.
JOHNSON, Q.C.:
Q. That's right, and we calculate that to be 32.5 percent higher. Are you fine with that?
MR. SMITH:
A. It's your math.
JOHNSON, Q.C.:
Q. Okay, and would it be reasonable to conclude, Mr. Smith, that by choosing a comparator group that excludes Atlantic region utilities from the comparator group,

that the resulting median compensation would be increased? Is that reasonable?
(12:45 p.m.)
MR. SMITH:
A. I can't agree with that. I think again it's something you're going to have to ask Hay. This is Hay's data.
JOHNSON, Q.C.:
Q. Okay. So in terms of the compensation policy at Newfoundland Power, you'd be very familiar with it, I expect?
MR. SMITH:
A. Sure.
JOHNSON, Q.C.:
Q. And you wouldn't know if the comparator salaries would be lower if the sample used was regional, you just don't know that?
MR. SMITH:
A. Again I wouldn't want to speculate. That's the information that Hay would do.
JOHNSON, Q.C.:
Q. And you wouldn't know whether the comparator salaries would be lower if the sample used had a utility focus? You wouldn't know that?

MR. SMITH:
A. Again I think this is the work that Hay does, so you're better off asking that question to Hay.
JOHNSON, Q.C.:
Q. And you wouldn't know if the salaries would be lower if the sample used included crowns and government utilities, you wouldn't know?
MR. SMITH:
A. Again as I've said, that would be a question you would have to ask Kay.
JOHNSON, Q.C.:
Q. Let us turn to CA-NP-199 at page 24 of 41 in Attachment "A".
MS. PERRY:
A. Page 24 of 41?
JOHNSON, Q.C.:
Q. 24 of 41. There you go. This is a letter addressed to you, Mr. Smith, dated February 16th, 2015, from Hay Group in Toronto. Do you recognize this letter?
MR. SMITH:
A. Yes, I do.
JOHNSON, Q.C.:
Q. And it sets out the executive compensation

program updates, and so you are updated regularly by Hay in your role as President of the company, is that correct?
MR. SMITH:
A. Yes, Hay sends us correspondence each and every year before we adjust the executive compensation.
JOHNSON, Q.C.:
Q. Okay, and I understand, and if we perhaps scroll down a little bit, that paragraph towards the bottom of the screen, "As a component of this review, compensation benchmark was conducted for all Newfoundland Power executives". Finding from this benchmarking, he indicated the presence of a gap to your targeted median positioning against the Canadian commercial industrial market. "To address this compensation gap and reinforce the corporation's dedication to building a strong pay for performance culture, a number of changes to your executive compensation practices are proposed. Key changes, discuss in greater detail, and the first one is, "The adjustment of short term incentive targets,

and the other two deal with long term incentive program, and the changes to Fortis' share ownership guide policy". So now, I understand that these proposed changes that they recommended to you in this letter, that these were actually implemented, is that right?
MR. SMITH:
A. Yes, that would be correct.
JOHNSON, Q.C.:
Q. Okay, and was there any discussion between Newfoundland Power executives and Hay about these changes prior to Newfoundland Power receiving this letter?
MR. SMITH:
A. I certainly didn't talk to Hay. I know every now and then Jocelyn has a conversation with Hay, but I don't believe so.
MS. PERRY:
A. No, so they would do their review of executive compensation, which would have included where short term incentive targets have moved in the market, what would be common with respect to long term incentives, and then also with respect to share

ownership guidelines. So they would just go conduct their research, and they would submit us a letter stating their findings. So there's not much discussion because it's their work and their recommendation.
JOHNSON, Q.C.:
Q. Just go to page 25. Just to come down a bit further, "The adjustment of STI targets". So just to understand what short term incentive targets are, we have Table 1, short term incentive targets as a percentage of base salary. So we see that they're referring to a former target for – this would apply to you, Mr. Smith, 40 percent, so that would mean 40 percent of your base salary would be a target that would come by way of a short term incentive, and they're proposing to move that to 50 percent, right?
MR. SMITH:
A. Yeah, I think some of what this is, and again you're going to have to ask Hay, but 2014 was a transition year between myself and Mr. Ludlow, so I was the CEO for part of the year, and I believe in 2013, Mr. Ludlow's percentage of STI would have been

50 percent. So what you may be seeing here is just a reflection of the partial year 2014 where I was in the role, and then when you go to 2015, I basically went back to the same percentage as it was when Mr. Ludlow was the CEO.

JOHNSON, Q.C.:
Q. Okay, let's explore this a little bit, because I take it, you had less points, Hay points, than Mr. Ludlow too, did you?
MR. SMITH:
A. I believe when Hay did their review, that's true.
JOHNSON, Q.C.:
Q. Okay, now just to understand how the short term incentives work, the short term incentives are specified percentages of base salary, is that correct?
MR. SMITH:
A. That is correct.
JOHNSON, Q.C.:
Q. Okay, and so as the base salary increases, the dollar amount of the short term incentive targets increase proportionally, correct?

MR. SMITH:
A. That would be true.
JOHNSON, Q.C.:
Q. Okay, and if the target goes up, the incentive amount increases for the same performance level, correct?
MR. SMITH:
A. That would be true, yes.
JOHNSON, Q.C.:
Q. And it is this target amount that Newfoundland Power includes in its revenue requirements, do I have that right?
MR. SMITH:
A. That is correct.
JOHNSON, Q.C.:
Q. Okay. Now the proposed change to the STI target starting in 2015 is shown here, and I note that the change increases the STI target for all position Hay points by up to 25 percent, I think is how it's described. I don't know if that's – is that further up the page, let me just see. Maybe it's further down. Keep on going. In any event, are you familiar with the recommendation that they would increase the STI targets for

all position Hay points by up to 25 percent?
MR. SMITH:
A. That's what's here in the table certainly.
JOHNSON, Q.C.:
Q. That's right.
MR. SMITH:
A. And maybe the 25 percent comes from 50 over 40.
JOHNSON, Q.C.:
Q. You moving from 40 to 50?
MR. SMITH:
A. Yeah.
JOHNSON, Q.C.:
Q. Okay.
MR. SMITH:
A. That could be.
JOHNSON, Q.C.:
Q. All right, and I understand that – if we could go back to the table for a moment, that the recommendation was for the 15 to 1800 position Hay points, they would move from 35 percent target to 40 percent, is that right?
MR. SMITH:
A. That's what's here, and it's correct.

JOHNSON, Q.C.:
Q. And my understanding is that's about a 14 percent increase in the target, right?
MR. SMITH:
A. 35 to 40.
JOHNSON, Q.C.:
Q. As regards these position Hay point that are referred to, it appears that the points correspond to the level of executive positions, such that a higher level will have higher Hay points, is that correct?
MR. SMITH:
A. That's true.
JOHNSON, Q.C.:
Q. And the intent, as I understand it, is to be able to identify comparable positions across companies without regard to a job title as such, is that correct?
MR. SMITH:
A. That is true.
JOHNSON, Q.C.:
Q. And so higher positions not only get higher salaries, they receive higher STI compensation, both because the base salary is higher and because the STI target is

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higher as well, would that be correct?

MR. SMITH:

A. That's how the math would work, that's correct.

JOHNSON, Q.C.:

Q. Right. So the short term incentive target that used to be included in the Newfoundland Power revenue requirement for rate setting purposes for you was 40 percent, but now it's 50 percent, is that correct?

MR. SMITH:

A. Yes, I believe I ended up at 50 percent, which is what Mr. Ludlow was in 2013.

JOHNSON, Q.C.:

Q. Okay, and as I understand it, the short term incentive target for you, as an executive at 50 percent, that means that the executive salary, your salary plus 50 percent, or one and a half times the salary, is paid by the rate payer, is that right?

MR. SMITH:

A. Could you repeat that again, sir?

JOHNSON, Q.C.:

Q. If you have a short term incentive target of 50 percent, that means that your salary –

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one and a half your salary is the amount paid by rate payers?

MR. SMITH:

A. I believe that is correct.

JOHNSON, Q.C.:

Q. And so Hay recommended that you go up, the Vice-President of Finance, Ms. Perry, go up from 35 to 40, the Vice-President of Regulatory Affairs increase from 35 to 40, is that correct?

MR. SMITH:

A. I believe that's how the points lined it up, yes.

JOHNSON, Q.C.:

Q. And could you just refer to their examination aid – let me just see here now, "Changes to the short term incentive plan".

GLYNN, Q.C.:

Q. Information #12, and #7 on the correspondence.

JOHNSON, Q.C.:

Q. Mr. Smith, have you had a chance to review this table?

MR. SMITH:

A. Yes, I've seen the table.

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JOHNSON, Q.C.:

Q. Have you had a chance to review the accuracy of the information in the table?

MR. SMITH:

A. Again, I guess, we just had the Hay letter up, and it showed numbers, and, I guess, as long as what you've taken from the Hay letter and put it on this table in the exact same format, then it should be the same thing.

JOHNSON, Q.C.:

Q. So you're prepared to take this table, subject to check, are you?

MR. SMITH:

A. I guess that would be fair, yes, because I haven't checked it.

JOHNSON, Q.C.:

Q. Okay. Do you agree, Mr. Smith, and we see as we go along here for yourself, the former policy showed you at 40 percent, the new policy at 50 percent, on the base salary for 2016 of 360. So under the former policy, you got by way of a short term incentive, $144,000.00, and under the new policy you got $180,000.00. That's a $36,000.00

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increase just on the short term incentive, is that correct?

MR. SMITH:

A. That's what the math shows.

JOHNSON, Q.C.:

Q. Okay, and not only what the math shows, that's accurate in terms of you personally experienced that?

MR. SMITH:

A. That's what the math is in the table. I can't disagree with the math, subject to check, but that's what the math shows.

JOHNSON, Q.C.:

Q. And likewise for the other executives who were affected by the increase in STI targets, they went up $14,000.00 per year each just on the target, which would be 14.3 percent increase in their short term incentive target, is that right?

MR. SMITH:

A. That's what the table shows, sir.

JOHNSON, Q.C.:

Q. Okay. This increase is in addition to the salaries that are recovered from rate payers, the base salary, right?

MR. SMITH:
A. That is correct.
JOHNSON, Q.C.:
Q. Because that increased as well. Could we turn to CA-NP-332? So on the previous one, we compared the 2016 salaries, and we see here for 2015, you went up by $10,000.00 in base salary, right?
MR. SMITH:
A. That would be correct, sir.
JOHNSON, Q.C.:
Q. Mr. Murray went up by $24,000.00 in base salary in 2016?
MR. SMITH:
A. I'm not sure of that number, but if we went to the two tables and compared them, I'd take that subject to check, yes.
JOHNSON, Q.C.:
Q. Okay, that's what my information is. Ms. Perry's went up by $7,000.00, and Mr. Alteen's the same, right?
MR. SMITH:
A. Yes.
JOHNSON, Q.C.:
Q. Plus the STI changes, okay. Now I want to

address the concept of net income as a short term incentive plan factor, Mr. Smith. In this regard, could I refer you to PUB-NP-007 page 2? So we have the corporate performance measures, and this is in response to a Board staff question of Newfoundland Power, and asking for details as to corporate performance measures that you use, okay, and assessments of corporate – you start off at the top, Newfoundland Power does, "Assessments of corporate performance are based on the company's performance relative to weighted targets in respect of financial performance, system reliability, customer service and safety. The targets and weightings are modified annually to reflect changes in corporate focus and priority and to encourage continual improvement", and what I'm talking about here now is earnings at lines 14 to 16, which says, "Earnings. This measure represents corporate earnings as per the year end audited financial statements. The target is based on the company's earnings budgeted for the year". So what is the

weight assigned to earnings for 2016?
MR. SMITH:
A. Could you repeat the question? I'm just reading the -
JOHNSON, Q.C.:
Q. I'm sorry, yes. What's the weight assigned to earnings for 2016?
MR. SMITH:
A. I don't know off the top of my head. We'd have to find that percentage, I guess.
JOHNSON, Q.C.:
Q. Let's put it this way, I can tell you that it was 25 percent.
MS. PERRY:
A. It's 15 percent.
(1:00 p.m.)
JOHNSON, Q.C.:
Q. It's still 25 percent?
MS. PERRY:
A. Still 25 percent.
JOHNSON, Q.C.:
Q. And it was 25 percent in 2015 as well?
MS. PERRY:
A. Yes, that is correct.
JOHNSON, Q.C.:

Q. It's been 25 percent for some time, is that your understanding?
MS. PERRY:
A. Since 2012.
JOHNSON, Q.C.:
Q. Since 2012, okay. What was its weight prior to 2012?
MS. PERRY:
A. It was 35 percent.
JOHNSON, Q.C.:
Q. 35 percent. So a significant portion of short term incentive is related to earnings, would you agree with that?
MR. SMITH:
A. That is correct.
JOHNSON, Q.C.:
Q. Okay. If we could just turn for a second to PUB-NP-079, page 2 of 4. This shows the short term incentive plan, corporate targets, and results for 2015. We see at the bottom, earnings is 25 percent, controllable cost is 10 percent, regulatory, which we'll come to, regulatory performance, 15 percent, safety 20 percent, customer satisfaction 15 percent, reliability 15

percent. So are these still the same targets for 2016, Ms. Perry, do you know?

MS. PERRY:
A. They are, they're consistent.

JOHNSON, Q.C.:
Q. What caused the change from 35 percent to 25 percent as a weighting on earnings?

MS. PERRY:
A. It was in 2012 that we had done a review of the, I guess, corporate priorities within our STI targets, and at that time we felt there was increased weighting, I think reasonable to assume, towards safety, and we also included the regulatory performance, given that we place a lot of value on our regulatory performance, and we saw that as one of our key business risks.

JOHNSON, Q.C.:
Q. So prior to that change, there was no regulatory performance corporate target in terms of playing a role in the corporate target?

MS. PERRY:
A. That is correct, yes.

JOHNSON, Q.C.:

Q. So looking at the last General Rate Application decision, you'll recall that there was a dispute between myself and Newfoundland Power as to whether it was appropriate for the earnings target to be included in customer rates, do you recall that?

MS. PERRY:
A. I recall that, yes.

JOHNSON, Q.C.:
Q. And if we could haul up the General Rate Application decision starting at page 52.

MR. HAYES:
Q. That's the last GRA?

JOHNSON, Q.C.:
Q. Correct, yes.

MR. HAYES:
Q. PUB –

JOHNSON, Q.C.:
Q. 13, isn't it?

KELLY, Q.C.:
Q. Just go down through that. Number 13 –

MR. HAYES:
Q. Was the 2013, right?

MS. PERRY:

Q. Yeah, PU 13 there.

JOHNSON, Q.C.:
Q. Okay. If you could go to page 52. Just come down a bit further, Ms. Piercey. Thank you. Just starting at line 34, the Board's discussion of the issue starts off at line 34, "The Consumer Advocate submits that the revenue requirement for 2013 and 2014 should not include expenses in relation to the portion of the short term incentive plan for executives and managers that relates to achieving earnings targets. He argues that the achievement of these targets is for the primary benefit of shareholders and not rate payers. In support of his position, the Consumer Advocate provides regulatory precedent from the Public Utilities Board of North West Territories, Alberta Energy Utilities Board, and the Ontario Energy Board, and he submits that Newfoundland Power's earnings base compensation targets are not truly distinguishable from these regulatory precedents, and urges the Board not to allow their inclusion". Now ultimately we know that the Board decided

that the earnings incentives could be included in rates, right?

MR. SMITH:
A. That is correct.

JOHNSON, Q.C.:
Q. Now if we just look at page 53 for a moment at lines 7 to 8, there's reference to the Board's noting that Newfoundland Power explains that the regulated utility cost of service in British Columbia, Alberta, and Prince Edward Island, includes executive compensation with a financial performance factor. Do you see that?

MR. SMITH:
A. I do see that.

JOHNSON, Q.C.:
Q. Okay. Now I'd like to turn to decisions made by those boards since that 2013 General Rate Application. If I could turn you to the aid being FortisBC's 2014 to 2018 performance based rate making plan.

MS. GLYNN:
Q. Information #9, and it's #3 on the correspondence.

JOHNSON, Q.C.:

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Q. Thank you.

KELLY, Q.C.:

Q. It's number 3 in the letter, Sam, where you had it on the side there a minute ago. There you go, number 3, that's it.

JOHNSON, Q.C.:

Q. At page 202, if we could, and just for the record, this is the BCUC's decision of September 15, 2014, regarding a multi-year performance based rate making plan for 2014 through 2018, in the matter of FortisBC Inc. So just below where it talks about Hay study comparator group, where the Commission panel accepted that FortisBC competes for executive talent in the broad spectrum, right after that there's a provision of benefits to rate payers, and the panel notes, "The panel has concerns as to whether all of the components of FortisBC's corporate and individual performance objectives or score card provide value to the rate payer. The panel notes that the corporate financial objective with the highest weighting at 30 percent is regulated earnings. While there is no disagreement as

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to the importance of a utility being healthy and financially sound, the panel is not persuaded that exceeding its approved ROE is in the interest of rate payers", and then they go on to say, "For these reasons, the panel is not persuaded there is sufficient evidence to support the need for the short term incentive plan to be fully funded by the rate payer. The Commission Panel finds that 30 percent of the STIP cost are on account of the shareholder. Therefore, the panel directs FortisBC to recover only 70 percent of the STIP from the rate payer and reduce its O & M base accordingly". So, Mr. Smith, at the last hearing it would appear that Newfoundland Power was putting forward the regulatory model in BC as supporting the inclusion of that, but would you agree with me that that has now since changed?

MR. SMITH:

A. That's certainly what this document indicates that BC has had a change. Again I can't speak to the context or the background of why the decision was realized. I kind of go back to in terms of the last time we were

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before the Board, and the information you had up recently that we really believe that maintaining our financial integrity is good for our customers and good for the company, it's part of what allows us to maintain our bond rating, it gives us a lower cost of debt, allows us to do the capital work we need to do to service our customers, and I frankly look at it the other way, if we weren't maintaining our financial integrity, that the company would be worse off.

JOHNSON, Q.C.:

Q. Okay. Now I point this out, Mr. Smith, because that was an example of a regulatory jurisdiction that Newfoundland Power pointed to that has changed its view on that.

MR. SMITH:

A. That's what this would show, that they made a change.

JOHNSON, Q.C.:

Q. Right.

MR. SMITH:

A. But again the context and the background, I can't speak to.

JOHNSON, Q.C.:

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Q. Did you – this was sent over to you on the 24th of March. Did you have a chance to go through the decision and even look for the discussion?

MR. SMITH:

A. I just read the words that are here on this sheet of paper, sir.

JOHNSON, Q.C.:

Q. Okay. So let me just turn to the ENMAX decision, which is another aid that was passed over.

MS. GLYNN:

Q. It's number 2 on the correspondence, and it would be Information #8.

JOHNSON, Q.C.:

Q. If you could go to page 70, Ms. Piercey, and again I've provided the Table of Contents so you could see where the discussion takes place in the decision, but at paragraph 312, and this is just after a discussion of eligible earnings, etc, by employees of the company. "In argument, EPC maintain that without AVPP", and, I guess, that's its total direct compensation would fall below the market median. "EPC recognized that the

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Commission has indicated that no more than 10 percent of variable pay should be at risk to financial measures. And EPC noted that as a result of the different waitings for different positions certain employees above the level of manager may have more than 10 percent of the variable pay at risk to financial measures. And Mr. Smith, it would indicate that the Alberta Commission has indicated that while compensation could be at risk for financial measures, that there would be a limit of 10 percent of what the rate payor would absorb. Did you follow that discussion?

MR. SMITH:

Q. That's' what I read on the sheet of paper, sir.

JOHNSON, Q.C.:

Q. Okay. And if we could just turn now to ATCO Electric 2013/2014 tariff application.

MS. GLYNN:

Q. Number 4 on the correspondence and Information No. 10.

(1:15 p.m.)

JOHNSON, Q.C.:

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Q. Thank you. And I'm just going to quote a section from page 215, paragraph 10-41. This is under "Commission Findings Net Income Component". The Commission agrees with the CCA, I guess that's an Intervenor at the proceeding, that the 10 percent ceiling on VPP which is, I think, the variable pay, applicable to net income metrics should be determined in relation to individual VPP amounts and not the overall VPP budget. The Commission reiterates its findings from the decision 2011 450 that a net income component greater than 10 percent might result in an inherent conflict between shareholders interest and customers. If ATCO Electric wishes to include the net income component for specific individuals higher than 10 percent of their VPP compensation, these costs are to be borne by shareholders. And again, you don't take exception to the fact that the Alberta body has decided that way?

MR. SMITH:

Q. No, I mean, that's what the words say, but again the context of the background, what

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they mean by inherent conflict between shareholder interests and customers, I'm not sure, but that's what the words say.

JOHNSON, Q.C.:

Q. And just go to—just to round out—the first item on that letter is CANP 612 of the 2013/2014 application.

MS. GLYNN:

Q. Information Number 7.

JOHNSON, Q.C.:

Q. Just for the record, do you recall when the Board was discussing Newfoundland Power's argument at the last GRA? They were referring to what Newfoundland Power had presented in terms of what's done in BC, Alberta and PEI from the last time and it's just there for the Board's and this proceeding's record, okay. Now, can we go to Item Examination document regarding STIP policies, the Short Term Incentive Plan policies which would be –

MS. GLYNN:

Q. Number 8 on the list and Information No. 13.

JOHNSON, Q.C.:

Q. Right. Mr. Smith, this provides a short

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term incentive plan policies and just gives a survey of what's happening in Newfoundland, BC, Alberta, Ontario, New Brunswick and Nova Scotia. Do you accept, in Nova Scotia, that they are not allowed to recover STI, in their customer rates?

MR. SMITH:

Q. I believe it's been that way for a long time, sir.

JOHNSON, Q.C.:

Q. And do you accept similarly in New Brunswick?

MR. SMITH:

Q. That's what the sheet of paper says.

JOHNSON, Q.C.:

Q. Right. And likewise, Ontario, I think that was the case the last time that net income targets were excluded in Ontario as well.

MR. SMITH:

Q. Again, Mr. Johnson, like we said before, I can confirm what I read.

JOHNSON, Q.C.:

Q. Okay. And we see—we've just gone through that Alberta is restricted, apparently, to 10 percent now, is that right?

MR. SMITH:

Q. That's what the document says.

JOHNSON, Q.C.:

Q. Okay. And Newfoundland is presently included and to your knowledge, BC also includes, is that right, for Fortis or for British Columbia or do you have any awareness of that? You don't?

MS. PERRY:

Q. I can't confirm what is included in customer rates for exec comp.

JOHNSON, Q.C.:

Q. Would you agree that with the recent decisions I have put to you, including from Alberta, that there seems to be a trending towards disallowing net income as a recoverable component of rates?

MR. SMITH:

Q. I can't really agree with that, Mr. Johnson, other than that the information that you've provided provides some data, but whether or not that's a trend or a common or uncommon, I really don't know, sir.

JOHNSON, Q.C.:

Q. Can you undertake to provide how much of

Newfoundland Power's revenue requirement for 2016 and 2017 relates to meeting the net income targets? (Undertaking)

MR. SMITH:

Q. I'm trying to think if it's there already. Can we just look PUB NP 79 for a second, or maybe 74?

MS. PIERCEY:

Q. 74?

MR. SMITH:

Q. Yes, I think it's 74.

MS. PERRY:

Q. If you could go down, Samantha, to Table 1.

MR. SMITH:

Q. Okay, so it's not quite what you're looking for. This just shows the executive compensation from 13 to 17 looks pretty flat, but it doesn't specifically breakout, I guess, the component for earnings which is what you were looking for.

JOHNSON, Q.C.:

Q. Right.

MR. SMITH:

Q. I don't know if that's in a RFI.

JOHNSON, Q.C.:

Q. I'm not aware that it is. I wonder if you could undertake to provide that information as well as the component that's provided for what's called the regulatory performance for each of those years as well.

KELLY, Q.C.:

Q. We'll check to see if it's already in an RFI and if not, we'll undertake to provide it.

MS. GLYNN:

Q. Noted for the record.

JOHNSON, Q.C.:

Q. Thank you. Mr. Chairman, I probably would turn to a fresh area, but it's a bit late. So, if you—with your indulgence –

MR. CHAIRMAN:

Q. Certainly.

Upon conclusion at 1:23 p.m.

CERTIFICATE

I, Judy Moss, do hereby certify that the foregoing is a true and correct transcript of a hearing in the matter of a General Rate Application by Newfoundland Power Inc. to establish customer electricity rates for 2016 and 2017 heard on the 30th day of March, 2016 at the Public Utilities Commission office, St. John's, Newfoundland and Labrador and was transcribed by me to the best of my ability by means of a sound apparatus.

Dated at St. John's, NL this
30th day of March, 2016

Judy Moss
Discoveries Unlimited Inc.

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